

MERCANTILE LAW

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UNIT – I

Sale of Goods

- 1. Concept of sale as a contract**
- 2. Essentials of contract of sale**

CONCEPT OF SALE AS A CONTRACT

The Black's Law Dictionary defines a "sale" as a contract between two parties, called, respectively, the seller (or vendor) and the buyer (or purchaser), by which the former, in consideration of the payment or promise of payment of a certain price in money, transfers to the latter the title and the possession of property. It is a contract whereby property is transferred from one person to another for a consideration of value, implying the passing of the general and absolute title, as distinguished from a special interest falling short of

complete ownership;¹ an agreement by which one gives a thing for a price in current money, and the other gives the price in order to have the thing itself. To constitute a sale, there must be parties standing to each other in the relation of buyer and seller, their minds must assent to the same proposition, and a consideration must pass.

Section 4 (1) of the Sale of Goods Act², defines a “contract of sale” as under:

A contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price.

Section 5 (1)³ deals with as to how a contract of sale is made and reads as follows:

“A contract of sale is made by an offer to buy or sell goods for a price and the acceptance of such offer. The contract may provide for the immediate delivery of the goods or immediate payment of the price or both, or for the delivery or payment by instalments, or that the delivery or payment or both shall be postponed.”

The interpretation clause of the Indian Contract Act, 1872⁴, reads as follows;

- a) 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;
- b) when the person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted. A proposal, when accepted, becomes a promise;
- d) when, at the desire of the promisor, the promisee or any other person has done or abstained from doing, or does or abstains from doing, or promises to do or abstain from doing, something, such act or abstinence or promise is called a consideration for the promise;
- e) every promise and every set of promises, forming the consideration for each other, is an agreement;
- h) an agreement enforceable by law is a contract;

The interpretation clause indicates that an agreement can be reached by the process of offer and acceptance. It has been held in myriad cases that every transaction to be recognised as a contract, must in its ultimate analysis, resolve itself into a proposal and its absolute and unqualified acceptance.⁵ Thus, section 5 (1), Sale of Goods Act⁶ read with section 2, Indian Contract Act⁷, makes it amply clear that “sale”, by virtue of being an “offer” to buy or sell

¹ S. 2(11), Sale of Goods Act, 1930.

² 1930.

³ Sale of Goods Act, 1930.

⁴ Section 2.

⁵ *Badri Prasad v State of Madhya Pradesh* AIR 1970 SC 706; *Suraj Besan and Rice Mills v Food Corpn of India* AIR 1988 Del 224; *Deep Chandra v Rukruddaula Shamsher J N M Sajjad Ali Khan* AIR 1951 All 93.

⁶ 1930.

⁷ 1872.

goods, for a consideration, termed as “price”⁸, and the acceptance of such offer thereafter, is a contract within the meaning of section 2 of the Indian Contract Act⁹.

The following are the elements necessary for formation of a valid contract:

- a) There must be an agreement i.e., there must be a proposal (offer) and an acceptance. The person making the proposal is called the ‘promisor’ and the person accepting the proposal is called the ‘promisee’.
- b) The parties must be competent to contract.
- c) It must be made by the ‘free consent’ of parties. Two or more persons are said to consent when they agree upon the same thing in the same sense.
- d) Consideration for the contract must be lawful.
- e) Object of the agreement must be lawful.
- f) It is not expressly declared to be void under the Act.

Clearly, therefore, a sale fulfils all these necessary elements of a contract and can thereby easily be concluded to be a contract within the meaning of the Indian Contract Act.¹⁰ Another point which may be noted here is that the Sale of Goods was earlier a part of the Indian Contract Act¹¹ as sections 76-123 which were later repealed by the Sale of Goods Act, 1930.

Sale consists of two separate and distinct elements: First, contract of sale which is completed when offer is made and accepted and, second delivery of property which may precede, be accompanied by, or follow, payment price as may have been agreed on between parties. An essential element of sale is the money price which must either be fixed by agreement or capable of being ascertained therefrom.

ESSENTIALS OF CONTRACT OF SALE

Section 4 (1)¹² defines a contract of sale as under:

“A contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in the goods to the buyer for a price.”

