

Special Contracts: Indemnity, Guarantee, Bailment and Pledge

The term Indemnity literally means “Security against loss”. In a contract of indemnity one party – i.e. the indemnifier promise to compensate the other party i.e. the indemnified against the loss suffered by the other.

The definition of a contract of indemnity as laid down in 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, is called a contract of indemnity.

ILLUSTRATION

A contracts to indemnify B against the consequences of any proceedings which C may take against B in respect of a certain sum of 200 rupees. This is a contract of indemnity.

VALIDITY OF INDEMNITY AGREEMENT

A contract of indemnity is one of the species of contracts. The principles applicable to contracts in general are also applicable to such contracts so much so that the rules such as free consent, legality of object, etc., are equally applicable.

Where the consent to an agreement is caused by coercion, fraud, misrepresentation, the agreement is voidable at the option of the party whose consent was so caused. As per the requirement of the Contract Act, the object of the agreement must be lawful. An agreement, the object of which is opposed to the law or against the public policy, is either unlawful or void depending upon the provision of the law to which it is subject.

RIGHT OF THE INDEMNITY HOLDER – (SECTION 125)

- An indemnity holder (i.e. indemnified) acting within the scope of his authority is entitled to the following rights

1. Right to recover damages – he is entitled to recover all damages which he might have been compelled to pay in any suit in respect of any matter covered by the contract.

2. Right to recover costs – He is entitled to recover all costs incidental to the institution and defending of the suit.

3. Right to recover sums paid under compromise – he is entitled to recover all amounts which he had paid under the terms of the compromise of such suit. However, the compensation must not be against the directions of the indemnifier. It must be prudent and authorized by the indemnifier.

- **RIGHT OF INDEMNIFIER –**

- Section 125 of the Act only lays down the rights of the indemnified and is quite silent of the rights of indemnifier
- as if the indemnifier has no rights but only liability towards the indemnified.

CONTRACT OF GUARANTEE

- A "contract of guarantee " is a contract to perform the promise, or discharge the liability, of a third person in case of his default. The person who gives the guarantee is called the " surety“.
- the person in respect of whose default the guarantee is given is called the " principal debtor ", and the person to whom the guarantee is given is called the " creditor ". A guarantee may be either oral or written.

- ILLUSTRATIONS

- (a) B requests A to sell and deliver to him goods on credit. A agrees to do so, provided C will guarantee the payment of the price of the goods. C promises to guarantee the payment in consideration of A's promise to deliver the goods. This is a sufficient consideration for Cs promise.
- (b) A sells and delivers goods to B. C afterwards requests A to forbear to sue B for the debt for a year, and promises that, if he does so, C will pay for them in default of payment by B. A agrees to forbear as requested.
- This is a sufficient consideration for Cs promise.

Bailment

- Bailment is a kind of activity in which the property of one person temporarily goes into the possession of another. The ownership of the property remains with the giver, while only the possession goes to another.
- Several situations in day to day life such as giving a vehicle for repair, or parking a scooter in a parking lot, giving a cloth to a tailor for stitching

- Section 148 of Indian Contract Act 1872, defines bailment as follows –
- Section 148 – A bailment is the delivery of goods by one person to another 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 them. The person delivering the goods is called the bailor and the person to whom they are delivered is called the bailee.

- **Duties of a Bailor**

- A bailor may give his property to the bailee either **without any consideration or reward or for a consideration or reward.**
- In the former case, he is called **a gratuitous bailor**, while in the latter, **a bailor for reward.** The duties in both the cases are slightly different. Section 150 specifies the duties for both kinds of bailor. It says that the bailor **is bound to disclose any faults in the goods bailed that the bailor is aware of, and which materially interfere with the use of them or which expose the bailee to extraordinary risk.** This means that if there is a fault with the goods which may cause harm to the bailee, the bailor must tell it to the bailee.
- For example, if a person bails his scooter to his friend and if the person knows that the brakes are loose, then he must tell this to the friend. Otherwise, the bailor will be responsible for damages arising directly out of the faults to the bailee. But the bailor is not bound to tell the bailee about the fault if the bailor himself does not know about it.

- Section 150 imposes a bigger responsibility to the non-gratuitous bailor since he is making a profit out of the bailment. A non gratuitous bailor is responsible for any damage that happens to the bailee directly because of the fault of the goods irrespective of whether the bailor knew about it or not.

Duties/Responsibilities of a Bailee

- **1. Duty to take reasonable care:** Section 151 treats all kinds of bailees the same with respect to the duty. It says that in all cases of bailment, the bailee is bound to take as much care of the goods bailed to him as a man of ordinary prudence would, under similar circumstances take, of his own goods of the same bulk, quality, and value as the goods bailed. The bailee must treat the goods as his own in terms of care. However, this does not mean that if the bailor is generally careless about his own goods, he can be careless about the bailed goods as well. He must take care of the goods as any person of ordinary prudence would of his things.

- **2. Bailee, when not liable for loss etc. for thing bailed – :** As per section 152, in absence of a special contract, the bailee is not responsible for loss, destruction, or deterioration of the thing bailed, if he has taken the amount of care as described in section 151. This means that if the bailee has taken as much care of the goods as any owner of ordinary prudence would take of his goods, then the bailee will not be liable for the loss, destruction, or deterioration of the goods. No fixed rule regarding how much care is sufficient can be laid down and the nature, quality, and bulk of goods will be taken into consideration to find out if proper care was taken or not. In *Gopal Singh vs Punjab National Bank*, AIR 1976, Delhi HC held that on the account of partition of the country, when a bank had to flee along with mass exodus from Pakistan to India, the bank was not liable for the goods bailed to it in Pakistan.

3. Duty not to make unauthorized use (Section 154) : Section 154 says that if the bailee makes any use of the goods bailed which is not according to the conditions of the bailment, he is liable to make compensation to the bailor for any damage arising to the goods from or during such use of them.

4. Duty to return (Section 160) : It is the duty of the bailee to return or deliver according to the bailor's directions, the goods bailed, without demand, as soon as the time for which they were bailed has expired or the purpose for which they were bailed has been accomplished.

Pledge

A pledge is only a special kind of bailment, and chief basis of distinction is the object of the contract. Where the object of the delivery of goods is to provide a security for a loan or for the fulfilment of an obligation, that kind of bailment is pledge. Under Indian Contract Act, 1872 the 'Pledge' has been defined in section 172 as:

S 172. "Pledge", "pawnor", and "Pawnee" defined:

The bailment of goods as security for payment of a debt or performance of a promise is called "pledge". The bailor is in this case called the "Pawnor". The Bailee is called the "Pawnee".