



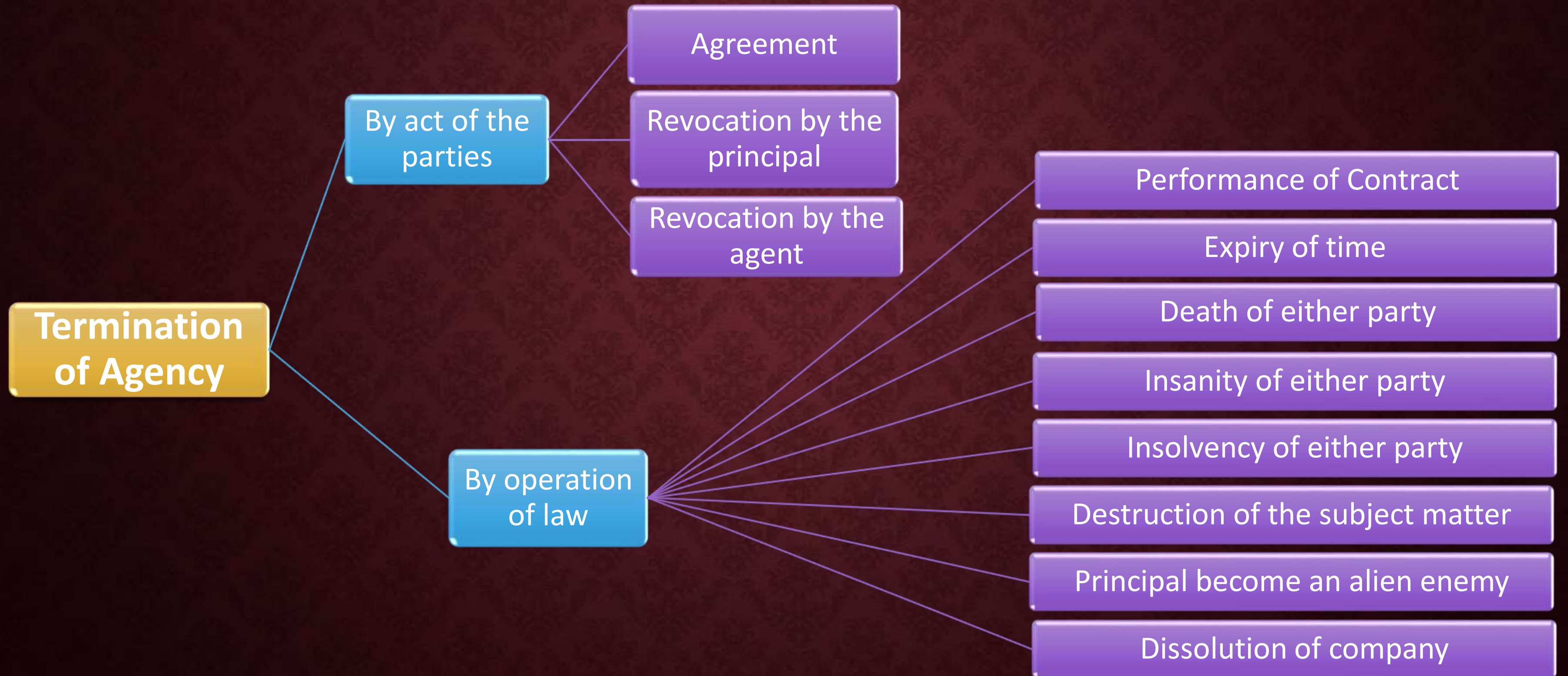
VIT<sup>®</sup>

Vellore Institute of Technology  
(Deemed to be University under section 3 of UGC Act, 1956)

# Legal Aspects of Business

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# Recapitulate





# Contract of Indemnity and Guarantee

## Contract of Indemnity

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'. The person who promises to make good the loss is called the indemnifier (promisor) and the person whose loss is to be made good is called indemnity-holder (promisee). A contract of indemnity is really a class of contingent contracts.

# Contract of Indemnity and Guarantee

## Contract of Indemnity

A contract of insurance is a glaring example of contract of indemnity

A contract of indemnity may arise either by

- i. An express promise or
- ii. Operation of law



# Contract of Indemnity and Guarantee

## Essential elements of Valid Contract

1. Offer and Acceptance
2. Intention to create legal relationship
3. Lawful consideration
4. Capacity of parties
5. Free and genuine consent
6. Lawful object
7. Certainty of Meaning
8. Possibility of Performance
9. Agreement not declared Valid
10. Legal Formalities

# Contract of Indemnity and Guarantee

## Rights of the Indemnified

- i. All damages which he may be compelled to pay in any suit in respect of any matter to which the promise to indemnify applies
- ii. All costs of suit which he may have to pay to such third party, provided in bringing or defending the suit
  - a. he acted under the authority of the indemnifier or
  - b. if he did not act in contravention o orders of the indemnifier and in such way as a prudent man would act in his own case
- iii. All sums which may have been paid under the terms of any compromise of such suit, if the compromise was not contrary to the orders of the indemnifier and was one which it would have been prudent for the promise to make.



# Contract of Indemnity and Guarantee

## Contract of Guarantee

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 guarantee is given is called the 'principal debtor' and the person to whom the guarantee is given is called the 'creditor'.