For example one Hexicon Limited enters into an agreement with M/s Furtado and Sons for purchase of steel. Furtado and Sons (the seller) sells the good (i.e. steel) to the company for Rs. 1, 25,000/- (i.e. the price). This is a contract for sale of goods.

⁸ S. 2(10), Sale of Goods Act, 1930.

⁹ 1872.

¹⁰ Ibid.

¹¹ Ibid.

¹² Sale of Goods Act, 1930.

Therefore, the essentials of a contract of sale can be deduced from the abovementioned definition as under:

- a) It is a contract between two parties, one known as the seller and the other the buyer.
- b) The subject-matter of the contract is “goods”.
- c) The seller should transfer or agree to transfer the property (ownership) in the goods to the buyer.
- d) The transfer of property (ownership) in the goods from the seller to the buyer is for a consideration referred to as “price”.

In *New India Association Co. Ltd. V. T.H. Devakumar*¹³, the Honourable Supreme Court observed that in order to constitute a valid sale of the goods under the [Sale of Goods Act](#),¹⁴ there must be cogent and convincing evidence of: (i) agreement between the competent parties, (ii) the price for the goods, and (iii) passing of the property in the goods. Unless all these ingredients of sale are duly proved, mere entry or endorsement made by the registering authority under Sec. 31 of the Act¹⁵ in the relevant record/register showing transfer of ownership of a vehicle does not amount to sufficient proof of sale of that vehicle. Further in this case, the Honourable Supreme Court cited the case of *Madras State v G. Dunkerley and Co.*, and said that sufficient light had been thrown in this case on the essential ingredients of a sale pertaining to sale of goods and quoted the following from this case:

“Thus, according to the law both of England and of India, in order to constitute a sale it is necessary that there should be an agreement between the parties for the purpose of transferring title to goods which of course presupposes capacity to contract, that it must be supported by money consideration, and that as a result of the transaction property must actually pass in the goods. Unless all these elements are present, there can be no sale. Thus, if merely title to the goods passes but not as a result of any contract between the parties, express or implied, there is no sale. So also if the consideration for the transfer was not money but other valuable consideration, it may then be exchange or barter but not a sale. And if under the contract of sale, title to the goods has not passed, then there is an agreement to sell and not a completed sale.”

The essentials of a contract of sale may be discussed in detail as follows:

a) Contract between two distinct parties namely the seller and the buyer

A contract of sale is a contract between two distinct parties namely a seller and a buyer. “Seller” is defined to mean a person who sells or agrees to sell goods¹⁶ and a “buyer” is defined to mean a person who buys or agrees to buy goods.¹⁷ The seller and the buyer should be two different persons. Therefore, if a person purchases his own goods, it is not sale. However, there may be a contract of sale between one part-

¹³ AIR 1996 Kant. 345.

¹⁴ 1930.

¹⁵ Motor Vehicles Act, 1988.

¹⁶ S. 2 (13).

¹⁷ S. 2 (1).

owner and another.¹⁸ A partner and a firm may also sell goods to each other. In the same way, when a person's goods are being sold in execution of a decree, he himself may purchase them. In case of sale by auction, the Act¹⁹ permits a seller of goods to reserve a right of himself making a bid at the auction and purchasing his own goods.

Contract under Statutory Compulsion

Sometimes a contract may not be entered into by the normal process of negotiation, but under a statutory compulsion. When the goods are supplied under a statutory compulsion, whether that results in sale or not, is the question which has arisen in a number of cases. In *New India Sugar Mills v. Commissioner of Sales Tax, Bihar*,²⁰ J.C. Shah and J.L. Kapur, JJ. in their majority decision held that supply of sugar by a sugar factory in compliance with the orders of the Sugar Controller of India under Sugar and Sugar Products Control Order, 1946 did not result in a contract of sale of goods, and hence that transaction could not be subject to sales tax. Hidayatullah J., in his dissenting opinion, however observed that in such a case there was implied contract of sale between the parties. In his view, "a compelled sale is nevertheless a sale". In a later decision in *Vishnu Agencies v. Commercial Tax Officer*,²¹ The Supreme Court overruled its earlier decision in the *New India Sugar Mills* case, expressed its agreement with the dissenting judgment of Hidayatullah, J. in that case, and held that the transaction of supply of cement by a distributor to a permit holder in terms of the provisions of West Bengal Cement Control Act and the West Bengal Cement Control Order amounts to sale, and the same is eligible to sales tax.

