1. Explain in detail Contract of Indemnity. Distinguish it from contract of guarantee.

Ans- **Contract of Indemnity**

According to dictionary meaning, indemnity is protection against loss, esp. in the form of a promise to pay, or payment for loss of money, goods, etc. It is a security against, or compensation for loss, etc. For instance, 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.

In a contract of indemnity, the person who promises to indemnify is known as "indemnifier", and the person in whose favour such a promise is, made is known as "indemnified" or "indemnity holder".

According to Section 124 of the Indian Contract Act, 1872, a contract of indemnity means "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 conduct of any other person." This provision incorporates a contract where one party promises to save the other from loss which may be caused, either (i) by the conduct of the promisor himself, or, (ii) by the conduct of any other person.

This definition covers indemnity for loss caused by human agency only. It does not deal with those classes of cases where the indemnity arises from loss caused by events or accidents which do not or may not depend upon the conduct of the indemnifier or any other person, or by reason of liability incurred by something done by the indemnified at the request of the indemnifier.

Insurance contract, if contract of indemnity ; India

It has been noted above that Section 124 recognizes only such contract as a contract of indemnity where there is a promise to save another person from loss which may be caused by the conduct of the promisor himself or by conduct of any other person. It does not cover a promise to compensate for loss not arising due to human agency. Therefore, a contract of insurance is not covered by the definition of Section 124. Thus, if under a contract of insurance, an insurer promises to pay compensation in the event of loss by fire, such a contract does not come within the purview of Section 124. Such contracts are valid contracts, as being contingent contracts as defined in Section 31.

United India Insurance Company v. M/s. Aman Singh Munshilal, the cover note stipulated delivery to the consigner. Moreover, on its way to the destination the goods were to be stored in a godown and thereafter to be carried to the destination. While the goods were in the godown, the goods were destroyed by fire. It was held that the goods were destroyed during transit, and the insurer was liable as per the insurance contract.

England

Under English law, the word 'indemnity' carries a much wider meaning than given to it under the Indian Contract Act. It includes a contract to save the promisee from a loss, whether it be caused by human agency or any other event like an accident and fire. Under English law, a contract of insurance (other than life insurance) is a contract of indemnity.

Life insurance contract is, however, not a contract of indemnity, because in such a contract different considerations apply. A contract of life insurance, for instance, may provide the payment of a certain sum of money either on the death of a person, or on the expiry of a stipulated period of time (even if the assured is still alive). In such a case, the question of amount of loss suffered by the assured, or indemnity for the same, does not arise. Moreover, even if a certain sum is payable in the event of death, since, unlike property, the life of a person cannot be valued, the whole of the amount assured becomes payable. For that reason also, it is not a contract of indemnity.

Contract of Guarantee

Section 126 of the Indian Contract Act, 1872, defines a contract of guarantee as under :

"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 Section further provides that :

"The person who gives the guarantee is called the "**surety**", the person in respect of whose default the guarantee is given is called "**principal debtor**", and the person to whom the guarantee is given is called the "**creditor**".

A guarantee may be either oral or written." For example, A takes a loan from a bank. A promises to the bank to repay the loan. B also makes a promise to the bank saying that if A does not repay the loan "then I will pay." In this case, A is the principal debtor, who undertakes to repay the loan, B is the surety, whose liability is secondary because he promises to perform the same duty in case there is default on the part of A. The bank in whose favour the promise has been made is the creditor.

The object of a contract of guarantee is to provide additional security to the creditor in the form of a promise by the surety to fulfill a certain obligation, in case the principal debtor fails to do that.

In every contract of guarantee, there are three parties, the creditor, the principal debtor and the surety. There are three contracts in a contract of guarantee.

Firstly, the principal debtor himself makes a promise in favour of the creditor to perform a promise, etc.

Secondly, the surety undertakes to be liable towards the creditor if the principal debtor makes a default.

Thirdly, an implied promise by the principal debtor in favour of the surety that in case the surety has to discharge the liability of the default of the principal debtor, the principal debtor shall indemnify the surety for the same. When a borrower and a guarantor both sign an agreement in favour of a bank, they are jointly and severally liable under that contract.

Main Features of Contract of Guarantee :
1. The contract may be either oral or in writing

According to Section 126, a guarantee may be either oral or written. On this point, the position in India is different from that in England. According to English law, for a valid contract of guarantee, it is necessary that it should be in writing and signed by the party to be charged therewith.

