

6th Edition

CAF-03

Business Law Made Easy

Including ICAP Past Papers and Solution
Topic Wise (Autumn 2009-Autumn 2020)



FOR THE PROFESSIONAL STUDENT OF

- ICAP-CAF 03
- ICMAP
- MBA
- PIPFA
- ACCA
- Other Equivalent Courses

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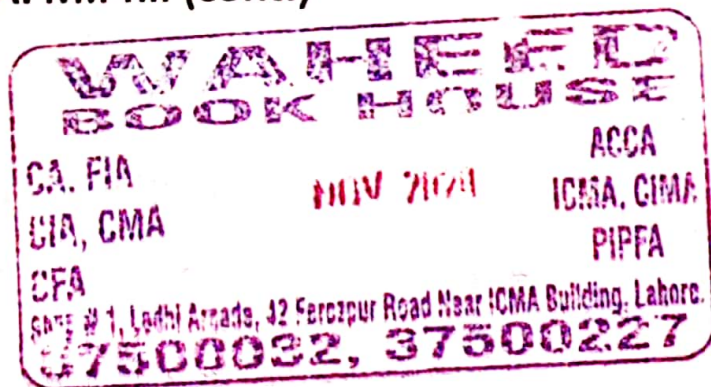
CAF-03 BUSINESS LAW

Business Law Made Easy

- - 6th Edition - -

*Including ICAP Past Papers and Solutions – Topic Wise
(Autumn 2009 – Spring 2020)
470 + Questions and Solutions*

Atif Abidi
ACA. M.Phil (cont.)



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Business Law Made Easy

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PREFACE

The Examinations of ICAP are a demanding test of student's ability to master the wide range of knowledge and skills required of the modern professionals. Subject of "Business Law (CAF-03)" is one of the efforts made by ICAP in this context for enhancing student's knowledge about detailed overview of the auditing standards.

The best and recommended source for this subject is the **official study text of the ICAP**. After the issuance of the said study text, it has been witnessed that ICAP is thoroughly following the text book in preparation of the exam and testing the competence of the students. Although the text book by ICAP covers all aspect of the syllabus in elaborative form; at times students are facing some issues in retaining the concepts given in any chapter, as the book is in the form of text blocks rather than bullets and key points.

For this purpose, there emerged a dire need to have some smart notes on the subject that covers the syllabus in the smartest way, emphasizing on the key points of law rather than explaining the concepts given therein. After some hectic efforts, we have been alhumdoLILLAH able to compile a (very first of its kind) book that shall be serving all the desired purposes i.e.

- Completeness of the Syllabus and the official text book by ICAP
- Smartness and easiness of the notes book
- Cross linked examples for proper understanding
- Availability of ICAP level exam questions for thorough practice

Now these notes contain all the topics of syllabus presented in bullets form making it easy to remember the key points (just like ICAP examiner wants). And these notes are arranged almost in same sequence as followed by "ICAP Text book" so that students may easily shift on the book for their revision without having fear of doing something new.

Students may also find this book useful while **final revision** of the subject, enabling them to revise in the minimum possible time.

***This book is not a substitute of ICAP Official Book !!!
(Rather it is to be used in conjunction with ICAP Official Book)***

Although reasonable efforts have been put to make the book free from majority of the errors, nevertheless absolute assurance is never possible due to inherent limitations in the process of compilations, interpretation and presentations of the book in easily understandable language.

So if you find anything missing or some spell, typo or other logical mistakes in these notes please mail us about such errors by referring to the chapter and page number at our mail id syedatifabidi@gmail.com or jz@canotes.net

*Primarily this book is designed, considering the needs and the syllabus of **CAF-03** paper of **ICAP**; however the comprehensiveness of this book makes it also relevant for equivalent papers of other qualifications such as **ACMA**, **CCS**, **CPA(Pak)**, **PIPFA** and **MBA** with a little or no divergence of the contents.*

Hope this book would inshaALLAH be serving you with its easy language, key point style, systematic pattern and an extensive question bank of approximately **470+ questions** from ICAP Past Papers (Chapter wise) along with ICAP recommended solutions.

May ALLAH bless all of you with success in every exam of both lives.

Please also remember us in your prayers

Talib e Dua !!!

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October 31st, 2020

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Syllabus Outline of Business Law – CAF 03

Mercantile Law

Introduction to legal system	Ch # 1	04-06
Contract Act, 1872	Ch # 2-8	20-30
Partnership Act, 1932	Ch # 9	10-15
Negotiable Instruments Act, 1881	Ch # 10	05-10
		50

Company Law

Preliminary and incorporation	Ch # 11, 12	05-10
Management administration and Disclosure of interest	Ch # 13, 14(C.O.B), 15	15-25
Investments, accounts and dividend etc.	Ch # 14 (Dividend), 16	10-20
Prospectus and Share Capital	Ch # 14 (remaining)	05-10
		50

Tutor's Note:

All the contents of the book (notes portion as well as question bank) have been revised to reflect the impact of change in contents of chapters and syllabus (with effect from Nov 2020)

Paper Pattern of Business Law – CAF 03

30 % Objective Types Questions (MCQs).

70% Subjective Type Questions (Written)

Knowledge based (40%); and

Application based (60%) based

having maximum weightage of 08 marks each question

Tutor's Note:

A very comprehensive practice of the MCQs (chapter wise) have been placed at a website portal www.test.canotes.net. Students can register their account with the website to do an unlimited practice of the MCQs [2000+ MCQs]. You can choose any chapter and any number of questions. You can practice randomly generated MCQs with automated checking and feedback immediately after your self-generated test. You can also see your stats & monitor performance

Business Law - Past Papers Analysis - Chapter Wise

	A.20	S.20	A.19	S.19	A.18	S.18	A.17	S.17	A.16	S.16	A.15	S.15	A.14	Total	%	Syllabus
Ch # 1 - Introduction to the Legal System	5	5	5	5	5	6	5	5	5	5	5	5	5	66	5%	4%-6%
Ch # 2 - Introduction to the law of Contract	7	3	0	2	5	0	4	0	0	4	3	3	0	31		
Ch # 3 - Lawful considerations and Objects and capacity of parties	1	6	0	0	0	0	0	4	9	0	0	0	0	20		
Ch # 4 - Free consent and Void agreements	4	0	7	0	4	0	3	2	9	5	0	0	12	46		
Ch # 5 - Performance of a contract	2	5	0	5	0	0	3	8	0	0	0	0	0	23		
Ch # 6 - Discharge of a contract and Remedies for breach of contract	8	4	0	2	7	4	5	0	0	8	8	7	0	53		
Ch # 7 - Specific types of contracts	2	2	8	10	9	11	3	11	0	8	14	7	3	88		
Ch # 8 - Agency	1	5	10	6	0	9	5	0	7	0	0	8	10	61		
	25	25	25	25	25	24	23	25	25	25	25	25	25	322	25%	20%-30%
Ch # 9 - Partnership Act	10	10	10	10	10	10	12	10	10	10	10	10	10	132	10%	10%-15%
Ch # 10 - Negotiable Instruments Act	10	10	10	10	10	10	10	10	10	10	10	10	10	130	10%	5%-10%
M.Law - Grand Total	50	50	50	50	50	50	50	50	50	50	50	50	50	650		
Ch # 11 - Introduction to Company and incorporation process	3	5	5	4	0	4	11	4	2	4	6	3	0	51		
Ch # 12 - Memorandum and articles	8	3	5	3	10	5	0	6	8	6	4	4	10	72		
	11	8	10	7	10	9	11	10	10	10	10	7	10	123	9%	5%-10%
Ch # 13 - Management	11	7	11	12	9	6	6	3	6	10	4	8	3	96		
Ch # 14 - (Commencement of business only)		0	0	2	0	0	0	7	0	0	0	0	7	16		
Ch # 15 - Meetings and Resolution	4	10	4	0	4	6	9	0	7	0	6	10	0	60		
	15	17	15	14	13	12	15	10	13	10	10	18	10	172	13%	15%-25%
Ch # 14 - (Dividend portion only)	5	0	0	0	7	5	0	6	0	0	10	0	5	38		
Ch # 16 - Accounts and Investment	10	8	7	10	0	5	6	4	7	10	0	5	5	77		
	15	8	7	10	7	10	6	10	7	10	10	5	10	115	9%	10%-20%
Ch # 14 - (Remaining Portion)	9	9	5	4	10	6	5	6	10	8	6	10	5	93	7%	5%-10%
Old Syllabus Areas (Not part of syllabus now)																
Audit Portion-		8	9	11	10	10	10	10	10	10	10	10	10	118		
Mortgages & Charges Portion			4	4		3	3	4		2	4		5	29		
	0	8	13	15	10	13	13	14	10	12	14	10	15	147	11%	
C.Law - Grand Total	50	50	50	50	50	50	50	50	50	50	50	50	50	650		
Business Law - Grand Total	100	100	100	100	100	100	100	100	100	100	100	100	100	1300		

Business Law - Past Papers Analysis - Chapter Wise

A.20	S.20	A.19	S.19	A.18	S.18	A.17	S.17	A.16	S.16	A.15	S.15	A.14	Total	%
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Super Important Chapters

Ch # 14 - Issue of Shares and Distribution of Profits

Ch # 9 - Partnership Act

Ch # 10 - Negotiable Instruments Act

Ch # 13 - Management

Ch # 7 - Specific types of contracts

14	9	5	6	17	11	5	19	10	8	16	10	17	147	13%
10	10	10	10	10	10	12	10	10	10	10	10	10	132	11%
10	10	10	10	10	10	10	10	10	10	10	10	10	130	11%
11	7	11	12	9	6	6	3	6	10	4	8	3	96	8%
2	2	8	10	9	11	3	11	0	8	14	7	3	88	8%
47	38	44	48	55	48	36	53	36	46	54	45	43	593	51%

Important Chapters

Ch # 16 - Accounts and Investment

Ch # 12 - Memorandum and articles

Ch # 1 - Introduction to the Legal System

Ch # 8 - Agency

Ch # 15 - Meetings and Resolution

10	8	7	10	0	5	6	4	7	10	0	5	5	77	7%
5	3	5	3	10	5	0	6	8	6	4	4	10	72	6%
5	5	5	5	5	6	5	5	5	5	5	5	5	66	6%
1	5	10	6	0	9	5	0	7	0	0	8	10	61	5%
4	10	4	0	4	6	9	0	7	0	6	10	0	60	5%
28	31	31	24	19	31	25	15	34	21	15	32	30	336	29%

81%

Slightly Less Important Chapters -

Ch # 6 - Discharge of a contract and Remedies for breach of contract

Ch # 11 - Introduction to Company and incorporation process

Ch # 4 - Free consent and Void agreements

Ch # 2 - Introduction to the law of Contract

Ch # 5 - Performance of a contract

Ch # 3 - Lawful considerations and Objects and capacity of parties

8	4	0	2	7	4	5	0	0	8	8	7	0	53	5%
3	5	5	4	0	4	11	4	2	4	6	3	0	51	4%
4	0	7	0	4	0	3	2	9	5	0	0	12	46	4%
7	3	0	2	5	0	4	0	0	4	3	3	0	31	3%
2	5	0	5	0	0	3	8	0	0	0	0	0	23	2%
1	6	0	0	0	0	0	4	9	0	0	0	0	20	2%
25	23	12	13	16	8	26	18	20	21	17	13	12	224	19%

Talib e doo

Syed Atif Hassan Abidi

Osama Waheed

25-Oct-20

Tutor's Note:

It is important to note that the revised syllabus and grid of chapter is applicable from Autumn 2020 and onwards therefore past papers trend can only identify the level of importance. But we can only relate latest attempt (Autumn 2020) with this syllabus and grid.

CH # 1**INTRODUCTION TO THE LEGAL SYSTEM****INTRODUCTION TO THE LAW AND ITS TYPES**

Law means a set of rules or a system of rules of conduct designed and enforced by the state to control and regulate the conduct of people.

Mercantile Law is part of civil law which deals with rights and obligations of persons dealing with each other. It includes laws relating to contracts, partnership, negotiable instruments etc.

Sources of law in Pakistan

- Legal system is derived from English common law (Equity)
- It is based on the Constitution of Pakistan 1973 as well as Islamic law (Sharia).

In Pakistan the main sources of law are following:

Legislation	▪ It includes the Act of Parliament, the Ordinance promulgated by President and the delegated legislations by different authorities
Precedent (case law)	▪ Precedents are judgments or decisions of a superior court which are binding on the subordinate courts.
Customs	▪ Certain customs, practices & beliefs are so vital and built-in part of a social and economic system that they are treated just like laws e.g. Sharia laws
Agreement	▪ Parties specify terms for themselves which constitute law for themselves.

Two major branches of the law are civil law and criminal law.

	Civil Law	Criminal Law
Description	<ul style="list-style-type: none"> ▪ Sets out rights and duties of persons as between themselves. ▪ Person whose rights are affected can claim remedy from wrongdoer ▪ A violation of the civil law is a tort (a wrongdoing), but is not a crime. 	<ul style="list-style-type: none"> ▪ Concerned with conduct that is considered so undesirable that State punishes persons disobeying. ▪ Legal action may be brought by the State against those individuals (and not private individuals)
Purpose	▪ Provide means where an injured party can obtain compensation	▪ Regulate the society by threat of punishment.
Harm caused	▪ The claimant sues the defendant for harm caused	▪ State (Government) prosecutes the accused (the defendant) whether or not harm was caused
Burden of proof	▪ If claimant can prove the wrong on balance of probabilities, defendant is held liable	▪ If state can prove offence beyond all reasonable doubt, the accused is found guilty & convicted

Remedy	<ul style="list-style-type: none"> • Civil court may order defendant to pay damages or other remedy like specific performance etc 	<ul style="list-style-type: none"> • Criminal court may sentence the defendant to fine or impose imprisonment or death sentence.
Some Examples	<ul style="list-style-type: none"> • Copyright disputes • Character defamation claim (Tort) • Disputes about an breach of contract (Contract Act) 	<ul style="list-style-type: none"> • Pakistan Penal Code • Anti-Money Laundering Act • Prevention of Electronics Crimes Act

Sometimes civil law and criminal law both are applicable. E.g. Suppose that a train company operates a train service, and there is a major accident involving loss of life and injury to passengers.

- The State may claim that the train company or its senior managers are guilty of a breach of the criminal law and bring a case in the criminal court.
- Individuals who have been injured in the crash and individuals who have lost a relative killed in the crash may bring civil actions against the train company, demanding compensation.

Basic Structure of Constitution of Islamic Republic of Pakistan

- Constitution was approved by the Parliament on April 10, 1973 and was ratified on August 14, 1973.
- Constitution is the supreme law and sets the governing principles of the country
- Parliament cannot make any laws which is against the Constitution.
- The Constitution contains preamble, 12 parts and 5 schedules as described below

Part	Articles	This Part includes
Preamble	-	<ul style="list-style-type: none"> • Objectives of the provisions of the Constitution. • Muslims will be enabled to live in accordance with teachings of Quran and Sunnah while provisions for minorities to practice their religion etc. • Guarantee for fundamental rights, safeguarding depressed classes, securing independence of judiciary, safeguarding sovereign rights.
I-Introductory	1-6	<ul style="list-style-type: none"> • Identification of country as Islamic Republic of Pakistan divided into 4 territories and defined the religion of state. • Elimination of all sorts of exploitation, rights of individuals to be dealt in accordance with law, loyalty to the state and abiding by the Constitution
II - Fundamental Rights and Principles of Policy	7-40	<ul style="list-style-type: none"> • Definition of State & laws regarding basic right and principles of policy • Safeguards regarding arrest and detention, prohibition of slavery, child labor & forced labor, right to do lawful profession and education • Policies like discouraging discrimination, providing free and compulsory education and developing friendly relations among all nations etc.

III – The Federation of Pakistan	41-100	<ul style="list-style-type: none"> ▪ Eligibility of President, term of office, powers, removal of President, job responsibilities and limitations. E.g. to follow advice of Cabinet etc. ▪ Composition, duration & meetings of Parliament, qualifications and disqualifications for membership. Introduction and passing of bills etc.
IV – Provinces	101-140A	<ul style="list-style-type: none"> ▪ Composition and function of the provincial governments and governor. ▪ Financial procedure such as Provincial Consolidated Fund and public account and procedure relating to budget statement and ordinances etc.
V – Relations between Federation and Provinces	141-159	<ul style="list-style-type: none"> ▪ Distribution of legal powers, admin relation between Federation and Provinces (e.g. inter-provincial trade etc) ▪ Special provisions relating to Council of common interests, National Economic Council, broadcasting & telecasting etc.
VI – Finance, Property, Contracts and Suits	160-174	<ul style="list-style-type: none"> ▪ Distribution of revenues between federation and provinces and other financial provisions such as exemption and imposition of certain taxes. ▪ Borrowing by Federal and Provincial government; appointment, powers & functions of Auditor General. ▪ Provisions regarding property, contracts, liabilities & suits
VII – The Judiciary	175-212	<ul style="list-style-type: none"> ▪ Establishments, jurisdictions and functions of courts (Supreme Court, High Courts and Federal Shariat Court), appointment of judges & other related general provisions.
VIII – Elections	213-226	<ul style="list-style-type: none"> ▪ Formation and duties of Chief Election Commissioner and Election Commissions along with electoral laws and conduct of elections.
IX – Islamic Provisions	227-231	<ul style="list-style-type: none"> ▪ Provisions relating to Holy Quran and Sunnah along with composition and functions of the Islamic Council.
X – Emergency Provisions	232-237	<ul style="list-style-type: none"> ▪ Declaration of emergency due to war or internal disturbance etc., power to suspend fundamental rights during emergency etc
XI – Amendment of Constitution	238-239	<ul style="list-style-type: none"> ▪ Amendment of Constitution by the Parliament through Constitution Amendment Bill.
XII – Miscellaneous	240-280	<ul style="list-style-type: none"> ▪ Establishment and constitution of Public Service Commission, command and functions of Armed Forces etc. ▪ Definition and administration of tribal areas; protection to President, Governor, Minister; national language etc.
1 st Schedule	-	<ul style="list-style-type: none"> ▪ Laws exempted from operation of Article 8
2 nd Schedule	-	<ul style="list-style-type: none"> ▪ Election of President
3 rd Schedule	-	<ul style="list-style-type: none"> ▪ Oaths of Office
4 th Schedule	-	<ul style="list-style-type: none"> ▪ Legislative Lists
5 th Schedule	-	<ul style="list-style-type: none"> ▪ Remuneration and Terms etc of Service of Judges

LEGISLATION

Governing Structure

- Pakistan has a Federal Parliamentary System of government
 - President as the Head of State; and
 - Elected Prime Minister as Head of Government.
- Federal Legislature is a bicameral Majlis-e-Shoora (Parliament), composed of the President, National Assembly (Lower House) and Senate (Upper House).

President

- President is considered a symbol of unity.
- President must be a Muslim.
- President is elected for 5 year by Senate, National Assembly and members of Provincial Assemblies.
- President is eligible for re-election, but cannot hold office for more than 2 consecutive terms.
- The majority party in the National Assembly usually nominates and elects President.
- President approves the statutes passed by National Assembly and thereafter by the Senate.
- He guides the Prime Minister in the matters of national importance.

Prime Minister

- Nominated and elected by a majority of members in the National Assembly.
- That individual is then appointed as Prime Minister by the President.
- The Prime Minister is assisted by Federal Cabinet.
~~(A council of ministers whose members are appointed by President on advice of Prime Minister)~~
- Federal Ministers are supported by secretaries and other government officers in each department
(for ensuring that policies formulated by the government are acted upon)

Senate

- Senate is permanent legislative body with equal representation from each of the 4 Provinces
- Representatives are elected by the members of their respective Provincial Assemblies.
- It promote national cohesion and harmony and gives smaller provinces equal representation
- There are also representatives from Islamabad Capital Territory
- Members are elected for a period of six years.
- Half members retire after 3 years and are replaced by equal number of newly elected.
- Election of all members is not held at same time, so Senate continues on a permanent basis.

- Chairman of Senate is next in line to act as President if office becomes vacant.
- The members elect from themselves a chairman and a Deputy Chairman.
- All statutes passed by National Assembly are also approved by Senate except money bills.

National Assembly

- Seats are determined on the basis of population of provinces.
- Members are elected for 5 years on the basis of direct votes by registered voters.
- There are also reserved seats for women and non-Muslims.
- The members elect from themselves Speaker, Deputy Speaker and Prime Minister.
- Most important function of the National Assembly is law making and formulation of policies.

Process of Legislation

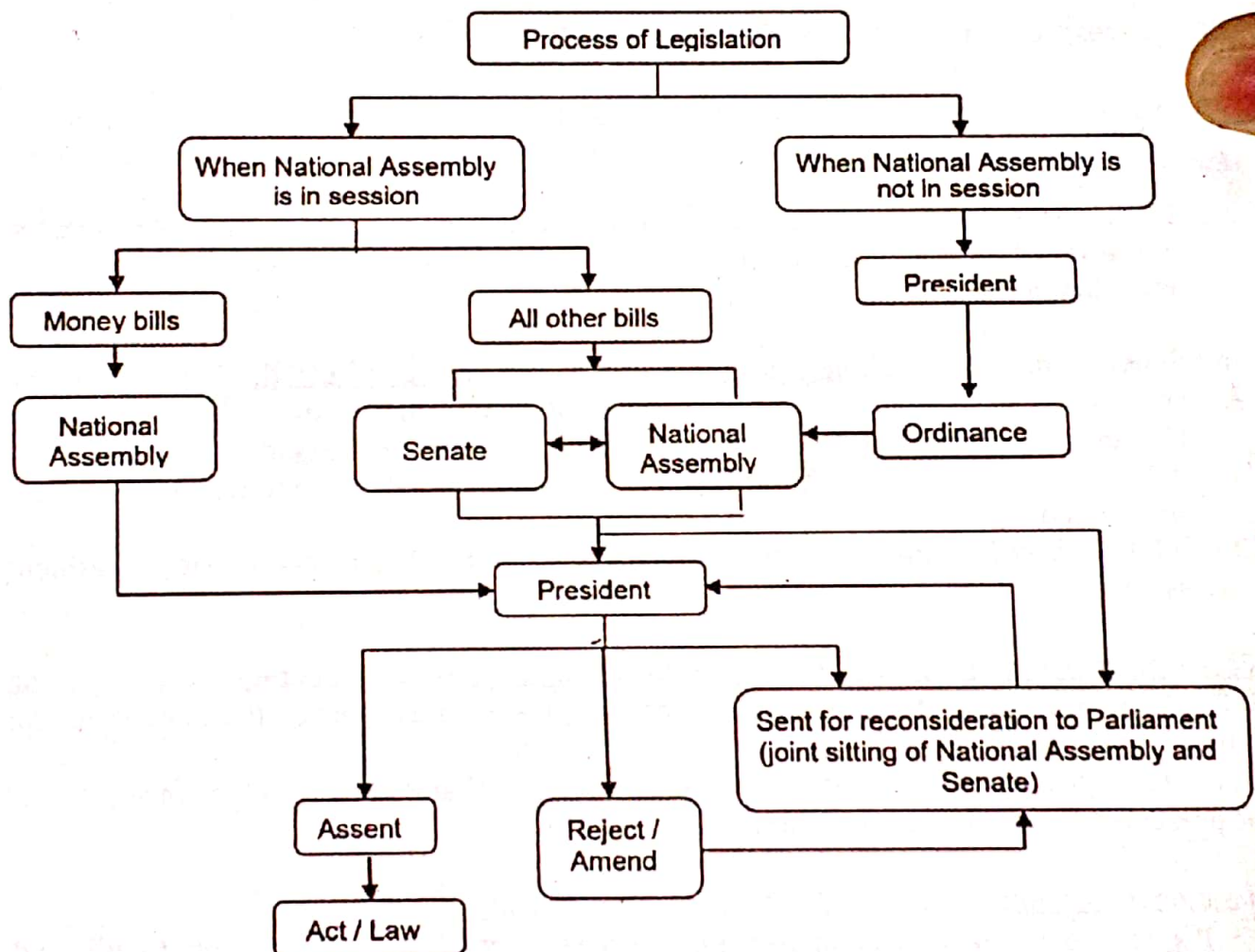
- A bill in respect of any matter may originate in either house.
- If it is passed by the house in which it is originated then it is transmitted to the other house
 - If bill is also passed by other house (without amendment), it is presented to President for assent.
 - If bill is passed with amendments it shall be sent back to the House in which it originated and if that House passes the Bill with those amendments it shall be presented to the President for assent.
- In following cases Bill shall be considered in the joint sitting of both the house (National Assembly and Senate) at the request of the house in which it originated
 - If a bill is rejected by the other house or not passed within 90 days; or
 - If bill sent to a House with amendments is not passed by that House with such amendments
- If that bill is passed by majority votes of members present it shall be presented to President for assent.
- President shall within 10 days approve the bill or return it to Parliament for reconsideration
- If President has returned a Bill to Parliament it shall be reconsidered by Parliament in Joint Sitting
- If it is again passed (with or without amendment) by Parliament by majority votes, It shall be presented to the President for assent.
- If National Assembly is dissolved before approval of a bill:
 - If a bill is pending in National Assembly or passed by it but pending in Senate; Bill shall lapse
 - If bill is pending in Senate not ~~passed~~ by National Assembly; Bill shall not lapse

Money bills

A money bill shall originate in the National Assembly and after it has been passed by the Assembly it shall (without being transmitted to the Senate) be presented to the President for assent.

The Ordinance

- When National Assembly is not in session, President if deems necessary has power to make Ordinance
- Such Ordinance shall have same force and effect as an Act of Parliament.
- The Ordinance shall stand repealed after 120 days if it is not presented or passed
 - By the National Assembly in case of Money Bill and
 - By both houses if it is other than Money Bill.



Delegated Legislation

- Power is given to an Executive (a minister or public body) to make legislation for specified purposes (e.g. SECP given the authority to prepare provisions for Companies Act 2017)
- Parliament has control over delegated legislation by restriction and defining power to make rules
- Such rules may be challenged in the courts on the grounds that it is ultra vires (i.e. it exceeds the prescribed limits) or has been made without due compliance.