In *Andhra Sugars Ltd. V. State of A.P.*,²² it has been held by the Supreme Court that in case of sale under the compulsion of a statute, the consent is not deemed to be caused by the coercion, undue influence, fraud, misrepresentation or mistake. In that case if any canegrower offered to sell his sugarcane to a factory in a certain zone, the factory was bound to accept the offer under the Andhra Pradesh Sugarcane (Regulation of Supply and Purchase) Act, 1961. It was held that in such a case even though there was legal compulsion for the factory to make the agreement, the validity of the agreement was not affected on ground of absence of free consent, and such an agreement being a contract of sale within the meaning of section 4 of the Sale of Goods Act, the State could validly impose purchase tax on the purchase of sugarcane. Similarly, in a decision of the Supreme Court in *Coffee Board, Karnataka v. Commissioner of Commercial Taxes*,²³ it has been held that the compulsory delivery of coffee by the coffee growers to the Coffee Board constitutes a sale, and not compulsory acquisition, and the State can impose purchase tax on the same.

¹⁸ S. 4 (1).

¹⁹ S. 64 (3).

²⁰ AIR 1963 SC 1207.

²¹ AIR 1978 SC 449.

²² AIR 1968 SC 599.

²³ AIR 1988 SC 1487.

FORMALITIES:

The Sale of Goods Act does not prescribe the observance of any formalities for creating a contract of sale. It rather expressly provides that such a contract may be made either in writing or by word of mouth, or partly in writing and partly by word of mouth or may be implied from the conduct of the parties.²⁴ If a customer goes to a shop where articles are exhibited for sale and picks up one and the shop-keeper packs the same for him, there has resulted a contract of sale of goods.

The above stated position, however, is “subject to the provisions of any law for the time being in force”. For example, in the case of transfer of shares in a company, the provisions of the Companies Act, 2013, have got to be observed. The process of transfer of shares is not deemed to be complete until the transfer has been registered with the company.²⁵

The contract of sale may provide for the immediate delivery of the goods or immediate payment of the price or both, or for the delivery or payment by instalments, or that the delivery or payment or both shall be postponed.²⁶

b) Goods

The subject matter of a contract of sale must be goods. The term ‘goods’ has been defined under section 2 (7) of the Act²⁷ to mean “every kind of moveable property other than actionable claims and money; and includes stock and shares, growing crops, grass, and things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale”.

Clearly then, the Act deals with the sale of goods, i.e., movable property. The sale of immovable property is dealt with in the Transfer of Property Act, 1882. Although the term “goods” means every kind of movable property, certain things have been specifically excluded and certain other things specifically included in the term, by the definition.

Stock and Shares, growing crops, grass etc.

The following have been specifically included within the definition of the term ‘goods’ under the Act: (i) stock and shares, growing crops, grass, and (ii) things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale.

It may be noted here that under section 3 of the Transfer of Property Act, 1882, “immovable property” does not include standing timber, growing crops or grass.

²⁴ S. 5 (2).

²⁵ S. 56, Companies Act, 2013.

²⁶ S. 5 (1), Sale of Goods Act, 1930.

²⁷ Sale of Goods Act, 1930.

These things, therefore, are moveable property and thus goods. Standing timber is distinct from trees, the former being moveable and the latter being immovable property. Explaining the basis of the distinction, the Supreme Court in *Shantabai v. State of Bombay*²⁸ observed:

Before a tree can be regarded as standing timber, it must be in such a state that, if cut, it would be used as timber, and when in that state it must be cut reasonable early. The legal basis for the Rule is that trees that are not cut continue to draw nourishment from the soil.