2. There should be a principal debt

A contract of guarantee pre-supposes a principal debt or an obligation to be discharged by the principal debtor. The surety undertakes to be liable only if the principal debtor fails to discharge his obligation. If there is no such principal debt, but there is a promise by one party in favour of another for compensating in a certain situation, and the performance of this promise is not dependent upon the default of somebody else, it is a contract of indemnity.

3. Benefit to the principal debtor is sufficient consideration

As in any other contract, the consideration is also needed for a contract of guarantee. For the surety's promise, it is not necessary that there should be direct consideration between the creditor and the surety, it is enough that creditor had done something for the benefit of the principal debtor. Benefit to the principal debtor constitutes a sufficient consideration to the surety for giving the guarantee. This is clear from Section 127, which reads as under :

"Anything done, or any promise made for the benefit of the principal debtor may be a sufficient consideration to the surety for giving the guarantee."

Illustrations;

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 sufficient consideration for C's promise.

4. Consent of the surety should not have been obtained by misrepresentation or concealment

The creditor should not obtain guarantee either by any misrepresentation or concealment of any material facts concerning the transaction. If the guarantee has been obtained that way, the guarantee is invalid. The position is explained by Sections 142 and 143, which are as under :

"**142. Guarantee obtained by misrepresentation invalid**. Any guarantee which has been obtained by means of misrepresentation made by the creditor, or with his knowledge and assent, concerning a material part of the transaction, is invalid."

"**143. Guarantee obtained by concealment invalid**.-Any guarantee which the creditor has obtained by means of keeping silence as to material circumstance is invalid.

Distinction between contracts of Indemnity and Guarantee :

1. There are two parties in a contract of indemnity, the indemnifier and the indemnity-holder, or indemnified. There are three parties in a contract of guarantee, the creditor, the principal debtor and the surety.

2. Contract of indemnity consists of only one contract under which the indemnifier promises to indemnify the indemnified in the event of a certain loss. There are three contracts in a contract of guarantee. One contract is between the principal debtor and the creditor in respect of a certain promise or obligation undertaken to be performed by the principal debtor. By a second contract, the surety undertakes to perform the same obligation which the principal debtor has undertaken, in case the principal debtor makes a default. The third contract, which is an implied one, is between the principal debtor and the surety. By this contract, the principal debtor is bound to indemnify the surety for whatever sum the surety has rightfully paid under the guarantee. It means that after the surety discharges his obligation, he is invested with all the rights which the creditor had against the principal debtor.

3. The object of a contract of guarantee is the security of the creditor. It presupposes a principal debtor and a certain debt or an obligation for which the principal debtor is primarily liable. A contract of indemnity is made to protect the promisee against some likely loss.

4. In a contract of guarantee, the liability of the surety is only a secondary one. Surety's liability arises only when the principal debtor makes a default. The liability of the indemnifier in a contract of indemnity is a primary one. He undertakes to be liable when the contemplated situation is there.

5. In a contract of guarantee, after the surety had discharged his liability and paid to the creditor, he steps into the shoes of the creditor and he can realize the payments made by him, from the principal debtor. In a contract of indemnity, the loss falls on the indemnifier and, therefore, after the indemnifier had indemnified the indemnity-holder, he cannot recover the amount from anybody.

6. In England, a contract of guarantee should be in writing whereas a contract of indemnity may be either oral or in writing. There is no such distinction in India. In India, whether it is a contract of indemnity or guarantee, the same may be either oral or in writing.

2. Who is Surety? Discuss Rights and Duties Of Surety.

Ans- Surety

A surety is a person who comes forward to pay the amount in the event of the borrower failing to pay the amount. In the event of a decree in favour of the creditor against the principal borrower, the wings of the decree can also be extended against the sureties as their liability in coextensive with the principal debtor. But when a suit against the principal debtor was dismissed for default and the decision became final, there being no liability surviving against the debtor, the surety's liability gets automatically terminated.

Liability of Surety: Its Nature and Extent :

According to **Section 128,** "The liability of the surety is coextensive with that of the principal debtor, unless it is otherwise provided by the contract."