Advantages of delegated legislation

- Parliament does not have **time** to examine matters in detail so that authority can give proper time
- Law is better worked out in **consultation** with professional and industrial groups outside Parliament.
- It is **more flexible** than an Act of Parliament. (i.e. simpler to amend than to emend an Act)

Disadvantages of delegated legislation

- It takes law making away from the democratically elected members.
- Law making power given to unelected civil servants etc working under supervision of minister.
- Such law making can become unmanageable (due to volume) and it is impossible to keep up-to-date

CH # 2**INTRODUCTION TO THE LAW OF CONTRACT**

Tutor's Note: Students are advised to just skim the contents of this unit because all the contents given therein would be repeated in sufficient details in the upcoming units and chapters

Definition of a contract**Contract**

An agreement enforceable by law is a contract.

Agreement

Every promise and every set of promises forming the consideration for each other is an agreement.

Promise

When the person to whom the proposal is made signifies his assent to it, the proposal is said to be accepted. A proposal, when accepted becomes a promise.

Proposal

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
- The person accepting the proposal is called the promisee.

Contract	=	Agreement	+	Enforceability
Contract	=	(Offer + Acceptance)	+	(Legal Obligation)

Essentials of a Valid Contract

- Offer and acceptance (Ch # 2)
- Legal relationship
- Competency of parties (Ch # 3)
- Consideration (Ch # 3)
- Free Consent (Ch # 4)
- Lawful Object (Ch # 3)
- Not declared as void (Ch # 4)
- Certainty
- Possibility of performance
- Legal formalities

Classifications of contract

As per Formation

- **Express contracts** A contract created by words i.e. verbally or in writing
- **Implied contract** A contract created by conduct of a person or the circumstances of a particular case
- **Quasi contract** An obligation imposed by law

As per Enforceability

- **Valid contract** An agreement which is enforceable by law
- **Void agreements** An agreement which is not enforceable by law
- **Void contract** A contract which ceases to be enforceable by law becomes void when it ceases to be enforceable
- **Voidable contract** An agreement which is enforceable by law at the option of aggrieved party
- **Illegal Agreement** An agreement the object of which is illegal
- **Unenforceable technical agreement** An agreement which is otherwise valid but due to some lacking, such as writing etc. remains unenforceable

As per Performance

- **Executed contract** When both parties have performed their respective promises
- **Executory contract** A contract in which something remains to be done
- **Unilateral contract**
A contract in which a promise on one side is exchanged for an act on the other side. In such contract one party to a contract has performed his part and performance is outstanding against the other party
- **Bilateral contract**
A contract in which a promise on one side is exchanged for a promise on the other

OFFER**Proposal / Offer**

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.

Essentials of an offer

- **Two persons**
 - The person making the proposal is called offeror
 - The person to whom offer is made is called offeree.
- **Certain and definite**
- **Contractual intention**

An offer must be made with an intention to create a contract.
- **Communication**
 - Offer must be communicated to offeree.
 - Communication is complete when it comes to the knowledge of offeree
 - If offer is made by post, its communication will complete when letter reaches offeree.
 - Offer can be made by words spoken or written or through conduct of the person.
- **Objective of consent**

Offer must be made with a view to obtain the consent of the other person
- **Conditional**
 - An offer may be subject to some condition.
 - It is on the sole discretion of offeree to either accept or reject it.
 - A conditional offer lapses when condition is not accepted.
- **Negative confirmation**

An offer cannot be in the form of negative confirmation
(i.e. if it's not accepted within specific time then it will be presumed to have been accepted)
- **Invitation of an offer¹**
 - An intention of a person to invite others with a view to enter into an agreement.
 - Purpose of such invitation is to circulate information of his readiness to do transaction
 - Such intentions are not considered offers.
- **Communication of special conditions**

If there are special terms in an offer, they must be specifically communicated to offeree.

Types of offer

Specific Offer²

- If an offer is made to definite or a particular person or specific group of persons
- Such offer can be accepted only by that definite person or that specific group of persons.

General offer³

- If an offer is made to the world or public than It is said to be general offer.
- Such offer can be accepted by any person.
- Contract is made with person who having the knowledge of offer comes forward and acts according to the conditions of the offer.

Cross offers⁴

- If 2 parties ignorant of each other's offer made similar offers to each other.
- Cross offers are not equal to acceptance.

Standing / Open / Continuing offer / Tender⁵

- If an offer is of on-going nature
- A contract is entered only when the person signifies his acceptance on the basis of tender.

ACCEPTANCE

Acceptance

When the person to whom the proposal is made signifies his assent to it, the proposal is said to be accepted

Essentials of acceptance

- **Absolute and unconditional**
 - An offer should be accepted without any condition.
 - If any condition is imposed on acceptance, then it would be called counter offer.
- **Communication**
 - Acceptance may be complete when it is communicated to the offeror.
 - An offer can be accepted by words spoken or written or through conduct of the person.
 - Acceptance is communicated either by offeree himself or any person authorized by him

By Post

- Communication is complete against proposer when it is put in course of transmission.
- Proposer becomes bound as soon as letter is posted (even if such letter is lost or delay)
- Communication is complete against acceptor when it comes to knowledge of proposer.
- Acceptor becomes bound when the letter of acceptance is actually received (before that acceptor may revoke his acceptance)

Contracts over telephone / telex / fax

- Treated on same principle as an oral agreement made between parties face to face
- Contract will complete only when acceptance is received by the proposer and not when it is transmitted by acceptor.

- **Reasonable time**
 - Acceptance should be within the time specified
 - Where no time is specified, acceptance should be within a reasonable time
- **Reasonable mode**
 - Acceptance should be made in the manner specified
 - Where no mode is specified, acceptance should be made in a usual manner.
 - If acceptance is not made in manner prescribed in proposal, offeror shall insist for that.
 - If he fail to insist within reasonable time it is deemed that he has accepted performance
- **Acceptor must be aware of the proposal at the time of acceptance**
- **Acceptance must be given before lapse of an offer**
- **Negative confirmation**

In cannot be in the form of negative confirmation
(i.e. if it's not accepted within specific time then it will be presumed to have been accepted)

REVOCATION OF OFFER AND ACCEPTANCE**Timing of revocation**

Timing of revocation of an offer - A proposal may be revoked at any time before acceptance or the communication of its acceptance is complete as against the proposer, but not afterwards.

Timing of revocation of an acceptance - An acceptance can be revoked at any time before the communication of the acceptance is complete as against the acceptor, but not afterwards.

Communication of revocation

As against the person who makes it
When it is put in a course of transmission.

As against the person to whom it is made
When it comes to the knowledge of the revokee.

Lapse of an offer

An offer is lapsed in following ways:

- Revocation before acceptance by the offeree
- Lapse of time
 - Lapse of time specified in the offer
 - Lapse of reasonable time (if no time is specified)
- Death or insanity of the offeror
(if fact of his death or insanity comes to the knowledge of the acceptor before acceptance)
- Non-fulfillment of condition precedent to the offer
- Counter offer is made
- Non-acceptance according to requirement of offeror
- Non-acceptance / Expressly Rejection by the offeree
- Subsequent illegality or destruction
(Offer comes to end if it becomes illegal or subject matter is destroyed before acceptance)

CH # 3**LAWFUL CONSIDERATION AND OBJECTS,
AND CAPACITY OF PARTIES****CONSIDERATION****Consideration⁶**

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

- When a party to an agreement promises to do something, he must get something in return.
- That return is consideration.
- Consideration may be following:
 - An act i.e. doing of something
 - An abstinence or forbearance i.e. abstaining or refraining from doing something.
 - A return promise

Essentials elements of consideration**Desire of the promisor⁷**

An act or abstinence must have been done or made at the desire or request of the promisor.

Move / from promisee or any other person⁸

In return consideration may be from promisee himself or by any other person (even stranger)

Consideration may be past, present or future

Past ⁹	Which has moved before formation of agreement (done or abstained from doing)
Present ¹⁰	Which moves simultaneously with the promise (does or abstains from doing)
Future ¹¹	Which moves after formation of agreement (promises to do or abstain from doing)

Consideration to have some value

Even it's not that much adequate. (not necessarily be equal in value to consideration received)

Consideration must be real¹²

The consideration must be real and not illusory¹³ (should be possible)

Something which the promisor is not already bound to do

Consideration must be something which the promisor is not already bound (because it adds nothing to the existing obligation)

Lawful¹⁴

The consideration must neither be unlawful nor opposed to public policy.

(even any one or any part of any one of several conditions for single object shall not be unlawful)

Agreements without consideration (following exceptions are not void)

Natural love and affection¹⁵	Agreements made on account of natural love and affection, if it is: <ul style="list-style-type: none"> ▪ Expressed in writing, ▪ Registered under the law, ▪ Made on account of natural love and affection, and ▪ Between parties standing in a near relation to each other.
Promise to compensate past voluntary services¹⁶	Such promise made is valid if: <ul style="list-style-type: none"> ▪ It is a promise to compensate and ▪ The person who is to be compensated has already done something voluntarily or has done something which the promisor was legally bound to do.
Time barred debt	A promise to pay time barred debt is enforceable if: <ul style="list-style-type: none"> ▪ It is made in writing, ▪ It is signed by the debtor or his agent, and ▪ It relates to a debt which could not be enforced by a creditor because of law of limitation.
Gifts¹⁷	Gifts which are accepted by the donee are called completed gifts and are valid
Charitable subscription	Where the promisee, on the faith of the promised subscription, makes commitments in continuance of any object and incurs liability ¹⁸
Contract of guarantee¹⁹	Consideration received by principal debtor is sufficient for the surety and it is not necessary to result in some benefit to the surety himself (Would be covered in detail in Ch # 7)
Contract of bailment²⁰	A consideration is not necessary for a contract of bailment i.e. gratuitous contract of bailment (Would be covered in detail in Ch # 7)
Contract of agency	A consideration is not necessary for a contract of agency (Would be covered in detail in Ch # 8)

Concept of Privity of contract

- Only parties to the contract may sue or may be sued under the contract.
- However, there are few exceptions (not examinable) to this rule, when a stranger to contract (non-party) may sue for enforcement of legal rights or obligations arising under the contract

LAWFUL / UNLAWFUL OBJECT AND CONSIDERATION

Legality of object and consideration

The consideration or object of an agreement is lawful unless:

- It is forbidden by law
- Is of such a nature that if permitted would defeat the provisions of any law
- It is fraudulent
- It involves an injury to the person or property of another
- The court regards it as immoral, or opposed to public policy

Forbidden by law²¹

If the law of state prohibits an object or consideration of an agreement, then such agreements are void. An act is forbidden by law when it is punishable by the law of the country.

The effects of such agreements are following:

- Collateral transactions to such agreement also become invalid and cannot be enforced.
- No action can be taken for the recovery of money paid or property transferred under such an agreement and for the breach of any such agreement.

Agreement, the consideration or object of which is partly unlawful

- If the illegal part cannot be separated than the whole agreement is illegal.
- If the illegal part can be separated than court will enforce the legal part and will reject illegal part.

Alternative promise being illegal²²

In the case of an alternative promise, one branch of which is legal and the other illegal, the legal branch alone can be enforced.

Agreements opposed to public policy

Trading with enemy	<ul style="list-style-type: none"> ▪ A person cannot enter into an agreement with an alien enemy during the period of war ▪ Contracts entered before the declaration of war are either suspended or terminated during the period of war.
Stifling prosecution²³	<ul style="list-style-type: none"> ▪ Criminals should be prosecuted and punished ▪ An agreement for stifling (relaxing) prosecution is illegal.
Sale of public offices	<ul style="list-style-type: none"> ▪ The agreements of sale of public offices are illegal as such agreements, if enforced, would led to inefficiency and corruption on public life. ▪ Similarly, an agreement to pay money to a public servant to induce him to act corruptly or to retire and thus make way for the appointment of promisor are also void.
Restraint of parental rights	<ul style="list-style-type: none"> ▪ An agreement which prevents a parent to exercise his right of guardianship is void. ▪ A father is entitled by law to the custody of his child. ▪ He cannot enter into an agreement which is inconsistent with his duties arising out of such custody.
Restraint of personal liberty	<ul style="list-style-type: none"> ▪ As Law generally allows all people's freedom to enter into any contract they please.
Agreement to create monopoly	<ul style="list-style-type: none"> ▪ An agreement to create monopoly is void ▪ This will impair consumer power and result in high prices for low quality of goods and services.
Marriage brokerage agreement	<ul style="list-style-type: none"> ▪ An agreement in which a person promises for reward to procure marriage for another is void (e.g. giving money to parents of bride or groom for their agreeing to the contract of marriage)

COMPETENT TO CONTRACT

Every person is competent to contract who is:

- of the age of **majority** according to the law to which he is subject, and
- of **sound mind**, and
- is **not disqualified** from contracting by any law to which he is subject.

Minor

In Pakistan a minor is a person who has not attained majority which is:

- 21 years where a guardian of a minor's person or property is appointed by the court of law under the Guardians and Wards Act, 1890; or
- 18 years in other cases.

Position of agreements by a minor

- An agreement with a minor is void.
- Where an infant / minor represents fraudulently or otherwise that he is of the age of majority and induces another to enter into a contract with him, he will not be liable
- An agreement with a minor cannot be ratified subsequently after he attains majority.
- If a minor enters into an agreement jointly with a major person then such agreement can be enforced against the major person who has jointly promised to perform.
- A minor cannot be a partner until he attains majority.
- A minor can be admitted for the benefits of partnership with the consent of all the partners.
- A minor can be agent but cannot be a principal but if anyone acts on behalf of minor principal, he will be personally liable.
- A minor cannot be declared insolvent because he is incompetent to contract.
- A minor can file a suit but cannot be sued.
- If parent of a minor entered into on behalf of a minor being within the scope of authority and for the benefit of minor, then such agreements can be enforced by or against the minor.
- A person who supplied necessities to a minor is entitled to be reimbursed from property of such minor. Such claim is against the property of the minor and not against the minor.

Tutor's Note:

Students are advised to only learn and understand point # 1,2,4 & 11 at this stage. All the other points would be covered in upcoming chapters (and need not be done here)

Unsound Mind

A person is said to be of sound mind for the purpose of making a contract

- if at the time when he makes it,
- he is capable to understand the terms of the contract,
- to form a rational judgment as to its effect upon his interests.

Position of agreements with a person of unsound mind

Specific persons/idiots

A person who is so mentally deficient by birth as to be incapable of ordinary reasoning or rational conduct is said to be a specific person

- An agreement with a specific person is void.

Lunatics

A person affected by lunacy (mental illness) is said to be 'lunatic'. A person can become lunatic at any stage of his life

- If a lunatic enters into a contract while he is of unsound mind, an agreement during this period is void.
- If a lunatic enters into a contract while he is of sound mind, an agreement during this period is valid.
- A person who is usually of unsound mind but occasionally of sound mind:
 - May make a contract when he is of sound mind²⁴
 - Burden of proof that he was of sound mind lies on the person who confirms it.

Delirious from fever or Drunken persons

- Cannot enter into a contract while such delirium or drunkenness lasts and he is not able to understand the terms of the contract or form a rational judgment.
- A person who is usually of sound mind but occasionally of unsound mind:
 - May not make a contract when he is of unsound mind²⁵
 - Burden of proof that he was of unsound mind lies on the person who questions the validity of contract.

General Rules

- A person of unsound mind can enforce a contract for his benefits
- A person who supplied necessities to a person of unsound mind or his defendant is entitled to be reimbursed from the property of such person of unsound mind. Such claim is against the property of the person of unsound mind not against the person personally.

Persons disqualified by law

Alien enemies	<ul style="list-style-type: none">▪ An alien is a person who is the citizen of a foreign country.▪ He can enter into a contract and be sued during peace time▪ If a war is declared than an alien enemy can neither enter into a contract or be sued during period of war.▪ Contracts entered before the declaration of war are either suspended or terminated during the period of war.
Foreign sovereigns and ambassadors	<ul style="list-style-type: none">▪ Such persons have immunity unless they choose to submit themselves to the jurisdictions of our courts.▪ They have a right to enter into a contract but can claim the privilege of not being sued.
Convicts	<ul style="list-style-type: none">▪ A convict while under imprisonment is incapable of contracting▪ Disability comes to end after expiry of sentence or when he is on parole.
Insolvent	<ul style="list-style-type: none">▪ An insolvent cannot enter into a contract (his property is dealt with by official assignee)
Companies	<ul style="list-style-type: none">▪ Contract entered into by a company will be valid only if it is within the powers granted to it by the MOA

CH # 4**FREE CONSENT AND VOID AGREEMENTS****Consent**

Two persons are said to consent when they agree upon the same thing in the same sense.

Free consent

The consent is said to be free when it is not caused by:

- Coercion or
- Undue influence or
- Fraud or
- Misrepresentation or
- Mistake

Effect of absence of free consent

- Contract becomes **voidable** at the option of the party whose consent was so caused if the consent is obtained by **coercion, undue influence, fraud or misrepresentation**
- If the consent is obtained by **mistake**, then agreement may be **void-ab-initio** or contract is not voidable depending upon the nature of the mistake.

COERCION**Coercion²⁶ is:**

- Committing or threatening to commit any act which is forbidden by Pakistan Penal Code; or
- Unlawful detaining or threatening to detain any property with an intention of causing any person to enter into an agreement

Coercion may be exercised from any person, and may be directed against any person, even a stranger²⁷

Effects of coercion²⁸

- Contract becomes voidable at the option of the party whose consent was so caused.
- The burden of proof lies on the party who rescind (cancel) the contract.
- The party rescinding a voidable contract shall restore any benefit (if he has received any benefit from another party).
- A person to whom money has been paid or anything delivered by coercion must repay or return it.

UNDUE INFLUENCE

Undue influence²⁹

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 unfair advantage over the other.

Nature of relationship

A person is in a position to dominate the will of another where he:

- Holds the real or apparent authority over the other (e.g. parent and child)
- Stands in a fiduciary relation to the other (e.g. already indebted); or
- Makes a contract with a person whose mental capacity is temporarily or permanently affected by reason of age, illness or mental or bodily distress (e.g. attendant and patient)

In following relationships it is presumed that a person is in a position to dominate other's will:

- | | | |
|-----------------------|-------------------------|----------------------|
| ▪ Father & son | ▪ Trustee & beneficiary | ▪ Solicitor & client |
| ▪ Guardian & ward | ▪ Teacher & student | ▪ Fiance & fiancée |
| ▪ Employer & Employee | ▪ Doctor & patient | ▪ Pardanasheen lady |

In the following relationship there is no such presumption of dominating other's will:

- Landlord and tenant
- Creditor and debtor
- Husband and wife (non parda observing)
- Principal and Agent

Rebutting presumption

The presumption of undue influence can be rebutted by showing that the:

- Dominant party has made full disclosure of all facts to weaker party before making contract
- Price was adequate
- Weaker party was in receipt of competent independence advice before entering contract.

Effect of undue influence

- The contract becomes voidable at the option of the party whose consent was so caused.
- Burden of proof is on the party who was in a position to dominate the will of other party
- Contract may be set aside either absolutely or, if the party who was entitled to avoid it has received any benefit, upon such terms and conditions as to Court may seem just.

Difference between coercion and undue influence

Factor	Coercion	Undue influence
Consent obtained by	Giving a threat of an offence or committing an offence.	Dominating the will.
Nature of pressure	Physical pressure.	Moral pressure.
Relationship	Parties may or may not be related.	Parties are related to each in some way
Objective	To compel person to do contract	To obtain an unfair advantage.
Criminal liability	Criminal liability is incurred. (therefore it is illegal)	Criminal liability is not incurred.
On whom	Coercion may be employed on a person other than a party whose consent is desired (e.g. his son)	Undue influence may only be employed on the party whose consent is desired.
By whom	It can be exercised by a stranger to the contract.	It can only be exercised by a party to the contract and not by a stranger.
Onus of proof	On the party on whom coercion was exercised	On the party in a position to dominate the will of the other party.
Restoration of benefit	The aggrieved party has to restore the benefit received.	The party avoiding the contract may or may not restore benefit.

FRAUD

"Fraud" means and includes any of the following acts committed by a party to a contract, or with his connivance, or by his agents, with intent to deceive another party thereto his agent, or to induce him to enter into the contract;

- 1) the suggestion as a fact, of that which is not true, by one who does not believe it to be true;
(false assertion)³⁰
- 2) the active concealment of a fact by one having knowledge or belief of the fact;³¹
- 3) a promise made without any intention of performing it (empty promise);³²
- 4) any other act fitted to deceive;
- 5) any such act or omission as the law specially declares to be fraudulent.

Essentials of fraud

Party to a contract	<ul style="list-style-type: none"> Fraud must be committed by a party to a contract or by anyone with his involvement or by his agent.
False representation	<ul style="list-style-type: none"> Means that false representation is made with knowledge of its falsehood. It will equal to fraud if a true representation is made but becomes untrue at the time of formation of contract the fact is known to the party who made the representation.
Representation as to fact	<ul style="list-style-type: none"> A mere opinion does not amount to fraud. A representation must relate to a fact than it amount to fraud.
Actually deceived	<ul style="list-style-type: none"> Fraud must have actually deceived the other party who has acted on the basis of such representation.
Suffered loss	<ul style="list-style-type: none"> Loss has been suffered by the party who acted on the representation.

Effects of fraud

- Contract becomes voidable at the option of the party whose consent was so caused.
- Party whose consent was so caused may insist on performance of the contract.
- Party whose consent was so caused is entitled to claim damages.

Exceptions to rescind the contract

A party cannot rescind the contract where:

- Silence amounts to fraud and the aggrieved party had the means of discovering the truth with ordinary diligence
- The party gave the consent in ignorance of fraud
- The party after becoming aware of the fraud takes a benefit under the contract
- An innocent third party before the contract is rescinded acquires for consideration and in good faith some interest in the property passing under the contract,
- The parties cannot be restored to their original position.

Silence as to fraud

Mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud³³, unless

- the circumstances of the case are such that parties stands in fiduciary relationship³⁴; or
- where silence itself is equivalent to speech³⁵.

Note: In the early 80's the Federal Shariat Court decided that provision regarding position of silence in Contract Act is not in conformity with the teachings of Islam.

MISREPRESENTATION

Misrepresentation means and includes-

1) Unwarranted statement

When a person makes a positive statement that a fact is true when his information does not warrant it to be so, though he believes it to be true.

2) Breach of duty

Any breach of duty which, without an 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;

3) Inducing mistake about subject matter (Innocent misrepresentation)

A party to an agreement induces (however innocently) the other party to make a mistake as to the nature or quality of the subject of the agreement.

Essentials of misrepresentation

Party to a contract	▪ The representation must be made by a party to a contract or by anyone with his involvement or by his agent.
False representation	▪ Means that false representation is made <u>without knowledge</u> of its falsehood.
Representation as to fact	▪ A mere opinion does not amount to misrepresentation. ▪ Representation must relate to a fact than it amount to misrepresentation.
Object	▪ Objective is to induce other party to enter into contract without intention of deceiving the other party.
Actually acted	▪ The other party must have acted on the faith of the representation

Effects of misrepresentation

- Contract becomes voidable at the option of the party whose consent was so caused.
- The party whose consent was so caused may insist on performance of the contract.

A party cannot rescind the contract where:

- Party whose consent was caused had means of discovering truth with ordinary diligence;
- Party gave the consent in ignorance of misrepresentation
- Party after becoming aware of the misrepresentation takes a benefit under the contract
- An innocent 3rd party before the contract is rescinded acquires for consideration and in good faith some interest in the property passing under the contract,
- Parties cannot be restored to their original position.

MISTAKE

Mistake

Where both the parties to an agreement are under a mistake as to matters of facts essential to the agreement, the agreement is void.

Types of mistakes

Mistake of Law:

Mistake of Pakistan law

Contract is not void / voidable if it was caused by mistake as to any law in force in Pakistan. (Ignorance of Law is not an excuse)

Mistake of foreign law

A mistake as to the law not in force in Pakistan has same effect as a mistake of fact i.e. void.

Mistake of Fact:

Bilateral mistake³⁶

Where both the parties to an agreement are under a mistake as to a matter of facts essential to the agreement, the agreement is void.

Bilateral mistake as to the subject matter includes mistake as to the

- Existence of subject matter³⁷
- Quantity of subject matter³⁸
- Quality of subject matter³⁹
- Price of subject matter⁴⁰
- Identity of subject matter⁴¹
- Title of subject matter⁴²

Bilateral mistake as to the possibility of performance

Where parties believe that agreement is capable of performance and actually it is not

Unilateral mistake⁴³

Contract is not void / voidable merely because it was caused by one of the parties to it being under a mistake as to matter of facts (except under Fraud or Misrepresentation)

Following are the exceptions where agreement is void on the basis of unilateral mistake:

- Mistake relating to the identity of the person⁴⁴
- Mistake relating to the nature of the contract⁴⁵

EXPRESSLY DECLARED VOID AGREEMENTS

An agreement not enforceable by law is said to be **void**.

The agreements which are not enforceable by law right from the time when they are made are called **void-ab-initio**.

When an agreement is void, other agreement which is collateral to it is also void and is not enforceable by law if the other party has knowledge about it

Expressly declared void agreements

- 1) Agreements in restraint of trade
- 2) Wagering agreement
- 3) Agreements in restraint of legal proceedings
- 4) Agreements in restraint of marriage
 - Every agreement in restraint of the marriage of any person other than a minor is void.
 - Law regards marriage and married status as the right of every individual.
- 5) Uncertain agreements
(An agreement the meaning of which is not certain or capable of being made certain)
- 6) Agreements contingent on impossible events
(whether impossibility of event is known or not to the parties at the time when it is made)
- 7) Agreements to do impossible acts
- 8) Agreement to enter into an agreement in future

AGREEMENTS IN RESTRAINT OF TRADE⁴⁶

Every agreement by which anyone is restricted from exercising a lawful profession, trade or business of any kind, is to that extent void.