In *M/s Mukesh Kumar Aggrawal & Co v. State of M.P.*,²⁹ it has been held by the Supreme Court that the word timber should be understood in its common parlance, i.e. wood meant for building or carpentry, and, therefore, stacks of “Eucalyptus-wood” after separating “Ballies” and “Poles” is not timber for the purpose of levying sales tax.

Section 3 (26) of the General Clauses Act, 1897, defines “immovable” property to include land, benefits to arise out of land, and things attached to the earth, or permanently, fastened to anything attached to the earth. Section 3 of the Transfer of Property Act defines “attached to the earth”, which means:

- i. rooted in the earth, as in the case of trees and shrubs;
- ii. imbedded in the earth, as in case of walls or buildings; or
- iii. attached to what is so imbedded for the permanent beneficial enjoyment of that to which it is attached.

It may be noted that the things attached to or forming part of the land, though immovable property, fall within the definition of goods, if they are agreed to be severed before sale or under the contract of sale. Thus, trees or doors and windows could be severed from the land, and sold as goods.

Actionable Claims and Money not included

‘Actionable claims’ means claims which can be enforced by a legal action or a suit. The transfer of actionable claims is made by “assignment” under Chapter VIII (Sections 130 to 137) of the Transfer of Property Act, 1882, and, therefore, the transfer of the same has been specifically excluded by the Sale of Goods Act. Section 3 of the Transfer of Property Act defines actionable claim as under:

“actionable claim” means a claim to any debt, other than a debt secured by mortgage of immovable property or by hypothecation or pledge of movable

²⁸ AIR 1958 SC 532. At 537, per Vivian Bose, J.

²⁹ AIR 1988 SC 563.

property, or to any beneficial interest in movable property not in the possession, either actual or constructive, of the claimant, which the Civil Courts recognise as affording grounds for relief, whether such debt or beneficial interest be existent, accruing, conditional or contingent.

An actionable claim, therefore, means, either:

- i. Any unsecured debt; or
- ii. Any beneficial interest in movable property, not in the possession of the claimant.

A claim for the arrears of rent, or a claim in respect of salary, or a claim in respect of a prize on a lottery ticket, or a claim on an insurance policy are the examples of actionable claims, which could be transferred by assignment under the Transfer of Property Act.

Money means the recognised currency in circulation, and for obvious reasons it is not subject matter of sale of goods. Money constitutes consideration for the sale of goods, rather than itself being goods. Old and rare coins,³⁰ however, are goods, and they can be sold or purchased as such.

Water, Electricity and Gas

While defining goods, the Sale of Goods Act does not make any mention of water, electricity and gas. This matter attracted the attention of the Law Commission of India and it has stated in its report on the Sale of Goods Act that: “In view of the fact that contracts with regard to the supply of electrical energy and water are common, we think that the matter should be placed beyond doubt and amendment should be made in section 2 (7) so as to include power in the shape of electrical energy, water and gas within the definition of “goods”.”³¹

Consequent to the recommendations of the Law Commission, some amendments were made in the Sale of Goods Act in 1963 but somehow section 2 (7) has been allowed to remain unamended.

In *The Commissioner of Sales Tax, Madhya Pradesh v. Madhya Pradesh Electricity Board*,³² the question before the Honourable Supreme Court was that whether electric energy could be considered to be goods for the purpose of sales tax. The Court observed as follows:

The term “movable property” with reference to “goods” as defined for the purposes of sales tax cannot be taken in a narrow sense and merely because electric energy is not tangible or cannot be moved or touched like, for instance, a piece of wood or a book, it cannot cease to be movable property

³⁰ *Moss v. Hancock*, (1899) 1 Q.B. 111.

³¹ Law Commission of India, 8th Report, (1958) p. 3.

³² AIR 1970 SC 732.

when it has all the attributes of such property... It can be transmitted, transferred, delivered, stored, possessed, etc., in the same way as any other movable property... If there can be sale and purchase of electric energy like any other movable object, we see no difficulty in holding that electric energy was intended to be covered by the definition of “goods”...