The provision that the surety's liability is coextensive with that of the principal debtor means that his liability is exactly the same as that of the principal debtor. It means that on a default having been made by the principal debtor, the creditor can recover from the surety all what he could have recovered from the principal debtor. For instance, the principal debtor makes a default in the payment of a debt of Rs. 10,000/-. The creditor may recover from the surety the sum of Rs. 10,000/- plus interest becoming due thereon as well as the amount spent by him in recovering that amount.

Narayan Singh v. Chattarsingh, it has been held that if the principal debtor's liability is scaled down in an amended decree or otherwise extinguished in whole or in part by a statute, the liability of the surety would also pro tanto be reduced or extinguished. In this case, the liability of an agriculturist, who was the principal debtor,. was scaled down under the Rajasthan Relief of Agricultural Indebtedness Act, 1957. It was held that the effect of scaling down the principal debt to Surety's liability for loan transaction

The loan was advanced by Bank to principal borrower under certain scheme with a clause in the scheme that bank shall not ask for borrower's contribution in the form of margin money or seek collateral security or third party guarantee. There was execution of document by borrower and surety for repayment of loan. In the instant case as surety had voluntarily agreed to repay the loan, therefore, he was liable to repay such loan jointly and severally with borrower as clause in scheme did not mean that if anybody voluntarily agreed to repay loan, it should be refused.
r's liability was that the surety's liability had also been reduced accordingly.

Creditor can sue the surety without exhausting remedies against the principal debtor

The liability of the surety is joint and several with the principal debtor. It has already been noted that according to Section 128, "the liability of the surety is coextensive with that of the principal debtor, unless it is otherwise provided by the contract." It means that if the principal debtor makes a default, i.e., he fails to perform his obligation, the creditor can sue either the principal debtor, or the surety or both of them. The creditor can sue the surety even though he has not exhausted his remedies against the principal debtor.

Limit on surety's liability by contract

It has already been noted that Section 128 declares that the liability of the surety is coextensive with that of the principal debtor, unless it is otherwise provided by the contract. It means that if the contract the parties so provides, surety's liability may not be there to the full extent as that of the principal debtor but smaller than that. Thus, if the surety undertakes to be liable to the extent of £250, his liability is limited to that extent.

Condition that there shall be a co-surety

Sometimes, there may be a condition in a contract of guarantee that there shall be a co-surety also. Where a person gives a guarantee upon a contract that the 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.3 It means that in such a contract, liability of the surety is dependent on the condition precedent that a co-surety will join. The surety can be made liable under such a contract only if the co-surety joins, otherwise not.

Liability of co-surety

It has been noted above that the liability of sureties is coextensive with that of the principal debtor. It implies that the creditor can proceed against the principal debtor or the surety, at his discretion, unless it is otherwise provided in the contract. The same principle is applicable with regard to the rights and liabilities of the co-sureties. Since the liability of the co-sureties is joint and several, a co-surety cannot insist that the creditor should proceed either against the principal debtor or against any other surety before proceeding against him.

Discharge of surety from liability

When the liability of surety, which he had undertaken under a contract of guarantee, is extinguished or comes to an end, he is said to be discharged from liability. The modes of discharge of a surety, as recognized by the Indian Contract Act, are as under :

1. Revocation by the surety (Section 130).
2. By surety's death (Section 131).
3. By variance in the terms of the contract (Section 133).
4. By release or discharge of principal debtor (Section 134).

5. When creditor compounds with, gives time to, or agrees not to sue, the principal debtor (Section 135).
6. By creditor's act or omission impairing surety's eventual remedy (Section 139).
7. By loss of the security by the creditor (Section 141).

RIGHTS OF SURETY :

A surety has certain rights against the principal debtor, the creditor and the co-sureties. His rights against each one of them are being discussed here under :

A. Rights against the Principal Debtor :

1. Right of Subrogation (Section 140)

When the principal debtor makes a default in the performance of his duty, and on such a default, the surety makes the necessary payment or makes performance of all what he is liable for, he becomes invested with all the rights which the creditor had against the principal debtor. In other words, the surety steps into the shoes of the creditor and by an action against the principal debtor, he can recover from him all that, which could have been recovered by the creditor. This is known as surety's right of subrogation.

2. Right of indemnity against the principal debtor (Section 145)

In a contract of guarantee, when the principal debtor makes a default, the surety has to make the payment to the creditor. This payment is made by him on behalf of the principal debtor. After making such payment, he can recover the same from the principal debtor. Such a claim can be made by the surety only in respect of the sums he has rightfully paid under the guarantee, but not the sums which he has paid wrongfully.