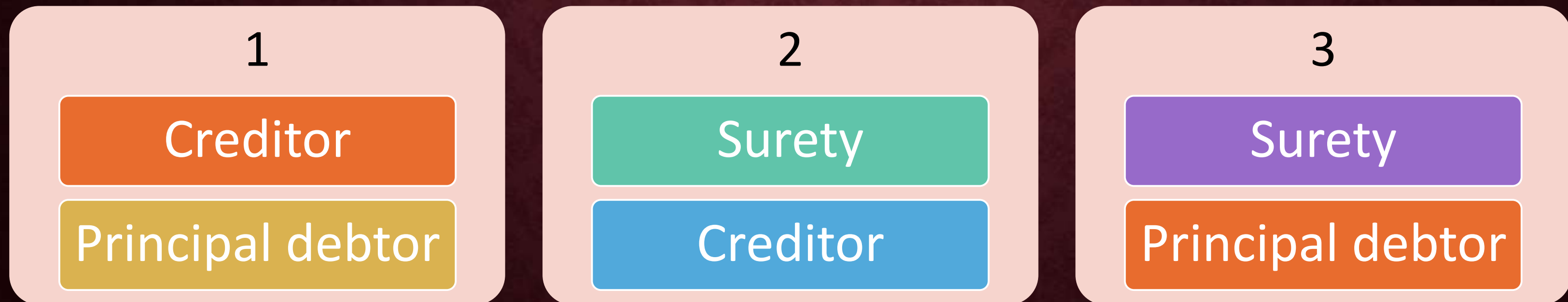
# Contract of Indemnity and Guarantee

## Contract of Guarantee

A guarantee may be either oral or written. It may be express or implied.

Contract of Guarantee is a tripartite agreement which contemplates the principal debtor, P, the principal creditor C, and the surety S in it.

There is a triangular relationship in which the following three collateral contracts may be distinguished;





# Contract of Indemnity and Guarantee

## Purpose of Contract of Guarantee

Most common business contracts uses the contract of guarantee for a number of purposes, these are;

1. The guarantee is generally made use of to **secure loans**
2. The contract of guarantee are sometimes called performance bonds.

**For example,** in the case of a construction project, the builder may have to find a surety to stand behind his promise to perform the construction contract. Also employers often demand a type of performance bond known as fidelity bond from employees who handle cash, etc., for the good conduct of the latter.

3. Bail bonds, used in criminal law, are a form of contract of guarantee. A bail bond is a device which ensures, that a criminal defendant will appear for trial.



# Contract of Indemnity and Guarantee

## Kinds of Guarantee

**1. Oral or Written Guarantee:** A contract of guarantee may either be oral or in writing, though a creditor should always prefer to put it in writing to avoid any dispute regarding the terms, etc. In case of an oral agreement the existence of the agreement itself is very difficult to prove.

**2. Specific and Continuing Guarantee:** A guarantee is a 'specific guarantee', if it is intended to be applicable to a particular debt and thus comes to end on its repayment. A specific guarantee once given is irrevocable.

Unlike specific guarantee which is irrevocable, a continuing guarantee can be revoked regarding further transactions.

**Example:** A guarantees payment to B, a tea-dealer, to the amount of Rs.10,000 for any tea he may from time to time supply to C. B supplies C with tea of the value above Rs.10,000 and C pays B for it. Afterwards B supplies C with tea to the value of Rs.15,000. C fails to pay. The guarantee given by A was a continuing guarantee and he is accordingly liable to B to the extent of Rs.10,000



# Contract of Indemnity and Guarantee

## Essential Features of a Contract of Guarantee

- 1. Concurrence:** The Principal debtor, the surety and the creditor
- 2. Primary liability in some person:** The primary liability is the principal debtor and secondary liability is the surety. It arises only when there is a default by the principal debtor.
- 3. Writing not necessary**

## 4. Essential elements of Valid Contract

- Offer and Acceptance
- Intention to create legal relationship
- Lawful consideration
- Capacity of parties
- Free and genuine consent
- Lawful object
- Certainty of Meaning
- Possibility of Performance
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# Contract of Indemnity and Guarantee

## Distinction between a contract of Indemnity and a Contract of Guarantee

Sl. No.	Contract of Indemnity	Contract of Guarantee
1	Two parties: Indemnifier and Indemnified	Three parties: The creditor, the principal debtor and the surety
2	The liability of the Indemnifier is primary and independent	The liability of the surety to the creditor is collateral or secondary, the primary liability being that of the principal debtor
3	One contract: Between the indemnifier and the indemnified	Three contracts: i. Between the principal debtor and the creditor, ii. Between the creditor and the surety iii. Between the surety and the principal debtor
4	Not necessary for the indemnifier to act on the request of indemnified	Necessary that the surety should give the guarantee at the request of the debtor
5	The liability of the indemnifier arises only on the happening of contingency	There is usually an existing debt or duty, the performance of which is guaranteed by the surety
6	Indemnifier cannot sue a third party for loss in his own name, there is no privity of contract.	A surety, on discharging the debt due by the principal debtor, can proceed against the him in his own right.



# Review Questions

1. As per the Indian law, a contract of guarantee must be in writing. **True or False**
2. Who is the primary liable person in case of contract of guarantee?
  - a. Surety
  - b. Principal debtor
  - c. Both
3. S and P go into a shop. S says to the shopkeeper, C, “Let P have the goods, and if he does not pay you, I will.” This is a....
  - a. Contract of guarantee
  - b. Contract of indemnity
  - c. Quasi contract
  - d. Contract of agency

# Answer

1. As per the Indian law, a contract of guarantee must be in writing.

**Answer:** False

2. Who is the primary liable person in case of contract of guarantee?

**Answer:** b. Principal debtor

3. S and P go into a shop. S says to the shopkeeper, C, "Let P have the goods, and if he does not pay you, I will." This is a.....

**Answer:** a. Contract of guarantee



# Thank You