Exceptions of agreements in restraint of trade

- 1) Sale of goodwill
Seller may agree with the buyer to refrain from carrying on a similar business within specified reasonable local limits

2) Partner's agreements

Partnership Act allows following agreements as an exception to this rule:

- Carrying on same business (competing with that of firm) by an **existing partner**
- An **outgoing partner** may agree that he will not carry on any business similar to that of the firm for a specified period and for specified local limits.
- Partners may, upon **dissolution of firm**, make an agreement that some or all of them will not carry on a business similar to firm for a specified period and for specified local limits.
- Partner(s) may upon **sale of the goodwill of a firm**, make an agreement that they will not carry on any business similar to firm for a specified period and for specified local limits.

3) Trade combinations⁴⁷

An agreement between different firms in the nature of a trade combination in order to maintain a price level and avoid under selling is not void.

4) Service Agreements⁴⁸

A clause in service agreement by which an employer restricts the employee not to compete with employer or accepting any other employment is not restraint of trade. If legitimate interest or goodwill or trade secret of employer is involved an employer may restrict his employee even after end of employment (restriction should be just & reasonable)

Wagering agreement⁴⁹

Agreement between two persons under which money or money's worth is payable, by one person to another on happening or non-happening of a **future uncertain event**.

- Such agreements are void
- No suit can be filed to recover the amount won on any wager.

Transactions which are not held wagers

- Prize competitions which are games of skill (e.g. picture puzzles, athletic competitions)
- Agreement to contribute to a plate or prize of the value of Rs. 500 and above to be awarded to the winner of a horse race.
- If there is intention of actually receiving and delivering goods (or shares) at a future date (but If only price difference is to be paid, this is wagering agreement)
- Contract of insurance

Agreements in restraint of legal proceedings

Every agreement by which any party is restricted from enforcing his right under a contract by the usual legal proceedings or which limits the time within which he may enforce his right

Exceptions

- An agreement between persons who agree that any dispute shall be referred to arbitration.
- An agreement whereby parties agree not to file an appeal in upper court of law.
- Parties selecting one court of law between two courts equally competent.

CH # 5:**PERFORMANCE OF A CONTRACT****PERFORMANCE OF A CONTRACT**

A contract is said to have been performed when the parties to a contract either perform or offer to perform their respective promises.

The parties to a contract must either perform, or offer to perform their respective promises (unless it is dispensed with or excused under the provisions of this Act, or of any other law)

| Types of performance**Actual performance⁵⁰**

When the promisor has made the performance in accordance with the terms of the contract and is accepted by the promisee it is called an actual performance.

Attempted performance⁵¹

When promisor has made an offer of performance but the offer of performance of promisor is not accepted by the promisee. Attempted performance is also known as tender.

| Types of tender

There can be two types of tender as follows:

1) Tender of goods or services

Where promisor offers to deliver the goods or services but the promisee refuses to accept.

Effects

- Goods or services need not be offered again.
- Promisor may sue the promisee for non-performance and claim damages.
- Promisor is discharged from his liability i.e. he is not liable for non-performance.

2) Tender of money

Where promisor offers to pay the amount but the promisee refuses to accept the same.

Effects

- Promisor is not discharged from his liability to pay the amount
- Promisor will not be liable for interest from the date of a valid tender

Essentials of a valid tender

Unconditional	▪ When it is made in accordance with the terms of the contract.
Proper Time	▪ Tender must be made at the stipulated time or during business hours. ▪ Tender of goods or money before the due date is also not a valid tender
Proper Place	▪ Tender must be made at the stipulated place or at business place
Proper Person	▪ It must be made to the promisee or his duly authorized agent. ▪ In case of several joint promisees, a tender made to one of them has the same legal consequences as tender to all of them
Reasonable Opportunity	▪ Promisee must have reasonable opportunity for examining that the goods offered are the same as per the terms of the contract
Whole Obligation	▪ A valid tender is for the whole obligation. ▪ However, minor deviation from contract terms may not render it invalid
Fixed amount & legal tender	▪ In case of tender of money the amount must be fixed and in legal tender

Effect of refusal to perform

When any party has refused to perform or disabled himself from performing his promise completely, promisee may put an end to the contract (unless he has signified (express or implied) his willingness in its continuance)

Who can perform and who can demand performance**Persons who can perform**

Promisor ⁵²	If a contract is of personal nature or it was agreed that promise will be performed by promisor himself.
Promisor's agent ⁵³	If intention of parties is that the promise can either be performed by the promisor himself or any person employed by him
Legal representatives ⁵⁴	On death of promisor (unless contrary intention appears or contract is of personal nature)
Third party	With consent of promisee a contract can be performed by a 3 rd party. (after acceptance, from 3 rd person, he cannot enforce it against promisor)
Joint promisor (devolution of joint rights) ⁵⁵	Unless contrary intention appears, in case of several promisors the following persons must perform the promise: <ul style="list-style-type: none"> ▪ All the promisors jointly (if all are alive) ▪ Representatives of deceased promisor jointly with surviving promisor(s) (in case of death of any of the joint promisors) ▪ Representatives of all of them jointly (death of all joint promisors)

Persons who can demand performance

- Promisee⁵⁶
- Promisee's agent:
- Legal representative⁵⁷
- Third party
(In some exceptional cases like beneficiary in case of trust etc)
- Joint promises⁵⁸
(same rules as provided above)

Rules regarding the performance of joint promise

Joint and several liability of joint promisors⁵⁹

Promisee may compel anyone or more of such joint promisors to perform the whole promise.

Right to claim contribution⁶⁰

Each of two or more joint promisors may compel every other joint promisor to contribute equally with himself to the performance of the promise (unless a contrary is agreed)

Sharing of loss in contribution⁶¹

If anyone of two or more joint promisors makes default in such contribution, the remaining joint promisors must bear the loss arising from such default in equal shares.

Release of one joint promisor by the promisee⁶²

- It does not discharge the other joint promisor or joint promisors
- It does not free the joint promisor so released from responsibility to other joint promisors

Time and place of performance

Time for performance is not specified	Contract must be performed within a reasonable time
Time for performance is specified	Contract must be performed on that day during usual hours of business and at a place where the promise ought to be performed.
Place for performance is specified	Promisee must apply for performance at a proper place and within usual hours of business.
Place for performance is not specified	Promisor must apply to the promisee to appoint a reasonable place.
Promisee prescribes ⁶³ manner or time	Promise must be performed in the manner and at time prescribed

Time as essence of contract

Time is essence of a contract means that it is necessary for the parties to a contract to perform their respective promises within the specified time.

Cases where time is essence

In the following cases, time is usually considered to be the essence of contract:

- Where the parties have expressly agreed to treat the time as the essence of the contract.
- Where the non-performance at the specified time operates as an injury to the party.
- Where the nature and necessity of the contract requires the performance of the contract within the specified time.

Consequences of breach

Time is essence ⁶⁴	Time is not essence
<ul style="list-style-type: none"> ▪ Voidable at the option of promisee ▪ Where performance beyond the stipulated time is not accepted, promisee entitled to claim compensation for any loss due to non-performance of at agreed time ▪ Where performance beyond stipulated time is accepted, promisee is not entitled to claim the compensation for any loss due to non-performance at agreed time, unless promisee gives notice to promisor of his intention to claim damages 	<ul style="list-style-type: none"> ▪ Not Voidable at the option of promisee ▪ Where performance beyond stipulated time is accepted, promisee is not entitled to claim the compensation for any loss due to non-performance at agreed time, unless promisee gives notice to promisor of his intention to claim damages

RECIPROCAL PROMISES

The Promises which form the consideration or part of the consideration for each other.⁶⁵

Types of reciprocal promises

Mutual and independent

When the promises are to be performed by each party independently (without waiting for the other party to perform)

Mutual and dependent

When the performance of one party depends on the prior performance of the other party

Mutual and concurrent

When the promises are to be performed simultaneously i.e. at the same time

Rules regarding performance of reciprocal promises

Simultaneous performance⁶⁶

When contract consists of reciprocal promises to be simultaneously performed, promisor need not perform his promise unless promisee is ready and willing to perform his promise

Order of performance⁶⁷

- Where order in which reciprocal promises are to be performed is expressly fixed by the contract, they must be performed in that order
- If not fixed, they must be performed in the order which the nature of transaction requires

Preventing the performance⁶⁸

When one party prevents the other from performing his promise, contract becomes voidable at the option of the party so prevented; and he is entitled to compensation from other party for any loss which he may sustain in consequence of the non-performance of the contract.

Non-performance in case of mutual and dependent reciprocal promises⁶⁹

Where the party who is liable to perform first, fails to perform it, then such party cannot claim the performance from the other party and must make compensation to the other party for any loss which the other party may sustain by the non-performance of the contract.

Promise to do legal and illegal things⁷⁰

Where persons reciprocally promise, firstly, to do certain legal things, and secondly, to do certain illegal things, the first set of promises is a contract, but the second is a void agreement.

APPROPRIATION OF PAYMENT

Appropriation of payment means allocation of payment to a particular debt.

Rules regarding appropriation of payment

Debt to be discharged is indicated⁷¹

The payment, if accepted must be applied accordingly.

Debt to be discharged is not indicated

The creditor has option to apply the payment to any lawful debt due from the debtor (even if it is a time barred debt; but he cannot apply to a disputed debt)

Neither party makes an appropriation

Payment shall be applied in discharge of debts in order of time, whether or not they are time barred. If debts are of equal standing, payment be applied in discharge of each proportionately

If principal and markup both are due, then mark-up is settled first and then principal is settled.

ASSIGNMENT OF CONTRACTS

Assignment of a contract means transfer of contractual rights and liabilities to a third party.

1) Assignment by act of parties

When the parties to a contract themselves make the assignment.

- Contractual obligation/right involving personal skill or ability cannot be assigned.
- If contract expressly/impliedly provides that it shall be performed by the promisor only, then it cannot be assigned
- If contract does not expressly/impliedly provide that it shall be performed by promisor only, then promisor or his representative may employ a competent person to perform it (promisor still remains liable to the promisee for proper performance)
- By Novation, promisor may transfer his liability to third party with consent of all parties.
- Actionable claims (i.e. claim to any debt or to any beneficial interest in movable property) can always be assigned by an instrument in writing⁷².
(Notice of such assignment is also required to be given by the debtor)

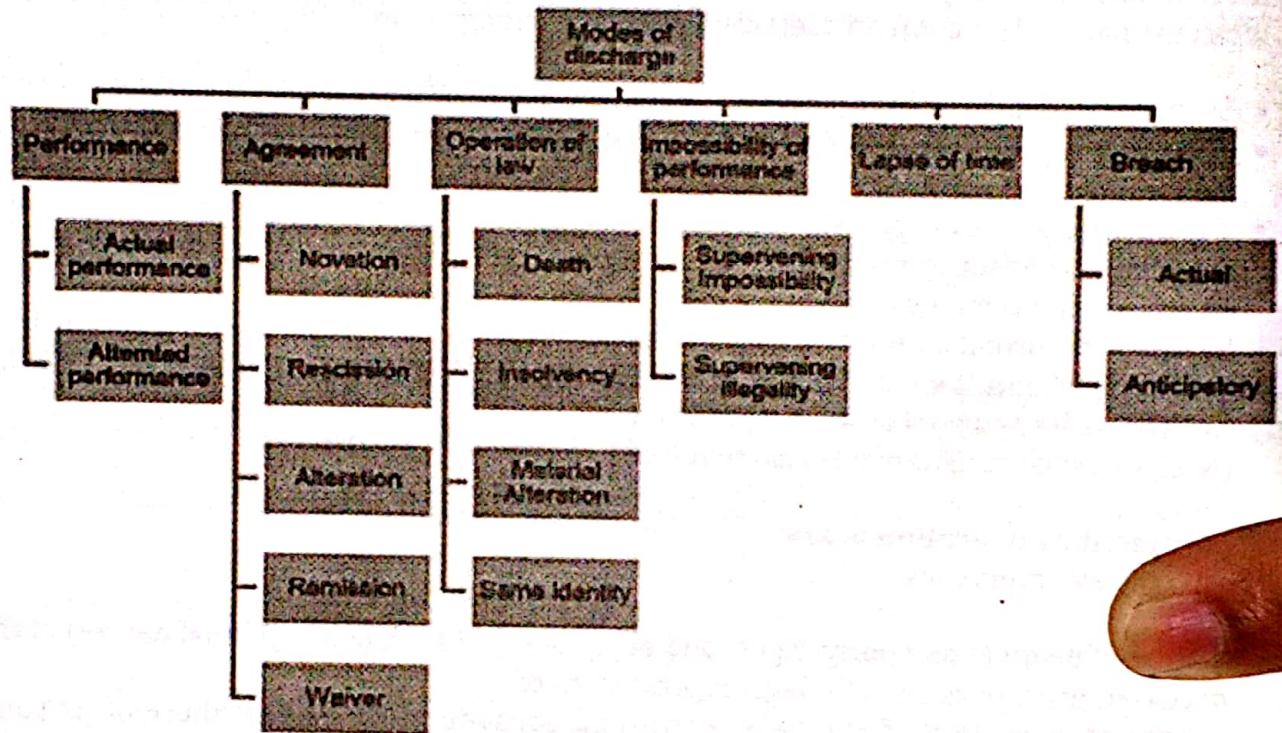
2) Assignment by operation of law

When the law intervenes

- In case of death of any party, rights and obligation (other than of personal nature) of the deceased party pass on to his legal representatives.
- In case of insolvency of any party, rights and obligations (other than those of personal nature) of the insolvent party pass on to the Official Receiver or Assignee.

CH # 6**DISCHARGE OF A CONTRACT AND REMEDIES FOR BREACH OF CONTRACT**

A contract is said to be discharged when contractual relations between the parties to a contract are terminated or comes to an end.

**Discharge by Performance**

A contract can be discharged by performance in any of the following ways:

Actual performance⁷³

If the parties to the contract perform their respective promises in accordance with the terms of the contract

Attempted performance⁷⁴

If the promisor has made an offer of performance as per the terms of the contract and the promisee refuses to accept the offer of performance.

- It is also known as tender.
- It is equivalent to actual performance.
- Contract is deemed to be performed.
- Promisor is discharged from his liability of non-performance.
- His rights against the promise are unaffected.

Discharge by Agreement or Consent

Novation ⁷⁵	Substitution of a new contract for an old one. <ul style="list-style-type: none"> It can be either between same parties or different parties In case of a new party, original debtor is totally released from the obligation, which is transferred to someone else.
Rescission	Cancellation of a contract by mutual agreement of parties
Alteration ⁷⁶	A variation made in language or terms of a contract with mutual agreement.
Remission	Accepting a less amount than the initial amount agreed
Waiver ⁷⁷	A unilateral act of one person that results in the surrender of a legal right.
Promisee's refusal neglect	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. <i>Tutor's Note: Logically this area doesn't belong here, it should be classified under attempted performance</i>

Discharge by Operation of Law

Death ⁷⁸	<ul style="list-style-type: none"> Contract involving personal skill or ability is discharged. In other contracts, rights and liabilities of the deceased person pass on to his legal representatives.
Insolvency ⁷⁹	<p>If a person's debts exceed his assets, he is adjudged insolvent and his property stands vested in Official Receiver or Official Assignee appointed by court</p> <ul style="list-style-type: none"> He cannot make contracts relating to his property, sue or be sued. On declaration as insolvent, he is discharged from his previous liabilities.
Material Alteration ⁸⁰	<p>If terms of contract are materially altered without prior consent of parties. A material alteration is one which changes following in a significant manner:</p> <ul style="list-style-type: none"> Legal identity or the character of the contract; or Rights and liabilities of the parties to the contract
Same identity ⁸¹	When the promisor becomes the promisee, the other parties are discharged (e.g. negotiation back in case of negotiable instrument i.e. creditor to himself)

Discharge by Lapse of Time

If a contract is not performed within the period of limitation, then it is discharged as the parties cannot legally enforce their rights.

After the expiry of the limitation period, the debt becomes time barred and hence cannot be recovered through court of law.

Discharge by Impossibility of Performance

1) Supervening impossibility

When contract is valid at time of formation and becomes impossible to perform subsequently

- Contract becomes void when an act becomes impossible after the formation of the contract (and is beyond the control of promisor)
- If promisor hides the impossibility, he is liable to compensate the promisee.
- Every person is bound to restore any benefit received or compensated earlier

Grounds of supervening impossibility

- If **subject matter is destroyed**⁸² after formation of contract without fault of either party.
- **Death or personal incapacity**⁸³ (doctrine of frustration) in contracts of personal nature
- On **declaration of war**⁸⁴ contracts with alien enemies are suspended or declared void.
- If that particular state of thing which forms basis of a contract **ceases to exist or occur**.⁸⁵

A contract is **not discharged by the supervening impossibility** in the following cases:

- If the **performance of a contract becomes difficult**⁸⁶, more costly or less beneficial than that agreed at the time of its formation
- When the contract becomes **commercially unviable**⁸⁷ or non-profitable
- On **default of a third party**⁸⁸, on whose work the promisor is relying
- Unless otherwise agreed by the parties to the contract, a contract is not discharged on the grounds of **strikes, lockouts and civil disturbances**.⁸⁹
- **Partial impossibility** of some of the objects of the contract.

2) Supervening illegality⁹⁰

If the performance of the contract becomes unlawful due to a change in the law after the formation of the contract, then the contract is said to be discharged.

DISCHARGE BY BREACH

If a party refuses or fails to perform his part of the contract, then the contract is said to be discharged due to breach. A breach of contract may be actual or anticipatory.

Actual breach of contract

When a party to a contract refuses or fails to perform his part of the contract at the time fixed for performance. Actual breach of contract can occur:

- On due date of performance⁹¹; or
- During the course of performance⁹²

Consequences of actual breach

Consequences depend upon whether the time was the essence of the contract or not.

Time is essence ⁹²	Time is not essence
<ul style="list-style-type: none"> ▪ Voidable at the option of promisee ▪ Promisee entitled to claim compensation for any loss due to non-performance of at agreed time where performance beyond the stipulated time is not accepted ▪ Promisee is not entitled to claim the compensation for any loss due to non-performance at agreed time where performance beyond stipulated time is accepted, unless promisee gives notice to promisor of his intention to claim damages 	<ul style="list-style-type: none"> ▪ Not Voidable at the option of promisee ▪ Promisee is not entitled to claim the compensation for any loss due to non-performance at agreed time where performance beyond stipulated time is accepted, unless promisee gives notice to promisor of his intention to claim damages

Anticipatory breach of contract

When before the performance is due, the party acts in a way that the contract may not be performed. A party may be intended not to perform the contract in the following two ways:

- When a party to a contract has refused to perform his promise before due date
- When a party to a contract has disabled himself from performing his promise in total.

Options to the aggrieved party	Damages will be equal to the
Rescind the contract and claim damages for breach of contract without waiting until the due date for performance; or	Difference between the price prevailing on the date of breach and the contract price.
Treat the contract as operative and wait till due date for performance and claim damages if the promise still remains unperformed	Difference between the price prevailing on the due date of performance and the contract price.

Consequences of treating contract as operative⁹³

- Promisor may perform his promise on or before due date of performance (promisee will be bound to accept the performance)
- Promisor may take advantage of discharge by supervening impossibility arising between the date of breach and the due date of the performance (Promisee shall lose his right to sue for damages)

REMEDIES FOR BREACH OF CONTRACT

A remedy can be defined as a manner in which a right is enforced or satisfied by a court when some harm or injury, recognized by society as a wrongful act, is inflicted upon an individual.

Types of remedy

Common law remedies

- Damages and action for price are common law remedies (more frequently used).
- Object is not to punish the party at fault but to compensate aggrieved party (financial loss).

Equitable remedies

- The court ordered action that directs parties to do or not to do something.
- Only appropriate in specialised circumstances
(e.g. where monetary damages would be inadequate compensation for the breach)
- Examples are specific performance and injunction.

Quantum meruit claim

- Categorized as a claim in quasi contract.
- The aim of this award is based on an implied agreement to pay for what has been done.
- It is likely to be used where one party has already performed part of his obligations and the other party then repudiates the contract.
- If injured treat contract as terminated, he may claim a reasonable amount for work done.

Remedies for breach

1) Rescission of contract

- Putting an end to a contract.
- A right not to perform your obligation
- Aggrieved party is discharged from all the obligations under the contract and is entitled to claim compensation for the damage which he has sustained because of non-performance.
- Court may allow rescission where contract is voidable at option of aggrieved party.
- In some cases, rescission may not be possible (e.g. when parties cannot be restored to their original position or where 3rd party has acquired rights in good faith)

2) Restitution

- Return of the benefit received by one party from the other under a void contract.
- When a contract becomes void it needs not to be performed by either party.

3) Damages

- Monetary compensation allowed for loss suffered by aggrieved party.
- Object is not to punish the party at fault but to compensate aggrieved party (financial loss).

4) Action for Price

- It is also a monetary compensation and is applicable when one party has performed his part of contract and now wants to recover the price of goods/services delivered or provided

5) Specific performance⁹⁴

Compelling a party to execute the agreement according to its terms.

Specific performance is allowed only in a limited number of cases, for example:

- Monetary compensation is not adequate
- Actual damage cannot be ascertain due to non-performance
- It is probable that compensation in money on non-performance cannot be obtained
- There is a contract for the sale of rare commodities
- There is a contract for the sale of land / building / apartment / houses

Suit for specific performance is not maintainable where:

- Monetary compensation is considered as an adequate remedy
- Contract is of personal nature (e.g. contract of services)
- Court cannot supervise the performance of the contract (e.g. construction of building)
- One of the parties is a minor
- Contract is inequitable to either party

6) Injunction⁹⁵

- Where a party to a contract does something which he promised not to do, the court may issue an order prohibiting him from doing so.
- It is particularly appropriate in case of anticipatory breach of contract.

7) Quantum meruit

- Same as discussed in previous unit and chapter # 7

Kinds of damages

Ordinary Damages⁹⁶

Which arise naturally in the usual course of things from the breach itself. These damages can be recovered if the following two conditions are fulfilled:

- The aggrieved party must suffer by breach of contract, and
- The damage must be a direct consequence of the breach of contract

Special damages⁹⁷

Arising due to special losses which are in reasonable knowledge of the parties at time of formation of contract and are suffered to the aggrieved party due to breach.

Exemplary (vindictive) damages

Which are awarded with a view to **punish the wrong doer** and not (primarily) to compensate the injured party. The court may award these damages only in following 2 cases:

- A breach of promise to marry

Damages shall be calculated on the basis of mental injury sustained by the aggrieved party.

- Wrongful dishonour of a cheque by a banker.

The rule is smaller the amount of the cheque, larger will be the amount of damages. (A trader may recover such damages as wrongful dishonour of cheque shall adversely affect his goodwill but a non-trader will have to prove loss of goodwill before claiming so)

Nominal damages

Where injured party has sustained very little (or even no) loss, a nominal amount of damage is claimed from the other party just to make that party realize his mistake.

Damages for inconvenience and uneasiness⁹⁸

If a party has suffered physical inconvenience and discomfort due to breach of contract, that party can recover the damages for such inconvenience and discomfort.

Liquidated damages

- When parties at the time of formation of contract, specify a sum which will become payable by the party responsible for breach
- That sum can be the genuine pre-estimate of the loss that would be suffered in breach

Penalty

If a contract states that a particular sum is to be paid on breach of the contract and

- That sum is not the genuine pre-estimate of the loss that would be suffered in breach or
- That the sum is disproportionate to actual loss likely to result due to breach
- Court can decrease but not increase the penalty stipulation.

Stipulation for Interest

Two parties may agree to give a specific rate of interest in case of breach of contract.

Forfeiture of Security Deposit (or Earnest Money)

In such cases, the court may award reasonable compensation only but in case where contract is made with the government, government can forfeit the whole amount of security deposit.

Rules regarding amount of damages

- The object of awarding damages is not to punish the party at fault
- The injured party is to be placed in the same position as money can do if the contract had been performed
- Aggrieved party can recover actual loss suffered by him arising naturally.
- If damages are difficult to assess, it does not prevent the injured party from recovering.
- Where no real loss arises nominal damages are awarded.
- If the parties fix **any amount** as damages, then the court will allow only reasonable amount.
- It is the duty of the injured party to minimise the damage suffered.

Remoteness of damages⁹⁹

Some losses clearly result from breach of contract but are considered too remote from the breach that it is unfair to expect the defendant to compensate the claimant for them.

CH # 7**SPECIFIC TYPE OF CONTRACTS****QUASI CONTRACTS**

A **Quasi contract** is an obligation imposed by law in absence of any agreement between the parties. A quasi-contract is not an actual contract, but is a legal substitute formed to impose equity between two parties. These are also known as constructive contracts.

Types of Quasi contracts**Supply of necessities¹⁰⁰**

If a person incapable to enter into contract or his dependent is supplied by another person necessities suited to his conditions in life the person supplying such necessities is entitled to be reimbursed his price from the property of such incompetent person.

Payment by interested person¹⁰¹

A person, who is interested in the payment of money which another is bound by law to pay, and who pays it, is entitled to be reimbursed by the other. Following conditions must be met

- The payment made should be bona fide for the protection of one's interest
- The payment should not be a voluntary one
- The payment must be such as the other party was bound by law to pay

Person enjoying benefit of non-gratuitous act / goods¹⁰²

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 benefit thereof, the latter is bound to make compensation to former in respect of, or to restore, thing so done or delivered.

- The thing must have been done lawfully
- The person doing the act should not have intended to do it gratuitously
- The person for whom the act is done must have enjoyed the benefit of the act.

Finder of goods¹⁰³

- A person who finds goods belonging to another, and takes them into his custody, is subject to the same responsibility as a bailee. (Ch # 7)
- He is bound to take as much reasonable care of the goods as he takes of his own goods.
- He must also take reasonable steps to trace its owner
- If he does not, he will be guilty of wrongful conversion of the property.