B is indebted to C, and A is surety for the debt. C demands payment from A, and on his refusal, sues him for the amount. A defends the suit, having reasonable ground for doing so but he is compelled to pay the amount of the debt with costs. He can recover from B the amount paid by him for costs, as well as the principal debt.

B. Right against the Creditor

Right to securities with the creditor (Section 141).

It has been noted above that after the surety has performed his duty under the contract of guarantee, he is subrogated to all the rights which are available to the creditor against the principal debtor. Section 141 makes a further provision in that regard, according to which a surety is entitled to the benefit of every security which the creditor has against the principal debtor at the time when the contract of suretyship is entered into. It is, however, not necessary that at the time of making the contract, the surety should be aware of the securities which the creditor had. It becomes the duty of the creditor not to lose or part with such securities belonging to the principal debtor which he possesses at the time of making of the contract of guarantee. If the creditor, without the consent of the surety, loses or parts with such securities, this is an act prejudicial to the interest of the surety and he is discharged thereby.

Securities received by the Creditor at the time of contract of guarantee

It may be noted that the surety is entitled to the benefit of such securities which the creditor has against the principal debtor at the time when the contract of suretyship is entered into. If the creditor loses the securities possessed by him at the time of making of the contract, that results in the discharge of the surety to that extent.

Loss of without creditor's negligence

Loss of the securities by the creditor results in the discharge the surety. If, however, the hypothecated securities are lost without any fault of the creditor, the surety is not discharged thereby.

Securities received by the creditor after the contract of guarantee

It has been noted above that according to Section 141, a surety is entitled to the benefit of every security which the creditor has at the time when the contract of suretyship is entered into. It means that the surety has no right to those securities which the creditor obtained from the principal debtor after making the contract of guarantee. Therefore, if a creditor parts with the securities which he had obtained subsequent to the making of the contract of guarantee, the surety will not be discharged as a consequence of the loss of such securities.

Surety has no right to goods in hypothecation

It may be noted that according to Section 141, the surety is entitled to the benefit of such goods which are with the creditor. It covers situations where the goods are pledged to the creditor and he has the possession of the goods. If he loses or parts with the goods, the surety is discharged thereby. In case there is hypothecation of the goods, the goods remain in the possession of the borrower. The hypothecatee does not have the possession of the goods and there is no question of his losing or parting with the same. If, therefore, the hypothecated goods are lost without any fault of the creditor, that will not discharge the surety. In other words, since in the case of the hypothecated goods, the creditor does not have the possession of the goods, the surety cannot invoke the provision of Section 141 in such case.

C. Right against the Co-sureties

Right of contribution against co-sureties (Sections 146 & 147)

Section 146 makes the following provision regarding the liability of the co-sureties when there are two or more co-sureties for the same debt.

"146. Co-sureties liable to contribute equally.-When two or more persons are co-sureties for the same debt or duty, either jointly or severally, and whether under the same or different contracts, and whether with or without the knowledge of each other, the co-sureties, in the absence of any contract to the contrary, are liable, as between themselves, to pay each an equal share of the whole debt, or of that part of it which remains unpaid principal debtor." the

The duty of the co-sureties is to contribute equally. This is so when they are co-sureties for the same debt. It is immaterial that they have undertaken a duty either jointly or severally, or under the same or different contracts, or with or without the knowledge of each other. For instance, A, B, and C are sureties to D for the sum of 3,000 rupees lent to E. E makes default in payment. A, B and C re liable, as between themselves, to pay, 1,000 rupees each.

Co-sureties bound in different sums (Section 147)

Sometimes the sureties may fix the maximum sum up to which their liability can go. There may be different limits as to the amount for which the sureties are to be liable. According to Section 147, who are bound in different sums are liable to pay equally as far as the limits of their respective obligations permit." This may be explained by the following illustrations[2] :

(a) A , B and C as sureties for D, enter into three several bonds each in different penalty, namely, A in the penalty of 10,000 rupees, B in that of 20,000 rupees, C in that of 40,000 rupees, conditioned for D's duly accounting to E. D makes default to the extent of 30,000 rupees. A, B and C are each liable to pay 10,000 rupees.