Payment by mistake or under coercion¹⁰⁴

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

QUANTUM MERUIT

Quantum Meruit means "as much as earned or deserved." The aim of such an award is based on an implied agreement to pay for what has been done. It is likely where one party has already performed part of his obligations and the other party then repudiates the contract.

Application of Quantum Meruit

Quantum meruit applies in the following cases:

Void agreement or contract that becomes void¹⁰⁵

Any person who has received any advantage under such agreement or contract is bound to restore it, or to make compensation for it to the person from whom he received it.

Person enjoying benefit of non-gratuitous act / goods¹⁰⁶

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 benefit thereof, the latter is bound to make compensation to former in respect of, or to restore, thing so done or delivered.

Act preventing completion of performance¹⁰⁷

If a party does not complete the contract or prevents the other party from completing it, the aggrieved party can sue on quantum meruit.

Divisible contract¹⁰⁸

The party at default may sue on a quantum meruit if the contract is divisible and the party not at default has enjoyed benefits of the part performance.

Indivisible contract performed completely but badly (i.e. with faults)¹⁰⁹

Party at default may claim the amount agreed after deducting any amount which the other party has paid to remove faults.

Express or Implied contract to render services but no remuneration is pre-settled

In such a case reasonable remuneration is payable.

CONTINGENT CONTRACTS

Contingent contract¹¹⁰

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 following are the characteristics of contingent contracts:

- It depends upon the happening or non-happening of some future event.
- Event must be collateral to the contract
- Event must be uncertain

Difference between contingent contract and wagering agreement

	Contingent contract	Wagering agreement
Validity	It is a valid contract.	It is void and illegal.
Interest of parties	Parties have real interest in the occurrence or non-occurrence of the event	Parties are not interested in occurrence or non-occurrence of the event except for the winning or losing the amount.
Uncertain event	The future uncertain event is merely collateral.	The uncertain event is sole determining factor of the agreement.
Reciprocal promises	It consists of reciprocal promises.	It may or may not consist of reciprocal promises.

CONTRACT OF INDEMNITY

Contract of indemnity [Section 124]

A contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person.

Parties in a contract of indemnity

- | | |
|---|---|
| ▪ Indemnifier (Promisor) ¹¹¹ | Person who promises to make good the loss |
| ▪ Indemnified / Indemnity holder (Promisee) | Person whose loss is to be made good |

Rights of indemnity holder

A promisee is entitled to recover following amounts from promisor:

- All damages which he may be compelled to pay in any suit in respect of any matter to which the promise to indemnify applies;
- All costs which he may be compelled to pay in bringing or defending such suits.
- All sums which he may have paid under the terms of any compromise of any such suit.

Indemnified should not act against the order of promisor and should act as any prudent man would act under similar circumstances in his own case, or with the authority of indemnifier.

Time of commencement of the indemnifier's liability¹¹²

- Contract Act is silent on the time of commencement of the indemnifier's liability
- On basis of judicial pronouncement of courts, it can be said that liability of an indemnifier commences as soon as the liability of the indemnity holder becomes absolute and certain.

CONTRACT OF GUARANTEE

Contract of guarantee [Section 126]¹¹³

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

Parties in a contract of guarantee

- | | |
|--------------------|--|
| ▪ Principal debtor | The person in respect of whose default the guarantee is given. |
| ▪ Creditor | The person to whom guarantee is given. |
| ▪ Surety | The person who gives guarantee. |

Essentials of a contract of guarantee

Tripartite agreement

There are three contracts in contract of guarantee:

- Contract between creditor and the principal debtor
- Contract between surety and the principal debtor
- Contract between surety and creditor

Consent of parties

All three must have consented in a contract of guarantee.

Existence of a debt

- If no such liability exists, then there cannot be a contract of guarantee.
- The principal debtor can be a minor; in this case surety will be liable personally.

Essentials of a contract

All the essentials required in a contract must exist in a contract of guarantee.

Not obtained through Misrepresentation

A guarantee must not be obtained by misrepresentation.

Not obtained through Fraud

A guarantee must not be obtained by fraud.

Kinds of guarantee

1) Specific guarantee¹¹⁴

Where a guarantee extends to a single transaction or debt. The liability of the surety comes to an end when the guaranteed debt is duly discharged or the promise is duly performed.

2) Continuing guarantee¹¹⁵

When a guarantee extends to a series of transactions, it is called a continuing guarantee. A surety's liability continues until the revocation of the guarantee.

Revocation of a continuing guarantee

A continuing guarantee can be revoked in the following ways:

- May be revoked by the surety as to future transactions, by **notice** to the creditor.
- In case of death of the surety (in the absence of any contract to the contrary)
- Novation
- Alteration
- Release or discharge of the principal debtor by creditor
- Compounding of creditor with the principal debtor
- Creditor's act or omission impairing surety eventual remedy
- Loss of security

Nature of surety's liability

Nature of surety's liability - It is co-extensive¹¹⁶

The liability of a surety is equal to that of the principal debtor unless otherwise agreed.

Limitation of surety's liability

Liability of surety may be made less than that of the principal debtor by an express contract.

Initiation surety's liability

The liability of the surety arises immediately at the time of default by the principal debtor.

Condition precedent to surety's liability

Where a person gives a guarantee upon a contract that a creditor shall not act upon it until another person has joined in it as co-surety, guarantee is not valid if that person does not join.

Rights of surety

Rights against / towards principal debtor

Right to subrogation

- After making a payment, surety is clothed with all the rights of the creditor, which he can himself exercise against the principal debtor.

Right to indemnity¹¹⁷

- There is always an implied promise by the principal debtor to indemnify the surety
- Surety is entitled to recover from the principal debtor all payments properly made under the guarantee (including the interest)

Rights against / towards creditor

Rights to securities

- Entitled to the benefit of every security which the creditor has against principal debtor (whether surety know existence of security or not at the time of contract of suretyship)
- If the creditor loses or without the consent of the surety parts with such security, the surety is discharged to the extent of the value of the security¹¹⁸.

Right to claim set off

- Surety has a right to claim set off if any which principal debtor had against the creditor.

Rights against co-sureties (Right to claim contribution)¹¹⁹

When a debt is guaranteed by two or more sureties, they are called co-sureties.

- Co-sureties are liable to contribute, as agreed, towards the payment of the guaranteed debt.
- If one of the co-sureties makes payment, he has a right to claim contribution from others

Rules of contribution between co-sureties:¹²⁰

- Normally, all co-sureties are to contribute equally in case of default by principal debtor
- If co-sureties have agreed to guarantee different sums than co-sureties are liable to contribute equally, subject to the maximum amount guaranteed by each one.
- Where there are co-sureties, a release by the creditor of one of them does not discharge the others, neither does it free the surety so released from his responsibility to other sureties

Modes of discharge of surety

Discharge of surety by revocation

Notice

A surety can be discharged by giving notice to the creditor in case of continuing guarantee

Death of surety

Deceased surety's estate will not be liable for any obligation after the death of the surety (even if the creditor has no notice of the death)

Novation

If there is a new contract of guarantee, the old rights and obligations would extinguish

Discharge of surety by the conduct of the creditor

Alteration¹²¹

If an alteration is made without the consent of the surety then the surety is discharged as to the transactions, subsequent to the alteration.

Release of principal debtor

Any contract between creditor and principal debtor, by which principal debtor is released.

Arrangement

A contract between creditor and principal debtor, by which creditor makes a competition with, or promises to give time to, or not to sue, the principal debtor, discharges the surety, unless the surety assents to such contract.

Discharge of surety by invalidation of contract

Misrepresentation/ Fraud¹²²

Any guarantee which has been obtained by means of misrepresentation by the creditor or keeping silence as to material circumstances concerning a material part of the transaction

Act or omission¹²³

If creditor does any act which is inconsistent with the rights of the surety, or omits to do any act which his duty to the surety requires him to do, and the eventual remedy of the surety himself against the principal debtor is impaired, the surety is discharged.

Failure of co-surety to join surety

Where a person gives a guarantee upon a contract that a creditor shall not act upon it until another person has joined in it as co-surety, the guarantee is not valid if that other person does not join.

Circumstances where surety is not discharged

- Where a contract to give time to the principal debtor is made by the creditor with a third person, and not with the principal debtor, the surety is not discharged.
- Patience on the part of creditor to sue the principal debtor or to enforce any other remedy against him, does not automatically discharge the surety.
- Where there are co-sureties, the release by the creditor of one of them does not discharge the other nor does it free the surety so released from his responsibility to other sureties

Difference between contract of indemnity and contract of guarantee

	Contract of Indemnity	Contract of guarantee
Number of parties	There are 2 parties; Indemnifier and indemnity holder.	There are 3 parties; Principal debtor, creditor and surety.
Number of contracts	There is only 1 contract.	There are 3 contracts.
Object	Saving the indemnity holder from any loss.	Payment of debts of principal debtor in case of his default.
Nature of liability	Primary and unconditional.	Secondary and conditional and co-extensive.
Arising of liability	Only on the happening of a contingency.	Only on non-performance of existing promise or non-payment of existing debt
Right to sue	The indemnifier cannot sue a third party in his own name	A surety, after payment, can sue the principal debtor in his own name.



BAILMENT

Bailment is the delivery of goods by one person (bailor) to another (bailee) for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them¹²⁴.

Essential elements of bailment

Agreement (Express/Implied)

Delivery of goods

- The delivery must be voluntary
- Delivery may be actual or constructive
 - Actual delivery is when goods are physically transferred by one person to another.
 - Constructive/symbolic delivery may be made by doing something which has the effect of putting the goods in the possession of the intended bailee or any authorised person

For some purpose

Return of specific goods

In contract of bailment the goods are either returned or disposed of as per the instructions of bailor after the purpose is achieved.

Types of bailment

Bailment on the basis of reward

- Gratuitous bailment
Contract of bailment where no consideration passes between the bailor and the bailee.
- Non-gratuitous bailment
Contract of bailment where some consideration passes between the bailor and the bailee.

Bailment on the basis of benefit

- Bailment for the exclusive benefit of bailor¹²⁵
- Bailment for the exclusive benefit of bailee¹²⁶
- Bailment for the mutual benefit of bailor & bailee¹²⁷

Sub-bailment

- A sub-bailee is a person to whom the actual possession of goods is transferred by someone who himself is not the owner of goods but holding that as a bailee of the owner.
- Relationship between owner and sub-bailee is that of bailor and bailee
(Where bailee sub-bails the goods with the authority of the owner)

Pledge/Pawn

Bailment of goods as security for payment of a debt or performance of a promise.

PLEDGE ¹²⁸

Pledge is the bailment of goods as security for payment of a debt or performance of a promise.

- | | |
|-----------------------|--|
| ▪ Pledger (or Pawnor) | The person who delivers the goods as security |
| ▪ Pledgee (or Pawnee) | The person to whom goods are delivered as security |

Rights of Pawnee

- Pawnee may retain the goods pledged for:
 - Payment of the debt or the performance of the promise
 - For the interest of the debt and
 - All necessary expenses incurred in respect of possession or for preservation of goods.
- Right of retainer for subsequent advances also¹²⁹
(unless those are separately secured)
- Right against true owner, when the pawnor's title is defective
(pawnee acquires a good title, if he acts in good faith and without notice of defect of title)

Rights where pawnor makes default in payment or performance**Right to sue**

Pawnee may file a suit against the pawnor upon the debt or promise and may retain the goods pledged as a collateral security.

Right to sell

Pawnee may sell the goods pledged after giving pawnor a reasonable notice of the sale.

- He can recover from the pawnor any deficiency arising on the sale of the goods by him.
- He shall have to hand over the surplus to the pawnor, if any, realized on sale of goods.¹³⁰

Rights of pawnor

- Right to get back goods on the performance of promise, or repayment of loan and interest
- Right to pay debt subsequently after default, before actual sale, to recover those goods back (he must pay, in addition, any expenses which have arisen from his default)
- Right to see that the pawnee preserves the goods pledged and properly maintains them.

Other duties of pawnee and pawnor are same as duties of bailor and bailee

Pledge by non-owners

Pledge by mercantile agent

Pawnee of goods from a mercantile agent, who has no authority from the principal to pledge, gets a good title to the goods if:

- Agent is in possession of the goods or documents of title to goods with consent of owner
- Agent pledges the goods while acting in ordinary course of business of a mercantile agent

Pledge by person in possession under voidable contract¹³¹

If such person pledges those goods before the contract has been rescinded, the pawnee acquires a goods title to them

Pledge by seller in possession after sale¹³²

Where a seller having sold goods, continues to be in possession of goods or documents of title to the goods and pledges them either himself or through a mercantile agent to a pawnee, it will be a valid pledge.

Pledge by buyer in possession before sale

Where a person having bought or agreed to buy goods obtains with the consent of the seller, possession of the goods or documents of title to the goods and pledges them either himself or through an agent to a pawnee, it will be a valid pledge

Pledge by co-owner in possession

One of the several co-owners of goods in possession thereof with the assent of the other co-owners may create a valid pledge of the goods

Note: In all of the above cases, it would be assumed that the pawnee acted in good faith and without notice about the defect of the title/true owner.

Difference between pledge and bailment

	Pledge	Bailment
Parties	Pawnor and Pawnee	Bailor and bailee
Purpose	Security for the payment of a debt or performance of a promise	For safe custody, transportation or any other purpose etc.
Right to use	Pawnee has no right to use the goods pledged.	Bailee can use, if the terms of bailment so provide.
Right to sell	Pawnee can sell goods after giving notice to pawnor (in default)	Bailee can either retain the goods or sue the bailor for his dues.

CH # 8**AGENCY****ROLE OF AN AGENT**

Agent: An agent is a person employed to do any lawful act for another or to represent another (the Principal) in dealing with a third person.

- There is a legal relationship between the agent and the principal.
- The agent acts on behalf of the principal, by negotiating with a third party.
- When the contract is made, it is between the principal and the third party.
- Any person who is of the age of majority and who is of sound mind may **employ an agent**.
- Any person may become an agent (even a minor or unsound mind)
- No consideration is necessary to create an agency.

Types of agent

- Commercial or Mercantile agent
An agent who regularly buys or sells goods on behalf of a principal
(various kinds of mercantile agent are broker, factor, commission agent and del credere)
- Broker
An intermediary who arranges trades or transactions on behalf of clients (principals).
- Del credere agent
Who in consideration of an extra commission, guarantees his principal that the persons with whom he enters into contract on behalf of the principal shall perform their obligation. (He occupies the position of both a guarantor and an agent)
- Auctioneer
An agent who is authorised to sell property of a principal at auction.
- Company directors, managers & employees
Act as agents for their company
- Partners in a business partnership
Business partners act as agents for their partnership business.
- Sub-agent
Person employed by the original agent to act under his control in the business of agency.
- Co-agent or a substituted agent
A person who is named by the agent, on an authority from the principal, to act for principal. He is agent of principal, though he is named, at the request of principal, by the agent. In selecting a co-agent for his principal an agent is bound to exercise the same amount of discretion as a man of ordinary prudence would exercise in his own case (if he does this, he is not responsible to principal for acts or negligence of his co-agent)

Rules regarding Sub-Agent

Agent may appoint a sub-agent and delegate the work to him if:

- The principal has expressly permitted delegation of such power.
- If is the ordinary custom of trade, a sub-agent may be employed.
- The nature of work is such that a sub-agent is necessary
- The acts to be done are purely immaterial.
- Unforeseen emergencies arise rendering appointment of the sub-agent necessary.

If a sub-agent is properly appointed:

- Principal is bound by the acts of sub-agent as if the sub-agent was an original agent.
- Agent is responsible to the principal for the acts of the sub-agent.
- Sub-agent is responsible for his acts to agent, but not to principal (except in case of fraud)

Where a sub-agent is not properly appointed (without authority and justification)

- Agent stands as a principal towards such a sub-agent
- Principal is not represented by such sub-agent and not liable for the acts of the sub-agent.
- Agent is responsible for acts of sub-agent to the principal as well as to the third parties.
- Sub-agent is responsible for his acts only to the agent and is not responsible to the principal at all. (even for fraud or willful wrong)

Difference between Sub-agent and Co-agent

	Sub-agent	Co-agent / substituted agent
Control	Works under the control of agent.	Works under instructions of principal
Contract	No contract with principal.	Contract exists with principal.
Responsibility	Responsible to the principal for the act of the sub-agent.	Not responsible to principal for the act of substituted agent
Termination	Terminated by the termination of original agency	Not affected by the termination of the original agency.
Remuneration	Paid by the agent.	Paid by the principal.

Legal problems with agency relationships

- A person might claim to act on behalf of a principal P, and 3rd party might enter into an agreement believing the contract to be with P. However, P might deny the agency relation.
- A person might be agent of P with authority to make agreements on behalf of P. Agent might go beyond limits of authority. P might then refuse to accept the agreement.

CREATION OF AGENCY

There are 4 ways in which an agency relationship, recognised in law, can be established:

- By express appointment (by agreement)
- By estoppel
- By ratification
- By necessity.

Agency by express appointment (by agreement)

- In many cases, the relationship is established formally, in writing.
- This written agreement would be a contractual agreement between principal and agent.
 - Usually specify the ways in which agent has authority to act on behalf of principal.
 - Makes it clear, between principal and agent, what the agent is allowed to do
- An agency agreement may also be established by verbal agreement (although it would be tough to prove onwards if anyone denies it; not much recommended)
- Principal may wish to give the agent the power to execute deeds (a form of written legal document which is executed by signature). In this case, agent must be appointed by a deed.
- When an agent is appointed by deed, he is 'given a power of attorney' to act for principal.

Agency by estoppel

'Estoppel' is a word used in law to mean 'stop' or prevent'.

An agency relationship may be created when someone has led others to believe that a person has the authority to act on his behalf. An express agency agreement does not in fact exist, but it may seem to other people that it does.

If a third party then agrees a transaction with person who appears to be an agent, 'principal' can be prevented ('estopped') from denying that an agency agreement does not exist.

For 3rd party to rely on existence of an agency by estoppel, following conditions must apply.

- The representation must be made by the principal.
- This representation must have been made to 3rd party
- 3rd party must have relied on the existence of agency relationship in reaching a decision.

If these circumstances apply, a third party who suffers losses resulting from the situation can hold the principal as liable, and take legal action against the principal.

Agency by ratification

Ratification' means 'giving approval to' or 'giving validity to' something.

When a person does not actually have actual authority as an agent negotiates with a third party, claiming to be an agent of a named principal; the person who has been named as principal might then choose to accept (i.e. ratify) the contract with the third party.

If the actions are not ratified, the contract is between the agent personally and the other party.

Effect of ratification

- Ratification is established from the time of formation of contract (past)
- A contractual relationship is established between the ratifier and the third party.

Requisites of valid ratification

- Act should be done on behalf of the person who wants to ratify it.
- Ratifier must be in existence at the time when the contract is entered into.
- Ratifier must be competent to contract at time of contract as well as at time of ratification.
- Only lawful acts can be ratified.
- There cannot be ratification of partial transaction (whole transaction must be ratified)
- Ratifier must have complete knowledge of transaction (else ratification will not be valid)
- No act can be ratified which result in third party to damages.
- Ratification must be made within a reasonable time.

Agency by necessity

Occurs in circumstances where there is no agreement between the parties, but an emergency requires that a party (agent) should take action to protect interests of other party (principal)

For agency by necessity to exist, the following conditions must apply.

- There must be a real emergency.
- It must be impossible for person acting as agent to contact owner and obtain instructions.
- Person acting as agent by necessity must act as far as possible, in best interests of principal.

Agency by operation of law

Sometimes an agency arises by operation of law.

- When a company is formed its first directors are its agents by operation of law.
- A partner is agent of the firm for the purposes of the business of the firm.

Authority of an agent¹³³**Express authority**

- A written agency agreement may give the agent express authority.
- Principal should specify what tasks, power and authority the agent can exercise.
- If agent acts outside limits of his express authority, this will affect contractual relationship between the principal and the third party.
- The legal consequences will depend on whether the third party knew that the agent was acting outside the limit of his authority.

Implied authority¹³⁴

- Authority of an agent in excess of his express authority (inferred from the circumstances)
- Unless third party has knowledge to the contrary, he is entitled to assume that an agent holding a particular position has all the powers that are normally given to such position.

Ostensible authority (apparent authority)

Ostensible authority arises in two ways.

- Where a person makes a representation to third parties that another person has authority to act as his agent, even though he has not actually been appointed as agent. (estoppel)
- Where a person has previously represented to a third party that another person has the authority to act as his agent and:
 - Authority was subsequently taken away/ended, but
 - Third parties who previously dealt with the agent have not been informed of this fact.

RIGHTS AND DUTIES OF THE AGENT AND PRINCIPAL

Duties of agent

- Carry out mandate (the work for which he has been appointed)
- Follow all lawful instructions of his principal
- Agent should conduct the business of agency with reasonable carefulness and proficiency.
- Maintain and render accounts
- Communicate to the principal in cases requiring principal's instructions / directions
- Not to deal personally
- Pay sums received (after deducting amounts due to him)
- In case of principal's death or insanity, agent is bound to take all reasonable steps for the protection and preservation of the interests entrusted to him
- Keep the information of principal secret (even after termination of agency)
- Not to make secret profit
- Not to delegate his authority to another person without the consent of his principal
- Exercise same amount of discretion as a man of ordinary prudence would exercise in his own case while selecting a sub-agent or substituted agent.
- In case of an emergency, do all such acts for the protecting his principal from loss as would be done by a person of ordinary prudence in his own case under similar circumstances

Rights of agent

- Right to receive remuneration (agreed or any reasonable)¹³⁵
- Lien on goods, papers and other properties of principal until remuneration has been paid
- An agent has a right to retain his principal's money in his hands for all money due to himself in respect of:
 - Remuneration;
 - Advances made; or
 - Expenses properly incurred by him in conducting the business of agency.
- Right to be indemnified against the consequences of all lawful acts done by him¹³⁶
- Right to be compensated for injuries caused by neglect or want of skill of the principal
- An agent has a right to stop the goods in transit to the principal just like an unpaid seller if:
 - He has bought goods for his principal by incurring personal liability for the price and
 - The principal has become insolvent.

Duties of principal

- Indemnify the agent for lawful acts
- Indemnify against consequences of acts done in good faith
- Compensate the agent for injuries sustained by him by neglect on part of principal.
- Pay the agreed remuneration (or if no remuneration is agreed, a reasonable remuneration)

Rights of principal

- The principal can revoke the authority (except in case of irrevocable agency)
- Must be compensated by the agent for any loss sustained due to non-following of the instructions of principal.
- Entitled to compensation for any loss which is the direct consequence of agent's neglect, want of skill or misconduct.
- To have proper accounts when he demands.
- To repudiate the transaction, if an agent deals on his own account without first getting prior consent of his principal
- Entitled to claim all benefits resulting from transaction where agent secured secret profit
- Principal can refuse to pay remuneration (or a part of it), If an agent has committed misconduct in the business of agency

PERSONAL LIABILITY OF AN AGENT

It's a general rule that an agent is not liable if he acts on behalf of the principal. However, in certain circumstances agent is personally liable which are discussed below:

- When an agent contracts for a **Foreign principal** (resident abroad)
- If an agent declines to disclose the identity of his principal (**Unnamed principal**).
- Where he contracts on behalf of a **principal who cannot be sued**
- Where an agent acts for an **undisclosed principal** and contracts in his own name
- An **agency coupled with interest**, as the agent has himself an interest in subject matter
- If there is any **usage or custom** of market or trade where agent assumes personal liability
- Where an agent **exceeds his authority** (he is personally liable for the excess part)
- For the acts of an **improperly appointed sub-agent**.
- Where an agent, while acting in the course of business of agency **incurs personal liability**
- Where an agent has been employed to do a **criminal act**
- If an agent enters into **special contract with third party** that he will be personally liable.

TERMINATION OF AGENCY

Termination by act of parties:

1) Mutual agreement between principal and the agent

2) Revocation by the principal

He may revoke the authority of agent at any time before agent has exercised his authority.

- Compensation
Principal must make compensation to agent for revocation without sufficient cause.
- Reasonable notice
Reasonable notice must be given of revocation where agency is for a fixed period of time
- Express or implied
May be expressed or may be implied by the conduct of the principal.
- Termination
The termination of the authority of an agent takes effect:
 - As regards to the agent from the time when it becomes known to him
 - As regards third persons from the time it becomes known to them
 - (even in case of death of principal)
- Effect of termination
Agent would be entitled to indemnity for acts done and to receive remuneration till date

3) Renunciation by the agent

He may renounce the business of agency at any time and in same manner in which the principal has the right of revocation.

- Compensation (same as above)
- Reasonable notice (same as above)
- Express or implied (same as above)

Termination by operation of law

- Completion of business
- Expiry of time for which agent was appointed
- Death of the principal or agent (unless the agency is irrevocable)
- Insanity of the principal or agent (unless the agency is irrevocable)
- Insolvency of the principal
- On winding up of a company (who was a principal)
- Destruction of subject matter
- Principal or agent becoming an alien enemy

CH # 9**PARTNERSHIP ACT****THE NATURE OF PARTNERSHIP****Partnership**

"Partnership is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all".

Firm and partners

"Persons who have entered into partnership with one another are called individually "partners" and collectively "a firm" and the name under which their business is carried on is called the "firm name".

Act of firm

"An act of firm means any act or omission by all the partners, or by any partner or agent of the firm which gives rise to a right enforceable by or against the firm."

Third party

"Third party used in relation to form or to a partner therein means any person who is not a partner in the firm."

Essential elements of a partnership**1) Association of two or more persons**

- There can be no partnership consisting of a single individual.
- If the number gets reduced to one, for any reason, it ceases to be a partnership.
- Partnership Act does not say anything about the maximum number of partners.

2) Agreement

- This agreement may be express (written or oral) or implied.
- The written agreement is known as 'partnership deed'.
- A partnership deed usually sets out the following:
 - Firm name
 - Place or principal place of business of the firm
 - Names of any other places where the firm carries on business
 - The date when each partner joined the firm
 - Number of partners
 - Names in full and permanent addresses of partners
 - Purpose and duration of partnership (if any)
 - Rights and duties of the partners.
 - Amount of capital that each partner should put into the business

3) Carrying on business¹³⁷

- The parties must have agreed to carry on a business.
- Where there is no business to be done, there can be no question of partnership.
- If the purpose is to carry on some charitable work it will not be a partnership.

4) Sharing of profits

- Partners may share it equally or in any other proportion.
- It is not necessary that the partners should agree to share losses.
- A person receiving profits is not necessarily a partner, such as:
 - Lender of money to persons engaged or about to engage in any business
 - Servant or agent as remuneration
 - Widow or child of a deceased partner as annuity
 - A transferee of a partner's interest
 - A minor who is admitted to the benefits of an existing partnership
 - Previous owner or part owner as consideration for the sale of goodwill or share of it.

5) Mutual agency¹³⁸

- Mutual Agency relationship means that each partner is both an agent and a principal.
 - Agent in the sense that he has the capacity to bind other partners by his acts done.
 - Principal in the sense that he is bound by the acts of other partners.

Types of partnership**Partnership-at-will**

- Where no provision is made between the partners for the duration of their partnership
- In such partnership there is no provision as to when the partnership will come to an end.
- Any partner is free to dissolve the partnership by giving a notice in writing to all other
- The firm is dissolved as from the date mentioned in the notice (if any) or if no date is mentioned as from the date of the communication of the notice.
- If agreement provides that the partnership can be dissolved by mutual consent of all the partners, it not constitute a partnership at will.

Particular partnership

- Where a partnership is created for any particular purpose or for a specific time period
- Such partnership comes to an end on the completion of venture or on expiry of the period.
- If partners decide to continue partnership after that, then it becomes partnership at will.

Types of partners

Actual or ostensible partner	<ul style="list-style-type: none"> ▪ A partner who is actively engaged in the conduct of a business ▪ Such partner is an agent of all other partners for the purposes of the business ▪ Can bind himself and others for acts done in ordinary course of business.
Sleeping or dormant partner	<ul style="list-style-type: none"> ▪ Not known as such as a partner to third parties dealing with the firm. ▪ May or may not take active part in the conduct of the business of the firm. ▪ He, like other partners, invests capital and shares in profits of the business. ▪ He is equally liable along with other partners for all debts of the firm ▪ Not required to give public notice of his retirement (not liable for any act done by the firm after his retirement)
Nominal partner	<ul style="list-style-type: none"> ▪ Does not contribute any capital or share in profits, but lends his name to firm ▪ He along with other partners is liable to the outsiders for all debts of the firm.
Partner in profits only	<ul style="list-style-type: none"> ▪ A partner may agree that a partner shall get a share of the profits only and that he shall not be liable to contribute towards the losses. ▪ But for third parties he is liable for all the debts of the firm.
Sub-partner	<ul style="list-style-type: none"> ▪ When a partner agrees to share his profits derived from firm with a stranger ▪ Sub-partner is not connected with firm and cannot call himself a partner ▪ He has no rights against the firm nor is he liable for the acts of the firm.
Silent partner	<ul style="list-style-type: none"> ▪ Those who by agreement with other partners have no voice in management ▪ They share profit and losses, are fully liable for the debts of the firm
Partner by estoppel or holding out	<ul style="list-style-type: none"> ▪ Where a person holds himself out as a partner or allows other to do it, they are then stopped from denying the character he has assumed and upon the faith of which creditors may be presumed to have acted.

Difference between a partnership firm and a joint stock company

	Partnership firm	Joint stock company
Formation	Created by an agreement alone.	Created by law.
Registration	Registration is optional.	Registration is compulsory.
Legal entity	It is not a separate legal entity.	It is a separate entity.
Nature of liability	Partners have joint and several liability (i.e. unlimited liability).	It has limited liability (i.e. liability is restricted to amount of capital)
Perpetual succession	A firm is dissolved on death or insolvency of a partner	It continues to exist irrespective of death or insolvency of its members/directors.
Agency	A partner is an agent of the firm	Shareholders are not agents.
Transfer of interest	Partner cannot transfer interest without getting other's consent	No such restriction for transfer of shares.
Number of persons	Minimum 2, Maximum 20 (other than banking business)	Minimum one person can carry SMC No limit on owners for public company.
Management	All partners can take part in it	All shareholders cannot take part in it.

Difference between a partnership firm and co-ownership

	Partnership firm	Co-ownership
Formation	Created by an agreement alone.	Not necessarily a result of an agreement
Business	Carry on business in essential	Does not necessarily involve business.
Number of persons	Minimum 2, Maximum 20 persons (other than banking business)	No limit on maximum number of the co-owners.
Sharing of profit	One of the essential elements.	Does not involve sharing of profit.
Agency	A partner is an agent of the firm	Co-owners are not agents to one another
Transfer of interest	Partner cannot transfer his interest without getting consent from others	Co-owner can transfer his interest without getting consent from other(s)

RELATIONS OF PARTNERS TO ONE ANOTHER

General duties of partner

Mandatory duties of a partner that cannot be changed by an agreement.

- **Duty to be just and faithful**
 - An ideal partnership is one where there is mutual trust and confidence
 - He must observe utmost good faith and fairness towards other partners
- **Duty to carry on business to the greatest common advantage of the firm**
- **Duty to render true accounts to co-partners**
 - Each partner must be ready to explain the accounts of firm
 - No partner should think of making a secret profit at the expense of the firm.
- **Duty to provide full information to other partners**
- **Duty to indemnify (compensate) for loss caused by his fraud**
- **Duty to be liable jointly and severally - unlimited liability¹³⁹**
 - Every partner is liable jointly with all other partners
 - Every partner is also liable severally (separately) to third parties for all acts of firm
 - Third party may take legal action for losses incurred as a result of a breach of contract against all the partners jointly, or any individual partner
- **Duty to act within authority**
 - Where he exceeds the authority conferred on him and firm suffers a loss he shall have to compensate the firm for any such loss
- **Duty in case of emergency¹⁴⁰**
 - To do all such acts for protecting firm from loss as would be done by a person of ordinary care, in his own case (under similar circumstances).
 - Can even exceed his authority in order to save the firm from any loss.

Qualified duties of partner

The qualified duties of a partner can be changed by an agreement amongst the partners.

- **Duty to attend diligently to his duties**
- **Duty to contribute to the losses**

- **Duty to indemnify for willful neglect**
- **Duty to use firm's property exclusively for the firm**
 - No partner should use partnership property for his personal benefit
- **Duty to account for personal profits derived¹⁴¹**
- **Duty not to compete with the business of the firm¹⁴²**
 - Liable to account to firm for all the profits that he earns from competing business
- **Duty not to assign his interest**
 - No partner can assign or transfer his partnership interest to any other person so as to make him a partner in the business without the consent of all other partners.
 - He can only assign his share of the profit and his share in the assets of the firm (transferee shall not have any right to interfere in the conduct of the business)

Rights of partner

- **Right to take part in the conduct of the business**
 - Every partner irrespective of his capital has an inherent right to take part in business
- **Right to be consulted in matters of the firm**
- **Right to have access to the books of firm**
- **Right to share the profits**
- **Right to interest on capital**
 - Interest on capital is allowed only when agreed among the partners.
 - If so entitled, such interest will be payable out of the profits, earned by the firm.
- **Right to interest on advances**
 - If a partner makes for any payment or advance beyond amount of capital he has agreed to subscribe, he is entitled to interest on it at rate of 6% per annum or as agreed upon.
- **Right to indemnity**
 - Every partner has a right to claim indemnity from firm in respect of payments made or liabilities incurred by him
- **Right to retire**
 - A partner has a right to retire with the consent of all partners or in accordance with an express agreement between the parties

- **Right of outgoing partner to share in the subsequent profits**
 - Surviving or continuing partners may carry on the business with the property of firm without any final settlement of accounts as between them and the outgoing partner.
 - Legal representative of deceased or outgoing partner, is entitled to proportionate share of the profits or interest at 6% on amount of his share in property of the firm.
- **Rights after reconstitution of firm**
 - Mutual rights and duties of the partners in the reconstituted firm remain the same as far as may be possible, as they were immediately before the change

Mutual Rights and Liabilities

Partners have following mutual rights & liabilities which are subject to contract between them

1. Duty to work without remuneration
2. Rights to share profits and losses equally
3. Right to interest on capital
4. Rights to interest on subsequent advance
5. Right to indemnity
6. Duty to indemnify for willful neglect

Partnership property¹⁴³

Subject to contract between the partners, the property of the firm includes:

- All property originally brought into the common stock of the firm
- All rights or interest in the property originally so brought
- All property acquired, by purchase or otherwise, by or for the firm and all rights and interest in any property so acquired and
- Goodwill of the business of the firm

RELATIONS OF PARTNERS TO THIRD PARTIES

Agent of the firm

A partner is the agent of the firm for the purpose of the business of the firm.

Authority of partners

Actual authority

- The authority of each partner may be specified in the partnership agreement.

Implied authority¹⁴⁴

- The act of a partner done by him as an agent of the firm in the course of business of the firm in the name of the firm, or in any other manner expressing an intention to bind the firm.
- An authority to bind the firm is known as implied authority of a partner.

Every partner within the scope of his implied authority may bind the firm by following acts:

- Buying and selling good, on behalf of the firm and giving valid receipts for them
- Receiving payments of debts due to the firm and giving valid receipts or discharge for them
- Contracting debts and paying debts on behalf of the firm
- Settling accounts with persons dealing with the firm
- Employing servants for the partnership of the firm
- Drawing cheques, accepting or endorsing bills of exchange and promissory notes in the name of the firm
- Pledging movable property of the firm
- Suing on behalf of the firm and defending suits in the name of the firm

Restrictions on the implied authority of a partner

Following acts are not included in the implied authority of a partner unless there is any usage or custom of trade

- | | |
|---|---|
| <ul style="list-style-type: none"> ▪ Arbitration ▪ Bank account ▪ Compromise ▪ Withdrawal of suit ▪ Liability Acceptance ▪ Acquisition ▪ Transfer ▪ Partnership | <ul style="list-style-type: none"> Submit a dispute relating to the business of the firm to arbitration Open a banking account on behalf of the firm in his own name Compromise or relinquish any claim or portion of a claim by the firm Withdraw a suit or proceeding filed on behalf of the firm Admit any liability in a suit or proceeding against the firm Acquire immovable property on behalf of the firm Transfer immovable property belonging to the firm Enter into partnership on behalf of the firm. |
|---|---|

Statutory restrictions

- The restrictions imposed by law
- Applicable against the whole world whether a particular person dealing with the firm has knowledge of it or not (e.g. about the name of the firm).

Restrictions by partnership deed

- Restriction which is specifically written in partnership deed
- It is effective only against the person dealing with the firm having knowledge of it¹⁴⁵

Ratification of actions taken by a partner outside his actual authority

- When a partner exceeds his authority, the other partners may approve such unauthorized act with retrospective effect.
- By ratification, partners can remove any doubt about
 - Existence of implied authority
 - Knowledge of the other party that the partner did not have the actual authority

Liabilities of partners and firm

- **Liability of a partner for acts of a firm**
 - The liability of the partner is both joint and several, so that the creditor may compel any one or more of the partners to discharge the whole of the debts of the firm.
- **Liability of the firm for wrongful acts of a partner¹⁴⁶**
 - Where by wrongful act or omission of a partner acting in ordinary course of business any loss or injury is caused to any third party, firm is liable to same extent as partner.
 - For fraud, the firm is liable to the third party for loss caused to them (same must be borne by partner committing the fraud and cannot be shared among all)
- **Liability of firm for misapplication by partners¹⁴⁷**
 - A partner/firm acting within his apparent authority receives money or property from a third party and misapplies it, the firm is liable to make good the loss.
- **Liability of partner to indemnify for willful neglect**
 - Every partner is under a liability to indemnify the firm for any loss caused to it by his willful neglect in the conduct of the business of the firm.
- **Liability of partners to share losses of the firm**
- **Liability of partner to account for personal (or secret) profits**
- **Liability to account for profit of competing business**
 - If a partner competes in business with partnership, without consent of other partners, he is liable to account to the firm for all profits earned from competing business.

Effect of admissions by a partner

Any admission or representation made by a partner is valid against the firm if:

- Such admission or representation relate to the affairs of the firm and
- Such admission or representation made in the ordinary course of business.

Effect of notice to an active partner

Any notice to a partner operates as a notice to the firm if the following conditions are fulfilled:

- Such notice must relate to the affairs of the firm
- Such notice must be given to a working partner and not to a sleeping partner
- There must not be any fraud committed by the partner receiving the notice.

Holding out / Estoppel

Where a person represents himself or allows partners to do it, he is then estopped from denying the character he has assumed and upon the faith of which creditors may have acted.

In order to render a person liable as a partner on the ground of estoppel or holding out:

- He must have by spoken or written or by his conduct represented himself to be a partner (Direct representation)
- He must have knowingly permitted himself to be represented as a partner to other person (Indirect representation)
- Other person must have acted on the faith of such representation and gives credit to firm. (whether or not person representing know that representation has reached other person)

Examples of applications of holding out partner

- Retiring partner

If a retiring partner does not give a public notice of his retirement and continuing partners still use his name as a partner he will be personally liable to third parties.

- A Minor on attaining majority

If a minor after attaining majority act as a partner without giving public notice, he will be liable as a partner by estoppel.

Exceptions of holding out

- Deceased partner

After a partner's death, the continued use of firm's name or of deceased partner's will not itself makes his legal representatives liable for any act of the firm done after his death.

- Insolvent partner

The estate of the insolvent partner is not liable for any act of the firm and the firm is not liable for any act of the insolvent.

Tutor's Note: Difference between Estoppel and Holding out

Due to its placement in the study text and the language given therein, a confusion normally arises in the minds of students regarding the difference between these 2. Although these 2 concepts are sometimes used as an alternate to each other (moreover the study text also have discussed the same in an overlapping tone and have explained both of the concepts together), yet we can make some demarcation between these 2 concepts.

Estoppel

- Where a person (appears to be Principal) makes a representation to third parties that another person (appears to be agent) has authority to act as his agent, even though he has not actually been appointed as agent; or
- Where a person (appears to be Principal) has previously represented to a third party that another person (appears to be agent) has the authority to act as his agent and:
 - Authority was subsequently taken away/ended, but
 - Third parties who previously dealt with the agent have not been informed of this fact.

In estoppel, due to **any act of (supposed) Principal** the 3rd party gets confused and think someone as (supposed) agent of that Principal

Holding out:

Where a person (supposed agent) represents himself, he is then estopped from denying the character he has assumed and upon the faith of which creditors may have acted.

In holding out, due to **any act of (supposed) Agent** the 3rd party gets confused and think someone as (supposed) Principal of that Agent

Rights of transferee of a partner's interest

A partner may transfer his interest in the firm by sale, mortgage or charge fully or partially.

Rights of Transferee

- He is entitled to receive the share of the profits of the transferring partner.
- On the dissolution of firm or on retirement of transferring partner he is entitled to receive:
 - Share of the assets of the firm to which the transferring partner is entitled.
 - Account from the date of the dissolution for the purpose of ascertaining the share.

Disabilities of Transferee

- No status of a partner.
- Disability to interfere in the conduct of the business during the continuance of the firm
- Disability to require accounts.
- Disability to inspect the books of the firm.
- Disability to challenge the accounts of profits agreed to by the partners.
- Disability to sue for dissolution of the firm.

Minor's admission to the benefits of partnership

A minor cannot enter into a partnership agreement but with the consent of all the partners for the time being a minor may be admitted to the benefits of partnership.

Position of a minor before attaining majority**Rights**

- Right to share property and profits of the firm as agreed by the partners
- Right to have access to accounts of the firm only and not to the secret books
- Right not to be adjudged insolvent

Liabilities:

- Personally not liable i.e. limited liability.
- His share is liable for the acts of the firm.

Disabilities:

- No status of a partner.
- No suit against partners for profit and property except after disconnecting his relation with the firm.
- Not entitled to have access to books other than accounts.

Position of a minor on attaining majority

- On attaining majority, the minor partner has to decide within 6 months whether he shall continue in the firm or leave it.
- These 6 months run from the later of:
 - His attaining majority or
 - When he first comes to know that he had been admitted to the benefits of partnership
- He should give a public notice of his choice to become or not to become a partner.
- If he fails to give a public notice, he is deemed to have become a partner in the firm on the expiry of those 6 months

Where such person elects to become a partner

- He hold Personal liability since the date of admission to the benefits of the firm
- He hold same share in profits and property of firm to which he was entitled as a minor.

Where such person elects not to become a partner

- The status of a minor holds up to the date of public notice
- His share is not liable for any act of the firm after the date of public notice
- He has right to sue partners for share of the property and profits

CH # 10**NEGOTIABLE INSTRUMENTS ACT****CHARACTERISTICS OF NEGOTIABLE INSTRUMENTS****Negotiable instruments**

A negotiable instrument means a:

- Promissory note
 - Bill of exchange or
 - Cheque
- payable either to order or to bearer.

Essential characteristics of negotiable instrument**1) Payable to order or bearer****Payable to order**

Which is expressed to be so payable or payable to a particular person (e.g. Pay A, Pay A or order)

A crossed cheque "Account Payee only" can however still be negotiated further.

Payable to bearer¹⁴⁸

Which is expressed to be so payable or on which the only or last endorsement is an endorsement in blank.

(e.g. "Pay to A or bearer or pay bearer")

2) Easy transferability

- Transferable from one person to another by mere delivery, if payable to bearer
- Transferable from one person to another by endorsement and delivery, if payable to order.

3) Transferee can sue in his own name

- It implies the right of the creditor to recover something from his debtor.
- Creditor can either recover this amount himself or can transfer his right to another person.
- Transferee is also entitled to sue on the instrument in his own name in case of dishonour, without giving notice to the debtor of the fact that he has become holder.

4) Title of holder in due course¹⁴⁹

- Once an instrument is received in the hands of holder in due course it becomes free from all defects.

5) Presumptions

Following presumptions are there, unless the contrary is proved;

- Every negotiable instrument was made, drawn, accepted, endorsed or transferred for **consideration**.
- Every negotiable instrument bearing a date was made or drawn on such **date**.
- Every bill of exchange was accepted **within a reasonable time** after its date and before its maturity.
- Every transfer of a negotiable instrument was **made before its maturity**.
- The **endorsements** appearing upon a negotiable instrument were made in **the order in which they appear**.
- A lost negotiable instrument was duly **stamped**.
- A holder of negotiable instrument is a **holder in due course**
(except any offence, fraud or unlawful consideration is proved)

Parties to negotiable instrument

Maker

The person who makes a promissory note.

Payee

The person named in an instrument, to whom or to whose order money is to be paid.

Drawer

The maker of a bill of exchange or cheque.

Drawee

The person on whom bill of exchange or cheque is drawn and who is directed to pay the amount.

Acceptor

A bill of exchange (other than a cheque) must be presented to drawee for acceptance first, and then presented for payment on due date. Drawee becomes acceptor when he accepts the bill duly signing it.

Holder

A person is called **holder** of a negotiable instrument if he satisfies following two conditions:

- He must be entitled to the possession of the instrument in his own name and
- He must be entitled to receive / recover the amount due on the instrument from the parties liable under the instrument

So holder means bearer of the bearer instrument and endorsee or payee of the order instrument.

When the note, bill or cheque is lost and not found or is destroyed, the person in possession of it or the bearer at the time of loss or destruction shall be deemed to continue to be its holder.

Holder in due course

A person becomes holder in due course when he fulfills the following conditions

- He must be a holder.
- There must be a lawful and adequate consideration.
- A person should receive the instrument before its maturity.
(For instrument payable on demand, he must have taken it within reasonable time of issue)
- The instrument must be Complete and regular.
(It is duty of every holder in due course to examine the form and contents of instrument to ensure that it does not contain any unauthorized material alteration or incompleteness)
- He should take the instrument without any negligence on his part and in good faith without having any reason to believe that any defect existed in the title of the transferor.

	Holder	Holder in due course
Meaning	A person who legally obtains the negotiable instrument, with his name entitled on it, to receive the payment from the parties liable.	A person who acquires the negotiable instrument bona fide for some consideration, whose payment is still due.
Consideration	Not necessary.	Necessary.
Right to sue	May not sue all prior parties.	Can sue all prior parties.
Good Faith	Instrument may or may not be obtained in good faith.	Instrument must be obtained in good faith.
Better title	May not get title free from defects.	Gets a better title than that of the transferor.
Maturity	Can become holder, before or after the maturity of the negotiable instrument.	A person can become holder in due course, only before the maturity of negotiable instrument.

Types of instrument

Order instrument

- Which is expressed to be so payable; or
- Which is expressed to be payable to a particular person and does not contain words:
 - which prohibit transfer, or
 - indicate an intention that it shall not be transferable.

Bearer instrument

- Expressed to be so payable; or
- Last endorsement must be an endorsement in blank.

Inland instrument

- Made or drawn in Pakistan and also made payable in Pakistan, or
- Made or drawn in Pakistan upon any person resident in Pakistan, although it may be payable in a foreign country.

An inland instrument remains inland even if it has been endorsed in a foreign country.

Foreign instrument

An instrument, which is not an inland instrument, is deemed to be a foreign instrument.

Demand instrument

- The instrument in which no time for payment is mentioned.
- A cheque is always payable on demand.
- A promissory note or bill of exchange is payable on demand where:
 - It is expressed to be so;
 - It is expressed to be payable "at sight" or "presentment"; or "on demand";
 - No time for payment is specified; or
 - The bill or note accepted or endorsed after it is overdue, as regards to person accepting or endorsing it.

Time instrument

- An instrument payable after a fixed time or on a specified date
- A cheque cannot be a time instrument
- Promissory note or bill of exchange is time instrument when it is expressed to be payable:
 - After a specified period
 - On a specific day
 - Certain date after sight
 - On the happening of event which is certain to happen e.g. death.

Endorsement**Endorsement**

"When the maker or holder of a negotiable instrument signs the same, otherwise than as such maker, for the purpose of negotiation on the back or face or on a slip of paper annexed to it thereto, or so signs for the same purpose a stamped paper intended to be completed as negotiable instrument he is said to endorse the same and is called the endorser."

Essentials of valid endorsement

- It must be on instrument itself, if no space is left on the back of the endorsement, further endorsements are signed on a slip of paper attached to the instrument.
- It must be signed by the endorser for the purpose of negotiation.
- No particular form of words is necessary for an endorsement
- It must be completed by the delivery of the instrument.
- Negotiation by endorsement must be of the entire instrument

Negotiation

"When a promissory note, bill of exchange or cheque is transferred free from defects to any person, so as to constitute that person the holder of it, the instrument is said to be negotiated."

Payment in due course

Payment in accordance with the apparent tenure (period expressly written) of the instrument in good faith and without negligence to any person in possession of it.

- The payment must be in accordance with the apparent tenure of the instrument.¹⁵⁰
 - It should be made at or after maturity.
 - A payment before maturity is not a payment in due course
- The payment must be made in good faith and without negligence.¹⁵¹
- The payment must be made to a person in possession of the instrument under circumstances which do not arouse the suspicion about his title to possess so.
- The payment must be made in money only
(unless holder agrees to accept payment in any other medium i.e. by cheque or draft)

PROMISSORY NOTE

Promissory note

"A promissory note is an instrument in writing (not being a bank note or currency note) containing an unconditional undertaking, signed by the maker, to pay on demand or at a fixed or determinable future time a certain sum of money only, or to the order of a certain person, or to the bearer of the instrument."

Following are the two main parties in a promissory note:

- **Maker** Who makes the promissory note and promises to pay the money stated in it.
- **Payee** To whom the promise to pay is made.

Specimen of a promissory note

Date: September 15, 2013	
Rs. 10,000/- only	
Three months after date I promise to pay ABC or to his order the sum of Rupees Ten Thousand, for value received	
To ABC (payee) Jail Road Lahore	Sign: _____ XYZ (maker) Saddar Karachi

Essential elements of a promissory note

In writing¹⁵²

- An oral promise to pay does not become a promissory note.
- Words must convey a clear undertaking to pay (use of words "promise" is not necessary)

Promise to pay¹⁵³

- A mere acknowledgement of indebtedness is not a promissory note

Definite and unconditional¹⁵⁴

- Promise must not depend upon the happening of some uncertain event
- But a promise to pay is not conditional if the amount is made payable
 - at a particular place or
 - after a specified time or
 - on happening of an event which must happen

Signed by maker

- Promissory note should be duly authenticated by the signature of the maker.
- If the maker is illiterate, he may place his thumb mark.

Certain parties

- Instrument point out with certainty as to who is the maker and who is the payee.
- If parties cannot be identified with certainty, the instrument is not a promissory note.
- A promissory note cannot be made payable to the maker himself.

Sum payable must be certain

- Amount payable must not be capable of contingent addition or subtraction

Sum payable must be legal tender

- A promise to pay a certain amount of foreign or to deliver a certain quantity of goods is not a promissory note. Thus, an instrument signed by A, "I promised to pay B Rs.500 and to deliver him my black horse" is not a valid promissory note.

BILL OF EXCHANGE**Bill of exchange**

"A bill of exchange is an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay on demand or at a fixed or determinable future time a certain sum of money only, to or to the order of, a certain person, or to the bearer of the instrument."

Following are the three main parties in a bill of exchange:

- **Drawer** It is a person who draws a bill of exchange.
- **Payee** It is a person to whom the amount of bill of exchange is payable.
- **Drawee** It is a person who is ordered to pay the amount of the bill of exchange
(When drawee accepts the bill of exchange he is called the acceptor)

Specimen of a bill of exchange

Date: September 15, 2013	
Rs. 10,000/- only	
Three months after date pay to XYZ (payee) or to his order the sum of Rupees Ten Thousand, for value received.	
Accepted ABC (drawee)	
To	<div style="float: right; text-align: right;">Sign: _____ MNO (drawer) Saddar Karachi</div> <div style="clear: both;"></div> ABC Jail Road Lahore

Essential elements of a bill of exchange

- In writing
- Order to pay
(Should not be a request to pay)
- Definite and unconditional
- Signed by drawer and drawee
- Certain parties
- Sum payable must be legal tender
- Sum Payable must be certain

Differences between promissory note and bill of exchange

	Promissory note	Bill of exchange
No of parties	2 parties (maker and payee)	3 parties (drawer, drawee & payee)
Same person	Maker cannot be the payee (same person cannot be both the promisor and the promisee)	Drawer and the payee may be one and the same person (e.g. "Pay to me or my order")
Tone	Promise to make the payment.	Order for making the payment.
Acceptance	Requires no acceptance	Needs acceptance by drawee before it is presented for payment.
Nature of liability	Liability of maker is primary and absolute.	Liability of a drawer is secondary and conditional. It arise only when the acceptor does not honour the bill
Maker's position	Maker stands in immediate relation with the payee.	Drawer stands in immediate relation with the acceptor and not the payee.
Notice of dishonour	No notice of dishonour is required to be given to the maker.	Notice of dishonour must be given by the "holder" to all prior parties (including drawer and endorser)

CHEQUE**Cheque**

Cheque is a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand.

Following are the three main parties in a cheque:

- **Drawer** It is a person who draws a cheque.
- **Drawee** It is a banker who is ordered to pay the amount of the cheque.
- **Payee** It is a person to whom the amount of cheque is payable.

Specimen of a cheque

ABC Bank Limited Main Branch, Karachi	Date: September 15, 2013 Cheque no: _____
Pay _____ OR BEARER	
Rupees _____	Rs.
Account no: _____	
Title of account _____	
Do not write below this line	Signature _____

Essential elements of a cheque

- In writing
- An express order to pay
(not a request to pay)
- Definite and unconditional
- Signed by the drawer
- Certain parties (drawer, drawee and payee)
- The order must be to pay a certain sum
- The order must be to pay money only
- It must always be drawn upon a specified banker
- It must always be payable on demand

Crossing

- A cheque is said to be crossed when it bears across its face two parallel transverse lines which are usually drawn on the left hand top corner of the cheque.
- Purpose of crossing is to direct the drawee (banker) to pay the amount only to a banker (so that the party who receives the payment can easily be traced)

Types of crossing

Type	How to Cross	Effects
General Crossing	An addition of words "and company" or any abbreviation of it between two parallel transverse lines.	Drawee shall not pay it otherwise than to a banker.
Special crossing	Where it bears across its face an addition of the "Name of the banker" (Parallel lines are not necessary)	Drawee shall not pay it otherwise than to a banker to whom it is crossed or his agent for collection.
Restrictive crossing	May be added with general crossing by adding the words "A/c Payee" or "A/c Payee only"	The amount collected on the cheque must be credited only to the account of payee.
Not negotiable crossing	May be added with general crossing or special crossing by adding the words "Not negotiable"	A holder with a defective title cannot give a good title to a subsequent holder. It does not restrict the further transfer ability. It only takes away main feature of negotiability (i.e. a transfer free from defects)

Crossing of a cheque after issue

Case	Right to cross
Cheque is uncrossed	Holder may cross it generally or specially.
Cheque is crossed generally	The holder may cross it specially by adding the name of the banker.
Cheque is crossed generally/specially	Holder may add the word "Not negotiable" .
Cheque is crossed specially	Banker to whom it is crossed may again cross it specially to another banker (his agent) for collection

Rules regarding payment of Cheques

- If cheque is crossed specially to more than 1 banker (except when crossed to an agent for collection), banker to whom it is drawn shall refuse payment
- If banker, on whom a cross cheque is drawn, makes a payment in due course, paying banker and drawer positioned as if cheque had been paid to and received by the true owner thereof.
- If banker, on whom a cross cheque is drawn, makes a payment out of due course, the paying banker shall be liable to true owner of cheque for any loss he may sustain for that payment

Protection to the collecting banker

If the collecting banker has collected a cheque on behalf of a person whose title to the cheque was defective, he would be protected and would not be held liable, provided he proves that:

- He acted in good faith and without negligence
- The cheque was already crossed before it reached his hands and
- He received the payment on behalf of a customer and not on his own account

Also, if collecting banker has collected a cheque which does not appear to be crossed "account payee", banker, in good faith and without negligence collecting payment of cheque and crediting proceeds thereof to a customer, shall not incur any liability.

Revocation of banker's authority

Duty and authority of a banker to pay a cheque drawn on him by customer are determined by:

- Countermand (Stopping) of payment;
- Notice of customer's death;
- Notice of adjudication of the customer as an insolvent

Differences between Cheque and Bill of exchange

	Cheque	Bill of exchange
Drawee	Always drawn on a banker.	May be drawn on any person, including a banker.
Payable on demand	Can only be payable on demand.	May be payable on demand or on expiry of a certain period after date or sight.
Payable to bearer on demand	A cheque drawn "payable to bearer on demand" is valid.	A bill drawn "payable to bearer on demand" is absolutely void (can be done later by endorsement in blank).
Acceptance	Does not require any acceptance	Requires acceptance by the drawee before he can be made liable upon it.
Stamp	Does not require any stamp.	Must be properly stamped.
Crossing	May be crossed for safety.	Cannot be crossed.
Stopping the payment	Payment may be stopped by the drawer.	Payment cannot be stopped by the drawer.
Noting or protest	No system of Noting or protest.	May be noted or protested for dishonour.

CH # 11

INTRODUCTION TO COMPANY & INCORPORATION

FEATURES OF A COMPANY

Sole trader

- An individual who owns and runs his or her own business.
- The law does not recognize the business as a separate person
- The person is personally liable for the debts of the business

Partnership

- Group of individuals who own and run their own business.
- A partnership business is not recognized as a 'person' by the law.
- Partners are personally liable jointly with other partners for debts

Companies

- Capital of a company is represented by shares
- Ordinary shareholders are its owners.
- Created by a process established by Companies Act 2017
- Company is a legal person, separate from its owners.
(doctrine of corporate personality)
- Companies are managed by their directors

Distinguishing Features of Company

Separate legal personality

- Company can enter into contracts with other persons
- A company owns its own assets
- A company is personally liable to pay tax on its income (profits).

Limited liability

- The liability of the owners of a company for the debts of the company is limited to the amount of their investment in the company.

Transfer of ownership and perpetual succession

- Any legal person can own shares in a company (even another company can own shares)
- Shareholders can transfer their share in the ownership of the company to someone else,
- It does not affect the legal status or legal existence of company.
- Company continues to exist (unaffected by change in ownership)

Law and governance of a company

Relevant Law	Companies are created by a process established by Companies Act, 2017
Memorandum of association (MOA)	Constitutional document that focuses on external stakeholders is called memorandum of association
Articles of association (AOA)	Bye-laws which focuses on internal procedures of company

TYPE OF COMPANIES**Company**

A Company formed and registered under this Act or the company law.

Company law

The repealed Companies Act, Companies Ordinance, 1984, Companies Ordinance, 2016 and also includes this Act unless the context provides otherwise

Body corporate "or" Corporation

Body corporate or corporation includes

- a company incorporated under this Act or company law;
- a company incorporated outside Pakistan, or
- a body corporate declared as body corporate in the relevant statute

but does not include

- A co-operative society registered under any law relating to the registration of co-operative societies; or
- Any other entity, not being a company as defined in this Act or any other law for the time being which the concerned Minister of the Federal Government may, by notification, specify in this behalf.

Companies limited by shares

Liability of its members is limited by the memorandum to the extent of amount, if any, remaining unpaid on the shares respectively held by them.

Companies limited by guarantee

Liability of owners is limited to the amount member guarantees to contribute in the event that the company goes into liquidation

- The company may or may not have share capital
- If Company has share capital; Liability shall also include amount unpaid on shares (if any)

Unlimited companies

This has all advantages of a normal company except that, liability of its members is not limited

Private company and public company

Public Company

A company which is not a private company

Listed Company

Whose securities are listed on stock exchange and are traded on it

Unlisted Company

Whose securities are not listed on stock exchange

Private Company

Single Member Company

Which consists of a single member who is director of the company.
[In these companies (SMC-PVT) Limited is added to the name]

Other Private Company

Company can be registered by at least two members and it restricts

- Maximum number of members to 50
(members jointly holding shares shall be counted as 1 member)
- Right to transfer the shares by its members,
- Invitation of subscriptions from general public for its shares debentures or Redeemable capital.

Holding Company & Subsidiary Company

Holding Company

Means a company which is another company's holding company if, but only if, that other company is its subsidiary.

Subsidiary company

In relation to any other (holding) company, it means company in which the holding company:

- Holds the Composition of the Board; or
- Exercise or controls more than one-half of its voting securities either by itself or together with one or more of its subsidiary companies

Notes

- Subsidiary of a subsidiary company would also be considered subsidiary company of the main holding company
- Composition of board is normally controlled by another company if it can appoint or remove all or a majority of directors (by exercise of power available to it)

AUTHORITIES, OFFICIALS, MEMBERS AND RESOLUTIONS**SECP (Securities & Exchange Commission of Pakistan)**

- SECP was operationalized on 1st January 1999.
- SECP replaced Corporate Law Authority
- SECP's head office is at Federal Capital, Islamabad
- SECP has 8 regional offices
 - 1 at Federal Capital
 - 4 at provincial capitals
 - 3 in other major cities i.e. Multan, Faisalabad and Sukkur.
- SECP has been given lot of powers under Companies Act
- SECP regulate the affairs of Companies, Insurance Companies, Banking Companies, Modarbas & Non-Banking Finance Companies
- Law has vested various powers to SECP
- In addition to Companies Act 2017, SECP is also empowered by SECP Act, 1997 to exercise many powers and functions.

Registrar

Means a registrar, an additional registrar, an additional joint registrar, a joint registrar, a deputy registrar, an assistant registrar or such other officer as may be designated by SECP, performing duties and functions under this Act.

Powers and duties

- Registration of companies
- Receiving various documents under the Act.
- Keeps track of company routine documents
- Can call the officers of company for information and explanations
- Empowered to inspect the books and records of the company.
- May seize the books and records, if think necessary

Officials**Officer**

Includes any director, chief executive, chief financial officer, company secretary or other authorised officer of a company.

Board

in relation to a company, means board of directors of the company

Members

Subscribers to memorandum of association are deemed to have agreed to become members of the company and become members on its registration and every other person-

- to whom is allotted, or who becomes the holder of any class or kind of shares; or
- in relation to a company not having a share capital, any person who has agreed to become a member of the company;

and whose names are entered; in the register of members, are members of the company.

Types of Resolutions

Ordinary Resolution

A resolution passed by a simple majority of such members of the company entitled to vote as are present in person or by proxy or exercise the option to vote through postal ballot, as provided in the articles or as may be specified, at a general meeting

Special resolution

A resolution

- which has been passed by a majority of not less than $\frac{3}{4}$ th of such members entitled to vote as are present in person or by proxy or through postal ballot at a general meeting
- of which not less than 21 days notice specifying the intention to propose the resolution as a special resolution has been duly given:

Note: if all the members entitled to attend and vote at any such meeting so agree, a resolution may be proposed and passed as a special resolution at a meeting of which less than twenty-one days notice has been given

ASSOCIATION NOT FOR PROFIT

SECP shall grant license if following conditions are fulfilled

- Such association may be set up for any of the following purposes
 - Commerce
 - Arts
 - Science
 - Religion
 - Health,
 - Education,
 - Research,
 - Sports
 - Environment Protection
 - Social Welfare
 - Charity
 - Any other useful object
- It shall apply its profits (if any) in promoting its objects
- It shall prohibit the payment of any dividend to its members and
- Its objects and activities are not and shall not, at any time, be against the laws, public order, security, sovereignty and national interests of Pakistan

SECP shall grant license on such conditions and subject to such regulations as it thinks fit.

Association shall enjoy all privileges of a limited company and be subject to all its obligations, except using the ending word(s) "Limited" or "(Guarantee) Limited"

License may be revoked at any time by SECP

- SECP shall give a notice in writing to Co, of its intention to do so
- SECP shall provide an opportunity to be heard to the association.

On revocation, registrar shall again add the ending words and it shall cease to enjoy exemptions and privileges granted by license.

Conditions for Revocation of the Licence

- Company/management has failed to comply with any terms or conditions of licence;
- Any of the requirements of this section or any connected regulations are not met;
- Affairs of company are conducted in a manner prejudicial to public interest; or
- Company has made a default in filing with registrar its financial statements or annual returns for immediately preceding 2 consecutive financial years;
- Company has acted against the interest, sovereignty and integrity of Pakistan, the security of the State and friendly relations with foreign States;
- Number of members is reduced, below 3;
- The company is
 - Conceived or brought forth for unlawful or fraudulent activities;
 - Run and managed by persons who fail to maintain proper and true accounts or they commit fraud, misfeasance or malfeasance in relation to the company;
 - Run and managed by persons involved in terrorist financing or money laundering;
 - Managed by persons who refuse to act according to MOA or AOA or provisions of this Act or failed to carry out directions or decisions of SECP or the registrar; or
 - Not carrying on its business or is not in operation for 1 year; or
- It is just and equitable that the licence should be revoked:

Effect of revocation of Licence

- Company shall stop all its activities except the recovery of money owed to it, if any;
- Company shall not solicit or receive donations from any source; and
- All the net assets of the company shall, in a specified manner, be transferred to another company licensed u/s 42, preferably having similar or identical objects, within 90 days of revocation or any extended period (if allowed by the SECP)
- A reasonable amount to meet expenses of voluntary winding up or making an application to the registrar for striking off the name may be retained by the company.
- After such transfer, the members and officers of the first company or any of their family members shall not be eligible to hold any office in later company for next 5 years.
- After compliance of above requirements, BOD shall file within 15 days, a report to registrar containing such information and documents as may be specified.
- Within 30 days of acceptance of the report by registrar BOD shall
 - Initiate necessary proceedings for voluntary winding up; or
 - Make an application to registrar for striking the name of company off the register (if it has no assets and liabilities)
- If requirements not complied with on a timely basis; SECP may appoint an administrator to manage affairs of company and initiate proceedings for winding up.

INCORPORATION (REGISTRATION) OF A COMPANY

Steps of Incorporation

- Getting availability of suitable name from registrar
- Preparing MOA and AOA with supporting documents
- Filing documents (along with application for registration) with registrar
- Obtaining the "certificate of incorporation" of company

Registration of MOA & AOA

- A declaration of compliance shall also be filed with MOA & AOA (Compliance with requirements regarding incorporation of Co)
- Registrar shall register MOA & AOA only if it satisfied that
 - Company is being formed for lawful purposes,
 - All requirements of this Act and associated rules have been complied with
- If registrar think that any document or information contains any matter contrary to law or is not complete
 - He may require revised document or to remove deficiencies within specified period.
 - If applicant fails to remove deficiencies, registrar may refuse registration of company
 - Co may file an appeal before SECP within 30 days of refusal.
 - Order of SECP, on such appeal, shall be final.

Certificate of Incorporation

- Registrar shall issue certificate of registration signed by him.
- The certificate of incorporation shall state
 - Name and registration number of company;
 - Date of its incorporation;
 - Whether it is a private or a public company;
 - Whether it is a limited (shares or guarantee) or unlimited;

Effect of registration

- Subscribers to MOA and subsequent members are body corporate by the name stated in the certificate of incorporation;
- It is capable of exercising all the functions of an incorporated company, having perpetual succession and a common seal
- Status and registered office are as stated in application
- Subscribers become holders of initial shares (if applicable)
- Persons named in AOA as proposed directors are appointed.

CH # 12**MEMORANDUM AND ARTICLES****MEMORANDUM OF ASSOCIATION (MOA)****Clauses of MOA****Name Clause**

Name of company with following last word

- | | |
|-------------------------|-------------------------|
| - Public Co: | "Limited" |
| - Private Co: | "(Private) Limited" |
| - Single Member Company | "(SMC-Private) Limited" |
| - Guarantee Ltd | "(Guarantee) Limited" |
| - Unlimited: | "Unlimited" |

Registered Office Clause

Province or part of Pakistan not forming part of a province
in which registered office is to be situated)

Principal line of business Clause

- Principal line of business will be mentioned in MOA
- It shall be matching with its name

Principal line of business" means the business in which substantial assets are held or likely to be held or substantial revenue is earned or likely to be earned by a company, whichever is higher.

- A company may carry on any lawful business or activity and do any act or enter into any transaction connected to it which is necessary in attaining its business activities.
- A company shall not engage in a business which is:
 - Prohibited by any law for the time being in force in Pakistan; or
 - Restricted by any law, rules or regulations(unless necessary licence, registration, permission or approval has been obtained)

Existing companies (those registered before Companies Act, 2017 was effective) may continue with their existing MOA and their object clause be treated as the principal line of business

Liability Clause**Company Limited by Shares**

"Liability of the Members is limited"

Company Limited by Guarantee

'Liability of the members is limited'.

An additional sentence is also added to clarify the extent of liabilities of the members of that company in the event of its being wound up.

Unlimited Company

"Liability of the Members is unlimited"

Authorised Share Capital Clause

Amount of share capital with which Co proposes to be registered, and the division into shares of a fixed amount

- Every subscriber of MOA is required to take at least one share
- Each subscriber shall write opposite to his name the number of shares he has agreed to take
- For company limited by guarantee, this clause shall not be included if company has no share capital

Undertaking Clause

The company shall add an undertaking, as may be specified by SECP.

Subscription Clause

Subscribers shall

- Write their names addresses and other required particulars
- Write following sentence:

"We, the several persons whose names and addresses are subscribed, are desirous of being formed into a company, in pursuance of the memorandum of association, and we respectively agree to take the number of shares in the capital of the company set opposite our respective names"

- Sign MOA in presence of at least one witness (witness shall also write his particulars)

Printing and signature of MOA & AOA

MOA and Articles shall be

- Printed
- Divided into paragraph numbered consecutively
- Dated
- Signed by each subscribers giving following details in presence of a witness (who shall attest signature and add his particulars also)
 - Present Name in full
 - Occupation
 - Fathers Name
(Husband name in case of married/ widow women)
 - Nationality
 - Usual residential Address
 - Others particulars as may be prescribed

Every Co, upon request and payment of a prescribed amount by its member, shall supply within 14 days a copy of MOA & AOA of the company.

Borrowing powers to be part of memorandum

MOA & AOA is deemed to include (implied) power to enter into any arrangement for obtaining loans, advances, finances or credit, and to issue other securities not based on interest for raising resources from a scheduled bank, a financial institution or general public

NAMES**Restrictions on Names****Prohibited Names**

- Containing word or expression notified by SECP;
- Inappropriate, undesirable or deceptive (in the opinion of SECP)
- Designed to exploit or offend religious sentiments of people.
- Identical with name of a company already registered
- Nearly resembling that name of a company already registered

Names which require prior approval of SECP

Prior approval of SECP required if proposed name suggest

- Patronage of any, past/present, Pakistani/foreign, Head of State
- Any connection with Federal Govt. or Provincial Govt. or any department or authority of any such Government;
- Any connection with any corporation set up by or under any Federal or Provincial law; or
- Patronage of, or any connection with, any foreign Government or any international organization.
- Establishing a modaraba management Co or to float a modaraba
- Any other business requiring a license from the government

Application for reservation of a name

- A person may make an application in specified form and manner with a specified fee, to the registrar for reservation of any name
- Reservation can be made for a period of maximum 60 days.
- If it is found that a name was reserved, by furnishing false or incorrect information
 - Such reservation shall be cancelled
 - The person making application shall be liable to a penalty.
 - If the company has been incorporated, it shall be directed to change its name.
- If application is refused by registrar, aggrieved person may within 30 days of the order of refusal prefer an appeal to SECP.
- Order of SECP shall be final and shall not be called in question before any court or authority

Change & Rectification of Name

Rectification of Name

- If wrong name selected by Co,
 - It may change name with the approval of registrar; and
 - It shall change name within 30 days if registrar directs so.
- Registrar shall, before issuing direction for change of name, give Co an opportunity of being heard
- If company fails to comply with above direction, registrar may
 - Register company under a new name selected by him, and
 - Issue a certificate of incorporation on change of name

Change of Name

- Special Resolution
- Approval of registrar.

No approval required if addition or deletion of words "(Private), (SMC-Private), (Limited) or (Guarantee Limited) or (Unlimited))

Effect of Change of Name

- Registrar shall enter the new name on register in place of old one.
- Registrar shall issue a new certificate of incorporation altered to meet the circumstances
- Continue to mention former name along with its new name outside every business place and in all documents (for 90 days from date of issue of new certificate)
- Change of name shall not affect the rights & obligations of Co.
- Legal proceeding may be continued against Co in new name

Publication of Name

- Name and incorporation number of every limited company shall be displayed outside company's every office or place of business in a conspicuous position.
- Company shall display a certified copy of certificate of incorporation at every place of business
- Name, address of registered office, telephone, fax number, e-mail and website addresses, if any, shall be mentioned on all documents appeared to be the documents of company.
- Level 1 Penalty on company and its officers for not displaying name in manner provided.
- Officer shall be personally liable for debt of company if he issue / authorize any document without mentioning the name of company (unless debt paid by the company itself)

REGISTERED OFFICE AND PRINCIPAL LINE OF BUSINESS**Registered office of a company**

- It is a single place which is the address of company for receiving all communications.
- It does not necessarily be same as head office of the company.
- A company shall have a registered office and its address shall be notified to the registrar within 30 days of its incorporation.
- Any change in such address shall be notified to registrar within 15 days of change:

Alteration of Registered Office clause in MOA

- Company may by special resolution alter its MOA to change its registered office from:
 - One Province to another Province or Islamabad Capital Territory and vice versa; or
 - One Province or Islamabad Capital Territory to a part of Pakistan not forming part of a Province and vice versa.
- Company shall apply to SECP for obtaining its approval
- When company actually shifts its registered office, it shall inform the registrar within 15 days of the date of such shifting.
- Where alteration involves a transfer of registered office from jurisdiction of one company registration office to another, physical record of company shall be transferred to the other registrar (where the registered office has been shifted)

SECP Approval for alteration

- SECP must be satisfied that
 - Circumstances for alteration of object/registered office exists
 - Sufficient disclosure has been given to every creditor and member of the company
- SECP may make an order confirming alteration either wholly or in part, and on such terms and conditions as it thinks fit.
- A copy of duly certified order of SECP shall be forwarded to the company and to registrar within 7 days from the date of the order.
- A certified copy of SECP's order and a printed copy of altered MOA shall be filed with registrar within 30 days of order
(May be extended by SECP)
- Registrar shall register it and issue a certificate

Alteration of Principal Line of Business clause

- Company may by special resolution alter its MOA to Change its principle line of business
- Such alteration shall not require confirmation by SECP
- Company shall file amended MOA with registrar within 30 days on specified form
- Registrar may give direction of change of name if change does not match with principal line of business of the company.

Note: For adopting any business activity which is subject to licence, registration, permission or approval under any law, company would follow the process of change in Registered office clause.

ARTICLES OF ASSOCIATION (AOA)

Byelaws of company, subordinate to constitution (MOA) and further subordinate to the Act, guiding day to day issues faced by a company.

- It is option for company limited by shares to
 - Get the articles registered; or
 - Adopt Table A (first schedule of Companies Act 2017)
- For other companies Registration of AOA is compulsory.
- For Guarantee Ltd or Unlimited Co, AOA shall state:
 - Amount of share capital at time of registration (If it have share capital)
 - Number of members at time of registration (If it does not have share capital)
- AOA shall list and specify the voting and other rights attached to different classes of shares and securities.
- If company contravenes its AOA, company and every officer shall be liable to a penalty

Contents of Table A

Details related to following areas are given in Table A so that companies may adopt it as it is:

- Restriction related to commencement of business
- Shares
- Transfer and Transmission of Shares
- Form for Transfer of Shares
- Bank Account Details of Transferee for Payment of Cash Dividend
- Transmission of Shares
- Alteration of Capital
- General Meetings
- Notice and Proceedings of General Meetings
- Votes of Members
- Instrument of Proxy
- Directors
- Powers and Duties of Directors
- Minute Books
- The Common Seal of company
- Disqualification of Directors
- Proceedings of Directors
- Filling of Vacancies
- Dividends and Reserve
- Accounts
- Mode of giving notices to members
- Winding Up
- Indemnity for officers and agents of the company

Applicability of Table A

- Table A is applicable in full, if articles are not registered separately.
- Table A is applicable to the extent not modified or excluded by articles filed by a company.
- Table A is not applicable at all, if specifically excluded by articles filed by a company.

Alteration in the articles of association

- Company may, by special resolution, alter its AOA
- Any alteration shall be as valid as if originally contained in AOA
- If alteration affects substantive rights or liabilities of members or class of members, it shall be carried out only if majority of at least 3/4th of those affected vote for that (personally or through proxy)
- A copy of altered AOA shall be filed with registrar within 30 days
- Registrar shall register the same.

GENERAL PROVISIONS AS TO MEMORANDUM AND ARTICLES

Effect of memorandum and articles

- Upon registration, MOA and AOA shall bind the company and the members (just like that they all have signed it)
- All moneys payable by a subscriber against the shares subscribed shall be a debt due from him and be payable in cash within 30 days from the date of incorporation.
- If share money is not deposited within prescribed time
 - Shares shall be deemed to be cancelled
 - Name of that subscriber shall be removed from the register
 - Registrar shall give such direction to company as deemed appropriate.
- Receipt of subscription money from subscribers shall be reported by company to registrar on a specified form within 45 days from date of incorporation, accompanied by a certificate by a practicing CA or a CMA verifying receipt of the money so subscribed.
- Any violation of this section shall be an offence liable to a penalty of level 1

Alteration to be noted in every copy

- If an alteration is made in MOA/AOA, every copy of MOA/AOA issued after the date of alteration shall contain that alteration
- In case of contravention, company and every officer in default shall be liable to the penalty

Form of MOA & AOA

Type of company	Document	Form
Company limited by shares	AOA	Table A
	MOA	Table B
Company limited by guarantee and not having a share capital	AOA & MOA	Table C
Company limited by guarantee and having a share capital	AOA & MOA	Table D
Unlimited company having a share capital	AOA & MOA	Table E
Company licensed under section 42 (Association not for profit)	AOA & MOA	Table F

CH # 13**MANAGEMENT****DIRECTORS****Director**

Includes any person occupying the position of a director, by whatever name called

- Only natural persons to be directors
- Directors act collectively or by majority
- Every director has got one vote in a directors meeting.
- Director cannot be a variable representative
(cannot claim relief from responsibility as a director in any particular area of business)

Directors in fiduciary relationship

- Directors are agents of the company
- They are supposed to make decisions in best interest of company
- They must be vigilant and should not be negligent in their duties

Minimum number of directors of a company

SMC	→	At least 1
Other private	→	At least 2
Public (unlisted)	→	At least 3
Public (listed)	→	At least 7

*No person shall be a director (including alternate director) at same time in more than such number of companies as may be specified
(this limit shall not include the directorships in a listed subsidiary)*

Consent to act as director

- No person shall be elected or appointed as a director or chief executive if he has not filed his consent in writing
- Company shall file such consent to registrar within 15 days of the date of appointment or election of director or chief executive

Ineligibility of certain persons to become director

- Minor;
- Unsound mind;
- Has applied to be adjudicated as an insolvent and his application is pending;
- Undischarged insolvent;
- Has been convicted by a court of law for an offence involving immoral behaviour;
- Has been debarred from holding such office under any provision of this Act;
- Has betrayed lack of fiduciary behaviour at any time during preceding 5 years;
- Does not hold the NTN as per Income Tax Ordinance 2001
- Not a member except
 - Person representing a member who is not a natural person
 - Whole-time director who is an employee of the company;
 - Chief Executive
 - Person representing a creditor or other special interests through contractual arrangement

Additional Ineligibilities only for Listed Co

- Declared by Court of competent jurisdiction as **defaulter in repayment of loan** to a financial institution
- Engaged in **business of brokerage**, or is spouse of such person or is sponsor, director or officer of a corporate brokerage house

If any person being an undischarged insolvent acts as chief executive or director of a company, he shall be liable to imprisonment for a term not exceeding 2 years or to a fine, or to both.

DIFFERENT TYPE OF DIRECTORS

First directors

- Names & number of first directors shall be decided by subscribers
- Their particulars shall be submitted along with the documents for incorporation.
- Additional directors may also be appointed in general meeting
- 1st directors shall retire at first AGM

Elected Director and the process of election

In first AGM, all first directors shall retire and election of directors shall be held. Afterwards election shall be held after every 3 years.
(Company limited by guarantee may reduce the period through AOA)

Process of Election

- Directors of Co shall, **fix No of elected directors** at least 35 days before general meeting at which directors are to be elected
(Number shall not be changed except prior approval of members)
- **Notice of meeting** shall expressly state-
 - No of elected directors fixed; and
 - Names of retiring directors.
- Any person who seeks to contest in election of director shall (whether he is a retiring director or otherwise), file with company a notice of his intention at least 14 days before meeting
 - Notice may be withdrawn at any time before election
 - All such notices shall be transmitted to the members at least 7 days before meeting
 - For listed: Notice also published in 1 Urdu & 1 English newspaper, in respective language, having wide circulation

For companies not having share capital

Elected by members in general meeting in manner provided in AOA.

For companies having share capital

(Where No of contestants are more than No of directors fixed)

- $\text{Votes} = \text{No of voting shares/securities} \times \text{No of directors (seats)}$
- Member may give all votes to 1 candidate or may divide votes between the contestants
- Candidate getting highest votes elected as director and then candidate getting next highest votes shall be so declared and so on until total directors elected.

Circumstances in which election may be declared invalid

Court may, declare election of all directors or any of them invalid if satisfied that there has been material irregularity in procedures.

- On application of members having at least 10% voting power
- Within 30 days of the date of election

Any act of director, or of meeting of BOD attended by him, shall not be invalid only due to any defect (subsequently discovered) in appointment

Nominee directors

By Creditors

- Creditors may also nominate directors on the board (if they are empowered to do so by virtue of any agreement)
- Such directors are in addition to minimum number of directors fixed by Act.

By Federal Govt., Provincial Govt. or Investor company

- Federal government, provincial government and any investor company (holding shares in other company) can nominate any person to represent them as director in that company
- Such person shall be considered to be 'elected director' (deemed)
- Shall be considered for calculation of minimum number

Fresh election on request of substantial acquirer

- If a person acquires requisite shareholding to get him elected as a director, he may require the company to hold fresh election.
- Number of directors fixed in last election shall not be decreased
- Board shall as soon as practicable within 30 days, proceed to hold such fresh election.
- Listed company shall follow such procedure as may be specified by SECP for such election

Casual Vacancy

- If directors resign earlier from the office (before 3 years), casual vacancy shall be filled by remaining directors.
- In listed company it shall be filled at the earliest but not later than 90 days from the date of vacancy.
- For others no time limit specified in Act for filling of casual vacancy, nor it is mandatory (unless number of directors falls below minimum)
- Casual vacancy shall be appointed for remainder term

REMOVAL OF DIRECTORS

Directors can be removed

- By Members (through resolution)
- By operation of Law (vacation of office)

Removal of directors by members

Members may remove directors through resolution in their meeting

However, the resolution shall not be considered as passed, if the number of votes casted against resolution (i.e. in favor of director) is equal to or exceeds:

- In case of Elected Directors:
Minimum No of votes casted at immediately preceding election of directors.
- First / Casual Directors:
Total votes available [i.e. No of directors x No of shares] divided by the No of directors for the time being.

Vacation of office by directors

- He or any firm (of which he is a partner) or any private company (of which he is a director)
 - Without sanction of general meeting accepts or holds any office of profit under company other than chief executive or a legal or a technical adviser; or
 - Accepts a loan or guarantee from Company in contravention of the Act
- Absents himself (without leave of absence from the directors) for 3 consecutive meetings of BOD
- Becomes ineligible under Companies Act 2017
[Any additional grounds may be specified in AOA for this]

POWER, DUTIES AND PROCEEDINGS OF DIRECTORS**Powers of Directors**

Directors may exercise all such powers as are not by Act/AOA/special resolution, required to be exercised by members.

They shall exercise **following powers** by resolution in BOD meeting

- Issue shares, debentures or other redeemable capital
- Borrow moneys other than debentures or Invest company's funds
- Make loans

For banking company: acceptance of deposits from public not be deemed a borrowing or placing of deposit with another banking company not be deemed making of loans

- Incur capital expenditure on any single item or undertake leasing obligations exceeding Rs 1 Million
- Sell or dispose of assets having book value exceeding Rs. 100,000
- To takeover a company or acquire a controlling stake in another
- Approve annual or periodical accounts
- Approve bonus to employees
- Declare interim dividend
- Authorise a director or firm (of which he is a partner) or a private company (of which he is a director) to transact with company
- If amount is material as per accounting principles.
 - to write off bad debts
 - to write off inventories and other assets
 - to determine terms and circumstances for compromise in a law suit or reduction/extinction of claim in favor of company
- Any other specified matter

Directors shall not **except with consent of general meeting** (either specifically or by way of an authorization), do any of following things

- Sell, lease or otherwise dispose of undertaking or any sizable part (i.e. 25% or more assets in that class as per audited accounts of preceding financial year) unless it is the company's business.
- Sell or otherwise dispose of the subsidiary of company
- Remit; give relief or extension of time for loans or advances provided under the provisions of Act (loan to directors)

Note: A listed company is not entitled to sell or otherwise dispose of undertaking resulting in closure of business operation or winding up, without there being a viable alternate business plan approved by BOD

Authorization by the members for exercise of such powers may be either specific or general. Any such resolution, if not implemented within 1 year from date of passing, shall stand lapsed.

Duties of directors [Section 204]

- Act in accordance with AOA.
- Act in good faith in order to promote the objects for the benefit of members as a whole, and in best interests of company, employees, shareholders, community and for protection of environment
- Discharge his duties with due and reasonable care, skill and diligence and shall exercise independent judgment.
- Shall not involve in a situation in which he may have a direct or indirect interest that conflicts with the interest of company.
- Shall not attempt to achieve any undue gain or advantage either to himself or to his relatives, partners, or associates
(If so, he shall be liable to pay that gain to the company)
- Shall not assign his office (such assignment shall be void).

SECP may provide for the extent of duties and the role of directors as may be specified. Any breach of duty, default or negligence by a director in contravention of articles or any of its policy or decision of board may be ratified by company through a special resolution and SECP may impose any restriction as may be specified.

Compliance with the code of corporate governance

- SECP may provide a framework for good corporate governance practices, compliance and connected matters for companies or class of companies in a manner as may be specified.
- It would be the duty of directors to act in line with good corporate governance practices

Liabilities of Directors

Any provision in AOA/Contract with Co shall be void that is exempting any Officer or auditor, from, or indemnifying him against, any liability that would otherwise attach to him in respect of any negligence, default, breach of duty or breach of trust of which he may be guilty in relation to the company

Exemption:

Company may indemnify any such person against any liability incurred by him in defending any proceedings (civil or criminal), in which judgment is given in his favor or he is not guilty.

Protection to independent and non-executive directors

For listed company and public sector company, an independent director and a non-executive director shall be held liable, only for such acts or omission which had occurred with his knowledge, attributable through board processes, and with his consent or involvement or where he had not acted diligently.

Non-executive director

In context of this section, means a person on the board of the company who:

- Is not from among the executive management team and may or may not be independent;
- Is expected to lend an outside viewpoint to the board of a company;
- Does not undertake to devote his whole working time to the company and is not involved in managing the affairs of the company;
- Is not a beneficial owner of company or any of its associated companies or undertakings;
- Does not draw any remuneration from the company except the meeting fee.

Independent director

A director who is not connected or does not have any other relationship, whether pecuniary (financial) or otherwise, with the company, its associated companies, subsidiaries, holding company or directors; and he can be reasonably perceived as being able to exercise independent business judgment without being subservient to any form of conflict of interest. In essence, an executive director can never be an independent director.

Proceedings of the BOD

- Quorum of Listed Co: Higher of 4 or 1/3rd.

Participation of directors by video conferencing or other audio visual means shall also be counted for the purposes of quorum

- Quorum for others shall be as provided in AOA.

If there are not enough directors to form a quorum to fill a casual vacancy, all remaining directors shall be deemed to constitute a quorum

Directors of **Public Co** shall meet at least once in each quarter of year.

Passing of resolution by the directors through circulation

- A resolution in writing signed by all relevant directors/committee shall be as valid and effectual as if it had been passed at a meeting of directors/committee duly convened and held.
- Before passing, the resolution should be circulated with necessary papers to all directors.
- Resolution shall be noted at subsequent meeting and made part of the minutes of such meeting.
- Directors' agreement to such a resolution, once signified, may not be revoked

Records of resolutions and meetings of board

- Every company shall keep records (in properly maintained books) comprising:
 - All resolutions of the board passed by circulation; and
 - Minutes of all proceedings of board meetings or committee meetings along with the names of participants.
- Minutes authenticated by chairman of the meeting or next meeting, shall be the evidence of the proceedings at the meeting.
- A copy of draft minutes shall be furnished to every director within 14 days of the meeting.
- Minutes must be kept at registered office simultaneously in physical and electronic form
- Shall be preserved for at least 10 years in physical form and permanently in electronic form

RESTRICTIONS, PROHIBITIONS AND LIMITATIONS

Restriction on directors remuneration, etc.

For performing extra services (including holding office of chairman)
Determined by directors / General meeting in accordance with AOA

For attending meetings.

Shall not exceed scale approved by Directors/Company in general meeting accordance with AOA

Assignment of office and alternate directors

- Any director shall not assign his office to any other person
- Such appointment shall be void ab-initio.
- Alternate director may be appointed under following situation
 - With the approval of board
 - During his absence from Pakistan of not less than 90 days
 - He shall vacate office when appointing director returns Pak.

Restriction on transactions involving directors

Non-cash transactions

Unless prior approval is accorded by a resolution of general meeting of company or its holding company, no company shall enter into an arrangement by which

- A director of company/holding/subsidiary/associated or a person connected with him acquires or is to acquire assets for consideration other than cash, from the company; or
- Company acquires or is to acquire assets for consideration other than cash, from such director or person so connected;

Notice for resolution shall include particulars of arrangement along with value of assets involved duly calculated by a registered valuer.

Cash transaction

The company shall ensure that all cash transactions with its directors are conducted only through banking channels.

Loans to directors, etc.

Company is not allowed, without approval of members through resolution to provide any of these financial facilities to:

- A director of the company or holding company or any of their relatives (spouse and minor children);
- Provide guarantee or security in connection with a loan made by any person to such a director; or to any of his relatives;

For Listed companies, approval of SECP is also required

Exception

This restriction does not apply to a company which in ordinary course of its business provides loans or gives such guarantees or securities

Other Prohibitions

Prohibition regarding political contributions

A company is not allowed to contribute any amount:

- to any political party; or
- for any political purpose to any individual or body.

Prohibition regarding distribution of gifts

A company is also not allowed to distribute gifts in any form to its members in its meeting.

DISCLOSURE OF INTEREST BY DIRECTORS**Timing of disclosure**

- If transaction or arrangement requires directors' approval before start-up of the contract or transaction
 - At first meeting of directors in which discussion is started
 - At first meeting after he becomes so interested
(if director was not interested at the time of first discussion)
- If transaction or arrangement does not require directors' approval
 - At first meeting held after transaction etc is entered into.

General notice of ownerships and directorships

- Instead making a disclosure on transaction by transaction basis, director may give a general notice regarding his directorships in other body corporate or partnership in firms
- Such notice should be given at directors' meeting or director may take proper steps to ensure that notice is read by other directors.
- General notice shall expire at end of financial year in which it is given and may be renewed by fresh notice in last month of expiry.

Interested director not to vote

Over the approval of matter where he is interested; director cannot take part in discussion, or vote. (Nor to be counted in quorum.)

For listed company, he shall not be present at BOD meeting in which matter involving his material personal interest, is being considered.

Exceptions:

- Private Company (neither subsidiary nor holding of Public)
- If director has acted as surety of company and the resolution relates to indemnification or insurance coverage of that director against any loss incurred by him for becoming surety of company
(company shall only insure liability arises out of a transaction validly approved by board or the members of company)

Interest of other officers, etc.

An officer who is in any way, directly or indirectly, concerned or interested in any proposed contract or arrangement with company is required to:

- Disclose nature and extent of his interest in the transaction; and
- Obtain the prior approval of the directors.

OTHER OFFICERS**Chief Executive**

Chief executive In relation to a company means an individual who, subject to the control and directions of the directors, is entrusted with the whole, or substantially the whole, of the powers of management of the affairs of the company, and includes a director or any other person occupying the position of a chief executive, by whatever name called, and whether under a contract of service or otherwise

Person appointed as chief executive (if not already a director), shall be **deemed** to be a director.

First chief executive

- First chief executive shall be determined by subscribers of MOA.
- His specified particulars shall be submitted with the documents of incorporation.
- Hold office till 1st AGM or shorter period (if fixed by directors) (unless resigns or being removed earlier)
- Federal Government shall have power to nominate and appoint chief executive of a company where majority of directors are nominated by the Federal Government.

Subsequent chief executive

- Appointed by the directors within 14 days of election of directors or casual vacancy
- Term; Maximum period of 3 years from the date of appointment.
- Retiring chief executive is eligible for re-appointment.
- Retiring chief executive shall continue to perform until successor is appointed unless
 - Non-appointment of successor is due to his fault; or
 - His office is expressly terminated.

Terms of Appointment of chief executive and ineligibilities

- Terms of appointment to be determined by directors or Co in general meeting in accordance with AOA.
- Terms of appointment of a chief executive nominated by Federal Government shall be determined by Federal Government
- If a person is ineligible to become a director, he shall also be ineligible to become a chief executive

Removal of Chief Executive

- By 3/4th majority of total number of directors in their meeting; or
- By special resolutions of members.
- By Government/authority/person nominated authorised by it, where more than 75% of voting rights are held by Government.

Chief Executive of public company and competing business

- He, his spouse and minor children are prohibited to engage in a business which competes with his company or its subsidiary
- If he is engaged in any business at the time of appointment in a public company, he shall disclose the details of such business

Chairman (for listed company)

- Board of listed company shall within 14 days from election of directors, appoint a chairman from non-executive directors.
- Chairman shall be responsible for leadership of board and ensure that board plays an effective role in fulfilling its responsibilities.
- Annual financial statements shall contain a review report by the chairman on overall performance of board and its effectiveness.
- Chairman shall hold office for 3 years unless he earlier resigns, becomes ineligible, disqualified or removed by the directors.
- Board shall clearly define the respective roles and responsibilities of chairman and Chief Executive.
(SECP may specify classes of companies for which the chairman and chief executive shall not be the same individual)

Company Secretary (for public companies)

- A qualified secretary should be appointed for public companies.
- He shall be an employee of company
- His responsibilities include making sure that company complies with all relevant corporate requirements.

Share registrar (for listed companies)

- Listed company should also appoint independent share registrars (to handle transfer of shares and all other obligations)
- Name of share registrar is also mentioned in notice of meetings

Sole purchase, sale or distribution agent

No company (incorporated in Pakistan or outside) which is carrying on business in Pakistan shall, without approval of SECP, appoint any sole purchase, sale or distribution agent:

Exception to this rule

Company incorporated, or person ordinarily residing, outside Pakistan are not required to obtain approval of SECP.

(unless the major portion of business of such company or person is conducted in Pakistan)

CH # 14**ISSUE OF SHARES AND DISTRIBUTION OF PROFITS****SHARE CAPITAL****Shares and Share Certificates**

Shares and share certificates have several characteristics.

- A share is a form of property, carrying rights and obligations, and is transferable from one person to another.
- A share must be paid for in full when it is allotted to shareholder.
- Every share shall be distinguished by its distinctive number.
- A certificate issued in physical form under common seal of the company or issued in book-entry form (i.e. Electronic) shall be the main evidence of the title of person to such shares.
- Manner of issue of certificate of shares, form of certificate & other matters may be specified

Authorized and Paid up share capital**Authorised Share Capital:**

- Maximum amount of shares (each class) that company may issue
- Amount of the authorized share capital has to be specified in MOA

Issued and paid up share capital

- Nominal (Face) value of shares (in each class) that have been issued to shareholders.
- Issued share capital may be less than authorised share capital, but cannot exceed it.

Adverts and notices

- If a company mentions its authorized capital in any advertisement or notice or statement, it shall also mention the amount of its paid up capital in equally conspicuous letters & equally prominent position
- Any company which makes default in complying with above requirements and every officer who is party to the default shall be liable to a penalty not exceeding level 1

Fully paid shares

A company having share capital shall issue only fully paid shares.

Previously partly paid shares were allowed but now companies can only issue fully paid share

Nominal value

This is face value of shares, also called par value and stated value.

Market value

Value at which share are traded at stock exchange etc (usually higher than nominal value)

Kinds and classes of shares

- A company limited by shares may have different kinds of share capital and various classes under each kind.
- Company can have more than one kind of share capital only if it has authorized capital for all those kinds

	Ordinary Shares	Preference Shares
Voting Power	√	X
Dividend	Depends on availability of distributable profits after <ul style="list-style-type: none"> - Unpaid cumulative preference dividends of previous years - Preference Dividend of this year 	Percentage of Dividend is normally fixed (defined)
Winding up	Receive payment (if any) after paying preference shares	Receive payment of capital on preferential basis
Different Classes	May be on the basis of <ul style="list-style-type: none"> - Different voting rights - Rights disproportionate to paid up shares - No voting rights - Different entitlements of dividend/right/bonus shares 	May be on the basis of <ul style="list-style-type: none"> - Cumulative preference shares (previous missed dividend also paid in year of profit) - Non-cumulative preference shares - Redeemable / Irredeemable - Convertible to ordinary shares

VARIATION IN SHARE CAPITAL

Procedure for variation in rights

- Can only be made by alteration of AOA through special resolution
- If variation affects the rights of any particular class, it can only be passed if 3/4th majority of that class approves that variation.

Right to challenge the variation in rights

- Any member(s) of affected class representing at least 10% shares of that class may apply to court for an order against resolution
- Such application should be filed within 30 days of resolution.
- Court shall declare resolution null and void if it feels that either;
 - Company withheld certain facts (that could lead towards non passing of resolution) while getting the resolution passed; or
 - Change is prejudicial (harmful) to the interest of members,
- Decision of court shall be final and no appeal can be filed against it
- A copy of court order shall be filed to registrar within 15 days.

Alteration in capital clause

- Co limited by shares, (if authorised by AOA), may alter capital clause of its MOA by passing Special Resolution to:
 - Increase its share capital by such amount as it thinks fit;
 - Cancel that part of its authorized capital which has not been paid up till the date of cancellation
(cancellation shall not affect rights of paid up shareholders)
 - Consolidate shares into larger amount than fixed by MOA
 - Sub-divide shares into smaller amount than fixed by MOA
- Company shall file resolution and altered copy of MOA with the registrar within 15 days of passing the same
(Otherwise resolution shall not be effective and shall lapse)
- New shares issued by the company (due to consolidation or sub division) shall rank equally with existing shares of the company.

PROSPECTUS**Prospectus (Section 2(41) Securities Act, 2015)**

Any document described or issued as a prospectus and includes any document, notice, circular, material, advertisement, offer for sale document, publication or other invitation offering to the public (or any section of the public) or inviting offers from the public for the subscription or purchase of any securities of a company, body corporate or entity, other than deposits invited by a bank and certificate of investments and certificate of deposits issued by non-banking finance companies.

Purpose of the prospectus

- If company wants to issue securities to large number of persons (public) it has to offer this to general public through a prospectus.
- If general public wants to subscribe or purchase securities of any company, it can help them by providing relevant information.

Timing of prospectus

Company may issue a prospectus at any point in time of its life.

- Can issue shares before commencement of business.
- Can decide to issue shares in the future

Note: Existence of Prospectus ends after the purpose is fulfilled
(It is not like MOA or AOA that are permanent)

Shelf-Prospectus

It is a single offering document allowing companies to make multiple offerings as disclosed in the offering document within a prescribed time and subject to prescribed conditions.

Supplement to Prospectus

A supplement to prospectus invites general public for subscription of the securities earlier offered to the public through shelf-prospectus. The supplement to prospectus for each offering contains updated disclosures.

Filing with registrar before issue

- On or before the date of publication, a copy signed by every person named as a director or proposed director, should be filed with the registrar.
- In case of any contravention, company and every person who is party to issue, publication or circulation of prospectus shall be liable to a penalty not exceeding level 2

Note: Normally authorities require the company to arrange and write risk factors separately (in a single para). Readers of prospectus are specifically advised to read at least that para before making any investment decision.

Approval of prospectus

- Prospectus must be approved by SECP prior to its issuance.
- Issuer or offeror shall submit a copy to SECP for approval at least 21 days before the proposed date of publication of prospectus.
- It shall be valid for a period of 60 days from the date of approval.
(Limit of 60 days maybe extended by SECP for some reasons to be recorded in writing)
- Prospectus cannot be issued, published or circulated without SECP approval.
(Same condition also applies on shelf-prospectus or supplement to the prospectus)
- SECP may impose further conditions or restrictions in this regard.
- Without prior written approval of SECP, no person shall issue, circulate, publish, telecast or broadcast, an advertisement, other than prospectus, announcing a public offer of securities unless a prospectus has been published and the advertisement gives an address in Pakistan from which it can be obtained.
- Issuer or offeror shall not, at any time, vary the terms of clauses given in its prospectus except with the approval of SECP

Exceptions where approval of SECP is not required

- Securities offered by the State Bank of Pakistan;
- If securities are offered in connection with a private offer;
- Issue of shares of a subsidiary to the members of a listed holding company (as a dividend) or any other distribution in the prescribed manner.
- If the securities are offered by the issuer to—
 - Members or employees of the issuer; or
 - Members of the families of any such members or employees; and
- If securities are shares and are offered as bonus shares to any or all of members of issuer.

Issue, circulation and Publication of Prospectus

Publication of Prospectus

- Prospectus (full text/approved abridged form) shall be published at least in one Urdu and one English daily newspaper.
- It shall be published in newspapers at least 7 days and at most 30 days before the commencement of public subscription.
- Sufficient number of copies of approved prospectus shall be made available (free of charge) from the date of its publication in newspapers till the closing of the subscription at:

- Registered office of the issuer
- All securities exchanges of the country
- All the bankers to the issue
- Concerned share registrar
- Concerned ballotter and
- Concerned credit rating agency (if any)
- Prospectus and subscription form shall be
 - Uploaded on website of the issuer; and
 - Shall remain there from date of its publication in newspapers till the closing of the subscription.

Expert

Expert to be independent

Expert should be a person who is not, and has not been, engaged or interested information or promotion or in management of company.

"Expert" includes banker, securities advisor, engineer, valuer, accountant, lawyer and any other person whose profession gives authority to a statement made by him..

Expert's consent:

A prospectus that contains a statement purporting to be made by an expert or to be based on a statement made by an expert shall not be issued, circulated or published unless:

- Expert has given, his written consent to issue of prospectus with the statement in the form and context in which it is included; and
- There appears in the prospectus a statement that the expert has given and has not withdrawn his consent.

Criminal liability for defective prospectus

A person commits an offence, who:

- Makes a misleading, incorrect, untrue or deceptive statement in a prospectus; or
- Omits information or a statement from prospectus that Securities Act, 2015 or any related rule or regulation requires to include.

Compensation for false or misleading prospectus

Every offeror, issuer, director of an offeror or issuer or any person who has signed prospectus shall be liable to pay compensation to any person who acquires securities, in reliance on prospectus and suffers loss in respect of them due to any incorrect, untrue or misleading statement in prospectus or omission of any required matter

CONDITIONS FOR COMMENCEMENT OF BUSINESS

- Private company and a guarantee limited company not having share capital can commence their business and exercise all of the powers regarding borrowings after incorporation
- Other companies shall not commence any business or exercise borrowing powers unless:
 - Shares have been allotted in cash not less than the minimum subscription
 - Every director has paid to company in cash full amount on each of the shares taken or contracted to be taken by him
 - No money is or may become liable to be repaid to applicants for any shares which have been offered for subscription;
 - Filed with registrar a duly verified declaration by the chief executive or one of the directors and secretary in prescribed form that conditions complied with
 - Registrar has issued a certificate of commencement of business (conclusive evidence)
 - Company has filed a prospectus or SILOP.
- Any contract made by a company before the date at which it is entitled to commence business shall be provisional only, and shall not be binding on company until that date
- For contravention of above provisions, every officer or other responsible person shall, in addition to other liabilities, be liable to a penalty not exceeding level 2

Minimum Subscription

Means the amount, if any, fixed by MOA/AOA upon which directors may proceed to allotment. If no amount is fixed, the whole amount of share capital (other than that to be issued not for cash) is minimum subscription.

Prospectus or Statement in Lieu of Prospectus (SILOP)

Circumstances	Relevant Document to be issued or filed
Inviting general public, or when company is listed	Prospectus
Not inviting the public to subscribe	SILOP
Issued a prospectus but could not obtain listing on stock exchange	Repayment of all money on the basis of prospectus AND filing SILOP

DIVIDENDS

Company has an implied power to use its profits to pay dividends to its shareholders.
(Unless specifically restricted by MOA & AOA)

Dividends will be either in cash or in the form of shares of listed company held by the distributing company.

Final dividend

- Proposed by directors and approved by members in AGM
- Members may reduce, accept or reject this proposed dividend
(Cannot resolve to increase the amount proposed by directors)

Paid within such number of days as may be specified by SECP from date of AGM
(*Tutor's Note: Previously it was 30 days; Now ICAP have suggested not to write 30 days*)

Interim dividend

Directors may propose and pay interim dividend before end of year.

Must be paid, within such number of days as may be specified by SECP, from

- Commencement of book closure for this purpose; or
- Directors Meeting (if books were not closed for this purpose)

Restriction on declaration of dividend

- Dividend cannot be declared out of **profits from sale of immovable property** or item of capital nature except
 - Business of company consists of buying and selling such items of capital nature; and
 - After such profits are adjusted against losses on sale of immovable properties or assets of capital nature
- Dividend cannot be declared from **unrealized gain** arising out of re-measurement of investment property directly credited to Income statement.

PAYMENT OF DIVIDENDS

- Dividends can be paid, at the order of shareholder through:
 - Cheque/warrant; or
 - Electronic mode
- In listed companies, dividend in cash shall only be paid electronically (in bank account designated by shareholders)

Penalty for delay in payment (more than days specified by SECP)

- Any one or both of the following penalties:
 - Chief executive may be fined for an amount up to **Rs. 5 Million**
 - Also imprisonment for a term which may extend to **2 years**.
- Ineligible to become a director or Chief Executive of any company for next **5 years**.

Circumstances in which delay in payment shall not be an offense

In following cases, company may withhold dividend after obtaining prior approval of SECP within 45 days of declaration of dividend

- If dividend cannot be paid due to operation of any law,
- If shareholder has given instructions regarding payment of dividend and such instructions cannot be followed
- There is a dispute on regarding the right to receive dividend
- If company has withheld the payment of dividend against any sum recoverable from shareholder,
- If non- payment of dividend or non -posting of the warrant was not due to any default on part of the company.

Company may also withhold dividend of a member where he has not provided the complete information or documents as specified by SECP.

CH # 15**MEETINGS****DIFFERENT TYPE OF MEETINGS****Director's Meetings**

- Board Meeting (all the directors)
- Committee Meeting (selected directors)

Member's Meetings

- General Meetings (all the members)
 - Statutory Meeting
 - Annual General Meeting
 - Extraordinary General Meeting
- Class Meetings (any class of members)

General meetings are chaired by chairman of BOD. Other directors also attend the meeting, but they don't have a right to vote there. If they are member as well, then they can vote as a member.

Statutory Meeting**Applicable on**

- Every public company having share capital
- A private company that converts itself into a public company within one year of its incorporation

Timing**Earlier of**

- 180 days from date of commencement of business; or
- 9 months from the date of its incorporation

Statutory meeting not required if AGM is held before its due date

Purpose

To discuss and approve "Statutory Report"
(sent to members with notice at least 21 days before meeting)

- Members may discuss any matter relating to company in this meeting however resolution shall only be passed only for those matters for which prior notice has been given
- Directors shall make available a list of members, along with their particulars, at start of meeting and it shall be open for inspection by any member during meeting
- Meeting may be adjourned from time to time and any resolution passed in adjourned meeting will be as effective as original one.

Contents of Statutory Report

- Total number of shares allotted by the company (distinguishing between shares allotted for cash and otherwise)
- Total cash received against shares allotted
- For shares allotted otherwise than in cash, details of consideration
- Summary of receipts and payments prepared to a date not earlier than 15 days before date of statutory report under separate heading:
 - Receipts from shares, debentures and other sources
 - Payments made;
 - Balance remaining in hand; and
 - Estimate of preliminary expenses showing separately any commission or discount paid or to be paid on issue of shares or debentures;
- Particulars of directors, chief executive, secretary, auditor and legal adviser;
- Particulars of any commission paid on issue of shares (particularly against the shares issued to directors, chief executive and to the private companies in which such persons are directors)
- Details of any contract to be modified with member's approval
- Extent of carrying out or not carrying out any underwriting contract (with reasons for not carrying out)
- A brief review of affairs of the company since its incorporation and the business plan.

Authentication and filing of Statutory Report

- Shall be certified by chief executive and at least 1 director. (for listed company, also by CFO)
- Report should be accompanied by an **auditor's report** on
 - Allotment of shares
 - Cash received against share allotted
 - Receipts and Payments account of the company.
- A copy of report, along with auditor's report, shall be filed with the registrar forthwith after sending report to the members.

Annual General Meeting (AGM)

- 1st AGM
Within 16 months of incorporation
- Subsequent AGM
 - Once in every calendar year
 - Within 120 days of close of its financial year
- Extension up to 30 days can be granted in AGM by
 - SECP for listed Co
 - Registrar for any other case

- Notice of AGM shall be given to members 21 days before meeting.
- For listed company, notice also to be
 - Published in an Urdu and an English daily newspaper having nationwide circulation
 - Sent to the SECP
- AGM of listed company shall be held in town of registered office or in a nearest city
- Members of listed company holding at least 10% shares, residing in another city, on written request at least 7 days before AGM, may require Co to provide facility of video-link to attend AGM

Note: SMC is not required to hold AGM

Extraordinary General Meeting (EGM)

- All meetings other than AGM and Statutory shall be called EGM.
- Notice of EGM shall be given to members 21 days before meeting. (For listed Co notice also be published in 1 Urdu & 1 English newspaper having circulation in province of stock exchange)
- For unlisted companies, if all members entitled to attend and vote at any EGM so agree, a meeting may be held at a shorter notice.
- Directors may call an EGM at any time for taking approval of members on any matter.

Meeting on requisition of members

- EGM can also be called on request of members (requisitionists) holding at least 10% voting power (or 10% in quantity in case of a company not having share capital)
- Requisition shall file a proper written requisition
 - Stating the objects of meeting
 - Signed by requisitionists
- On such requisition directors shall call the EGM.
- If directors do not proceed to call EGM within 21 days of requisition; the requisitionist themselves should call a meeting
- Meeting shall be called in approximately same manner as would have been called by directors.
- Any reasonable expenses incurred on meeting shall be repaid by company to requisitionist (company shall deduct this money from the remuneration payable to directors in default)

Meeting should be held within 90 days of filing requisition either by directors or by the requisiteness otherwise requisition shall be expired.

Calling of meetings by SECP

- SECP may call any general meeting if company makes a default in calling Statutory Meeting, AGM or EGM on requisition of members.
- SECP may give such incidental directions as it deems fit.
(including that even 1 member present can be treated as quorum)
- All costs borne by company unless SECP directs same to be taken from some defaulting official of company
- SECP may also direct that the cost and expenses of such meeting to be borne by any of the officers including directors

CONDUCT OF MEETINGS**Notice and Special Business****Notice**

- A formal document sent to each member at
 - His registered address; or
 - Any other address supplied by him
- Notice shall state place, day and time of the meeting
- Notice may be served to members
 - against an acknowledgement; or
 - by post or courier service; or
 - through electronic means; or
 - any other specified manner.
- Notice alongwith a statement of the business (to be transacted) shall be given to:
 - Every member or class of the members of the company as the case may be;
 - Every director;
 - Auditors of the company.
 - Any person who is entitled to a share in case of death or bankruptcy of a member (if company has been notified of his entitlement);
- Accidental omission to give notice to, or non-receipt of notice by, any member shall not invalidate the proceedings at any meeting
- Members may participate in the meeting personally, through video-link or by proxy.
- For listed company, it shall be mentioned in the notice that if certain members holding 10% of the total paid up capital (or such other percentage as may be specified), reside in a city, they may demand to provide them the facility of video-link for attending the meeting.

Special Business

- Any business (agenda of the meetings) other than the following "ordinary businesses" is known as "special business"
 - Consideration of accounts, auditors' and directors' reports
 - Appointment of auditors and fixing their remuneration
 - Declaration of dividends
 - Election or appointment of directors
- If any special business is to be discussed at meeting; notice shall include "Statement of material facts" about that business
- If any item of business requires an approval to any document by meeting, the time and the place where the document may be inspected, shall be specified in the statement

Presiding the meeting (Chairman of Meeting)

- Chairman of BOD shall preside as chairman at every general meeting.
- If at any meeting he is not available/present within 15 minutes of starting time, or is unwilling to act as chairman, any one of the directors present may be elected as chairman.
- If none of the directors is present or is unwilling to act, members present shall choose one of their member as chairman

Voting

- In company not having share capital, each member shall have 1 vote
- In company having share capital, member shall have votes proportionate to paid up value of shares

Type of Voting**Show of Hands**

- Voting is normally done by show of hands unless poll is demanded
- Every member shall exercise **one vote**
- Chairman shall declare the results of show of hands
(whether a resolution has been carried or not, unanimously or by a particular majority)
- Chairman's declaration will be valid (unless contrary is proved)
- Decision shall be entered in the books of minutes

Poll

- Before or on declaring result of voting by show of hands, a poll may be taken by chairman on his own or may be demanded by persons having at-least 10% voting power
- In a poll, **voting power** of shareholders is counted for voting.
- On a poll votes may be casted personally or through proxy
- Demand of poll may be withdrawn anytime by the person or persons demanding the poll.

Time of talking Poll**For election of chairman or adjournment**

Immediately

Any other case:

At such time as the chairman may direct
(not more than 14 days from demand of poll)

- After polling; chairman or his nominee and a representative of member(s) demanding poll shall scrutinize results
- Chairman shall declare the result
- Chairman has power to regulate manner in which polls may be conducted and the results of poll shall be final.

Proxies

- A person appointed to vote and speak on behalf of a member
- Proxy must be a member unless AOA permits.
- Proxy is entitled to all the acts which the original shareholder is entitled to do himself in meeting including:
 - to speak and vote at the meeting;
 - to demand a poll;
 - to abstain from voting, if poll is demanded.
- Notice must specifically mention the right to appoint proxy
(A blank proxy form should also be attached with the notice)
- Written proxy form/instrument shall be signed by appointer or his authorized agent
- Proxy form shall be filed at least 48 hours before meeting time
(Non working day shall not be counted in these 48 hours)
- If a valid proxy instrument (as per table A of Articles) is deposited, company cannot reject or question its validity
- A member cannot appoint more than 1 proxy
(if so appointed all the proxies shall be invalid)
- Every member entitled to vote at a meeting shall be entitled to inspect during the business hours of the company all proxies lodged with the company

Note: In case of companies not having share capital, members are not entitled to appoint another person as his proxy unless the articles provide otherwise.

Representations**Corporations at meetings of companies**

- If a company is member of another company, it may authorise any of its officials or any other person to act as its representative there
- Such representative shall have same powers, which an individual shareholder of that other company possesses at that meeting.

Creditors

- A creditor company may authorize any of its officials to represent it at the creditor's meeting (possessing all powers of creditors)

Federal or Provincial government as a member of any company

- Federal Government or Provincial Government may appoint any person to act as its representative at any general or class meeting;
- Such person shall be deemed to be a member of such company and he shall be entitled to exercise all the rights and powers of any member, including the right to appoint proxy

Quorum

Quorum means certain minimum number of members of a company as is fixed as competent to transact business in a general meeting of members in the absence of the other members. Any business transacted in a meeting without quorum shall be void

Unless larger number fixed by AOA, quorum shall be:

Listed

10 members present personally or through video link having at least 25% voting powers present in person/proxy

Other companies having share capital

2 members present personally or through video link having at least 25% voting powers present in person/proxy

Other companies not having share capital

As provided in the AOA

Presence/Absence of quorum

If Quorum not complete within half hour of meeting,

- If called by requisitionists; Shall be dissolved.
- If called by the directors; Shall be adjourned to same day, time & place in next week

If quorum not present within half hour at adjourned meeting, quorum shall be not less than 2 members present personally or through video link (unless articles provide otherwise)

Declaring meeting as invalid

When there are material defects or omission in the notice or there is irregularity in proceedings of the meeting:

- Members having 10% or more voting rights may file a petition
 - to court
 - within 30 days of the meeting
- Court may declare such proceedings or any part of the meeting invalid and may direct holding of fresh general meeting

RESOLUTIONS AND RECORDS

Notice of resolution

- In case of special resolution, notice shall be accompanied by the draft resolution.
- Members having at least 10% voting power may also give notice of a resolution (with supporting statement, if any) to company:
 - With the requisition for the meeting (meeting requested by requisitionists)
 - At least 10 days before the meeting (in any other case)
- Company shall forthwith circulate such resolution to all the members.

Resolution passed at adjourned meeting

If a resolution is passed at any of the adjourned meeting (any type), the resolution shall be treated as having been passed on the date on which it was in fact passed, and not on any earlier date

Resolution through circulation

- Except for ordinary businesses, members of a private company or a public unlisted company (having not more than 50 members), may pass a resolution (ordinary/special) by circulation signed by all members for time being entitled to receive notice of meeting.
- It shall be as valid and effectual as it is passed in general meeting.
- Resolution shall be circulated to all members (together with necessary papers)
- Members' agreement, once signified, may not be revoked.
- Such resolution shall be noted at subsequent meeting and made part of the minutes of that meeting.

Filing of resolutions

- A copy of all special resolutions shall be filed with registrar within 15 days of passing
- Such copy shall be authenticated by a director or secretary
- Copy of every Special Resolution to be annexed to every copy of (registered) AOA issued after date of resolution.

Minutes

- Every company is required to maintain
 - Records of copies of all resolutions of members passed otherwise than at general meetings; and
 - A fair and accurate summary of all proceedings of meetings of directors, member or committees of directors
- Minutes shall include names of attendees.
- Books of minutes of the meetings shall be kept at Registered office
- Signatures of the chairman of that meeting or next meeting shall be sufficient evidence of proceedings (unless contrary is proved)
- Minutes books shall be open to inspection by members for at least 2 hours on each day during the business hours (without charges)
- Members can demand certified copy of minutes of general meeting at any time after 7 days of meeting (prescribed fee)
 - Company shall provide him within 7 working days of request.
- Records must be kept at registered office from the date of the resolution, meeting or decision in physical and electronic form
- Records shall be preserved
 - For at least 20 years in physical form; and
 - Permanently in electronic form.

Note: All requirements of Companies Act regarding calling of, holding and approval in general meeting, board meeting and election of directors in case of a SMC, shall be deemed complied with; if decision is recorded in the relevant minutes book and signed by sole member/director

CH # 16**ACCOUNTS & INVESTMENTS****ACCOUNTS****Books of Accounts to be kept by a Company****Book and paper / Book or Paper**

Includes books of account, cost accounting records, deeds, vouchers, writings, documents, minutes and registers maintained on paper or in electronic form.

Books of Accounts

Include records maintained in respect of

- all sums of money received and expended by a company and matters in relation to which the receipts and expenditure take place;
- all sales and purchases of goods and services by the company;
- all assets and liabilities of the company; and
- items of cost in respect of production, processing, manufacturing or mining activities;

- A company must maintain **proper books of accounts** (which fairly present the state of the affairs of the company and a fair record of all its transactions)
- Books and records may be in the form of hardcopy books or any computerized system
- Books of accounts for at least **10 years** must be preserved
- Liquidator of company appointed for winding up of company is also required to maintain the above books during its winding up.

Keeping the books

- Books must be kept at registered office of the company
- Directors may opt to keep these books at some other place (Pass a resolution in directors meeting and intimate registrar within 7 days of that)
- If company has a branch office
 - Proper books of that branch may be maintained at branch
 - Proper summarized returns should reach registered office or other specified place periodically.

Inspection of books of accounts by Directors

- Directors are entitled to inspect books during business hours.
- If some financial information is maintained outside country
 - Copies shall be maintained and shall be make available for inspection by any director.
 - Employees shall give full assistance to director for inspection

Inspection of books of accounts by Members

Members do not have absolute right to inspect books of accounts. However, Companies Act 2017, or directors or general meeting may authorize member(s) to inspect books of accounts.

Presentation of Financial Statements

Financial Statements

- Statement of financial position as at the end of the period;
- Statement of profit or loss and other comprehensive income (or an income and expenditure statement in case of not for profit);
- Statement of changes in equity for the period;
- Statement of cash flows for the period;
- Notes, comprising a summary of significant accounting policies and other explanatory information;
- Comparative information in respect of the preceding period; and
- Any other statement as may be prescribed;

Financial year

In relation to a company or any other body corporate, means the period in respect of which any financial statement of the company or the body corporate, as the case may be, laid before it in general meeting, is made up, whether that period is a year or not.

Time Limit

- Once in every calendar year, directors are required to present the financial statements, in a general meeting of company, within **120 days of close of financial year** (not applicable to Single Member Companies)
- In case of first accounts of the company, it shall be presented in a general meeting within **16 months of date of incorporation**
- Company can apply for 30 days **extension** in presenting accounts
 - Listed company shall apply to SECP
 - Other companies apply to registrar
- Company should not prepare accounts for more than 12 months (On application of company the registrar may extend this period)

Audit of financial statements

- Such accounts shall be audited and the auditor's report shall accompany the accounts.
- The requirement of audit is not applicable to a private company having paid up capital not exceeding Rupees 1 million or such higher amount as may be notified by SECP

Sending copies of financial statements

- Copy of these financial statements along with auditor's and directors' report (+ chairman's review report; for listed) shall be sent to every member at least 21 days before meeting
- A listed company shall dispatch at least 3 copies of these documents to SECP, registrar and Stock exchange simultaneously with sending these to members.
- A copy of these documents should also be filed electronically to SECP by listed company
- Company shall also retain a copy at its registered office and every member shall be allowed to inspect such copy
- Reports shall be made available on website of company for time period as may be specified

Authentication of Financial Statements

- Directors authenticate financial statements in meeting by passing resolution.
- Members only receive accounts and can ask any questions in AGM.
- Chief executive and at least 1 director put their signatures on it.
(For listed companies CFO shall also sign the financial statements)
- If chief executive is out of Pakistan at the time of signing, then at least 2 directors shall sign the financial statements
- For private company having paid up capital up to Rs. 1 Million, financial statements shall be accompanied by an affidavit by Chief Executive (if accounts signed by him) or by any director (if accounts have been signed by 2 directors), that the financial statements have been approved by the board
- Financial statements of a SMC shall be signed by 1 director.

Chief financial officer (CFO)

Means an individual appointed to perform such functions and duties as are customarily performed by a CFO

Filing of Accounts (after AGM)

- Companies shall send 1 copy of its financial statements (adopted in AGM along with other required reports & documents), signed as per the requirements of act, to registrar within
 - 30 days of AGM, in case of listed companies
 - 15 days of AGM, in case of other companies.
- If general meeting does not adopt these accounts and reports, the fact shall be mentioned to registrar along with such copies
- This filing requirement shall not apply to a private company having paid up capital not exceeding Rs. 10 million or such higher amount as may be notified by SECP

Quarterly Accounts of Listed Companies

- Every listed company shall prepare quarterly financial statements within the period of-
 - 30 days of the close of 1st and 3rd quarters of its year of accounts; and
 - 60 days of the close of 2nd quarter of its year of accounts:
- SECP may, on application by company, extend the period of filing 1st quarter accounts for a period not exceeding 30 days (if company was allowed extension in previous year AGM)
- Half yearly accounts (i.e. 2nd Quarter) shall be subject to limited scope review by auditors of company in such manner, term and conditions as may be determined by ICAP and approved by SECP.
- Quarterly financial statements shall be
 - Posted on company's website for information of its members (for such time as may be specified by SECP)
 - Transmitted electronically to SECP, securities exchange and registrar within 30/60 days
 - Dispatched in physical form, if so requested by any member, without any fee
- Requirements of approval & authentication of final accounts are also applicable to the quarterly accounts

DIRECTORS REPORT

- Board shall prepare a directors' report for each financial year.
- Not applicable to a private company, not being a subsidiary of public company, having paid up capital up to Rs. 3 million
- SECP may by general or special order, direct such class or classes of companies to prepare a statement of compliance with such contents as may be specified.

Contents for every directors report

Directors shall make and attach to the accounts a report containing

- Statements regarding state of affairs of the company
- Particulars of any dividend recommended
- Particulars of any amount transferred/proposed to be transferred to any reserve account

Additional contents for public company & their subsidiaries

- Names of persons who, at any time during the financial year, were directors of company.
- Any specific changes and commitments affecting the financial position of company, occurring between financial year end date and the date of report.
- All material changes occurred during financial year which affect
 - business of the company; or
 - its holding company; or
 - any of its subsidiaries; or
 - any other company where it has made investments.
- Discuss the reservations, observations qualification etc. or any adverse remarks pointed out by the auditors.
- State the earnings per shares (EPS) and reasons for incurring loss and also contain the reasonable indication of future profit if any
- Pattern of shareholding shall also be circulated along with it
- Name and place of incorporation of its holding company (if such holding company is incorporated outside Pakistan)
- Information regarding default in repayments of loans or interests on loans, if any.
- Description of principal risks & uncertainties facing the company and shall contain the comments in respect of adequacy of internal financial controls.

Additional contents for Listed Company (Business review of listed company)

Must at least cover the following:

- Main trends and factors likely to affect the future development, performance and position of the company's business;
- Impact of the company's business on the environment;
- Activities undertaken by company in regard to corporate social responsibility during year;
- Directors' responsibility in for adequacy of internal financial controls as may be specified

Authentication of directors' report

Director's Report and statement of compliance must be approved by board and signed by chief executive officer and a director

INVESTMENTS

Investment in associated company

Associated company/Associated undertaking

Two or more companies or undertakings interconnected with each other in the following manner:

- If companies or undertakings are under common management/control
- If one is subsidiary of another
- If undertaking is a modaraba managed by the company
- If a person is owner or partner or director of company/undertaking, or who, directly or indirectly (spouse/minor child), holds or controls shares carrying not less than 20% of voting power in such company or undertaking, is also owner or partner or director of another company/ undertaking, or directly or indirectly, holds or controls shares carrying not less than 20% of voting power in that company or undertaking.

Exceptions: Following directorships or shareholdings shall not be considered while ascertaining status of companies to be associated

- Directorship by virtue of nomination by concerned Minister of the Federal Government or a Provincial Government or a financial institution directly or indirectly owned or controlled by such Government; or
- Directorship of a person appointed as "Independent Director"
- Shares owned by National Investment Trust (NIT) or the Investment Corporation of Pakistan (ICP) or a financial institution directly or indirectly owned or controlled by Federal Govt or a Provincial Govt; or
- Shares registered in the name of a central depository

Note: Modaraba is an Islamic financing activity, a set up created in order to ensure interest free financing. Modaraba Management Company is established as a public company which is licensed to float Modaraba which are separate legal entities

'Investment' include loans, advances, equity guarantees, by whatever name called, or any amount, which is not in nature of normal trade credit

Condition for investment

- Company can make investment in any of its associated companies or undertakings only under **Special Resolution**
(It shall indicate nature, period, amount of investment and related terms and conditions)
- **No variation** in the nature and terms & conditions of investment or an **increase in amount** without passing a **special resolution**.

For investments as a loan

- It should be done through a written agreement specifying the following additional points:
 - Nature of loan;
 - Purpose of loan;
 - Period of the loan;
 - Rate of return;
 - Fees or commission
 - Repayment schedule for principal and return;
 - Penalty clause (in case of default or late repayments); and
 - Security, if any, for the loan
- Return on investment shall not be less than borrowing cost of investing company or rate as may be specified by SECP.
- Directors shall certify that the investment is made after due diligence and that the borrower has the ability to repay loan.

SECP has specified certain classes of companies (e.g. private) on which requirements of this section not applicable. It has made certain regulations for imposing conditions on investments by companies in associated companies.

Investments of company to be held in its own name

All the investments of the company must be made and held in the **name of the company** itself and not in someone else's name

Exceptions

- If Investor Company has power to appoint its directors (nominee) on Investee company; then Investor company is allowed to hold such shares in name of that nominee that are qualification shares (required for any director) of Investee company.
- Holding company may hold any shares in its subsidiary company in name of its nominees if number of members of the subsidiary company has reduced below required minimum members.
- Company may also place its investment in the name of CDC.

Register for investments of company not held in its own name

Register shall contain nature, value and such other particulars as may be necessary fully to identify such shares or securities.

Inspection of Register

- Register shall be open to inspection of members free of cost for at least 2 hours daily
- Any other person may also inspect register on payment of such fee as company may specify.
- Company may impose certain restrictions on such inspection
- Any member may require a certified copy of register or any part:
 - On paying the fee fixed by company.
 - Certified copies requested shall be issued within 7 days.
- If any inspection is refused, Registrar may on an application direct immediate inspection.