The Calcutta High Court in *Associated Power Co. Ltd. V. Ram Taran Roy*,³³ has held that electric energy is included in the term “goods”. The High Court disagreed with Pollock and Mulla, who considered the inclusion of the term electrical energy in the term goods as doubtful.³⁴

In *Jabalpur Cable Network Pvt. Ltd. V. E.S.P.N. Software India Pvt. Ltd.*,³⁵ following the Supreme Court decision in *Commissioner Sales Tax, electronic T.V. signals* have been held to be “goods” since they are in the form of energy just like electricity and hence can be the subject matter of sale.

Different kinds of goods

Goods which form the subject matter of any contract of sale can be classified into various categories. This classification helps in determining as to when does the property in the goods pass from the seller to the buyer.

Existing and Future Goods

According to section 6(1), the goods may either be existing goods or future goods. Existing goods are such goods as are owned or possessed by the seller at the time of making of contract. For example, the seller agrees to supply sugar which is lying in his godown, such sugar will be considered to be existing goods.

Section 2(6) defines “future goods” to mean goods to be manufactured or produced or acquired by the seller after making of the contract of sale. An agreement to supply wheat which has yet to be grown, or watches which have yet to be manufactured, or machinery which has to be imported, or cloth which has to be purchased from the market is a contract in respect of future goods.

Specific and Unascertained Goods

Existing goods may further be classified into specific goods and unascertained goods. Section 2 (14) defines “specific goods” to mean goods identified and agreed upon at the time a contract of sale is made. For example, A has a number of horses and out of them he sells his white horse to B which is identified and agreed upon at the time of

³³ AIR 1970 Cal. 75.

³⁴ Ibid at p. 78.

³⁵ AIR 1999 MP 271.

the contract, the same is then considered to be specific goods. Similarly, if A agrees to sell 100 bags of wheat to B and for the purpose of that contract, out of 1,000 bags, which he has in his godown, he earmarks 100 bags at the time of making his contract with B, the goods sold are specific.

On the other hand, if the goods are not identified and agreed upon at the time of making the contract, such goods are known as unascertained goods. For example, A having 1,000 bags of wheat in his godown sells only 100 bags to B without specifying those which he wants to deliver to B, it is a sale of unascertained goods. This distinction is important as it clarifies as to when the property in the goods passes from the seller to the buyer. Section 18 clarifies that in the case of a contract for the sale of unascertained goods, no property in the goods is transferred to the buyer unless and until the goods are ascertained. In the case of specific goods, the property passes when the parties so intend.³⁶

c) **Transfer of Property (Ownership) in the Goods**

‘Property’ here means ‘ownership’. Transfer of property in the goods is another essential of a contract of sale of goods. A mere transfer of possession of the goods cannot be termed as sale. To constitute a contract of sale the seller must either transfer or agree to transfer the property in the goods to the buyer. The Sale of Goods Act, 1930, clarifies it under section 2 (11) that ‘property’ means the general property in goods, and not merely a special property. The term ‘general property’ means ownership and special property means only some rights such as rights of possession and use. If under a contract the ownership in the goods is transferred from one person to another, it may be a contract of sale, but when mere right of possession is transferred, the transaction may be by way of hire or pledge. Transfer of property i.e. the ownership in the goods from the seller to the buyer, is the essence of a contract of sale.

Sale and Agreement to sell

Where under a contract of sale the property in the goods is transferred from the seller to the buyer, the contract is called a sale, but where the transfer of the property in the goods is to take place at a future time or subject to some condition thereafter to be fulfilled, the contract is called an agreement to sell.³⁷ An agreement to sell becomes a sale when the time elapses or the conditions are fulfilled subject to which the property in the goods is to be transferred.³⁸ There may be a contract for the sale of goods the acquisition of which by the seller depends upon a contingency which may or may not happen.³⁹ Where by a contract of sale the seller purports to effect a present sale of future goods, the contract operates as an agreement to sell the goods.⁴⁰

³⁶ S. 19 (1).

³⁷ S. 4 (3).

³⁸ S. 4 (4).

³⁹ S. 6 (2).

⁴⁰ S. 6 (3).

The 'contract of sale' is a generic term and includes both sale and an agreement to sell. The sale is an executed or absolute contract whereas 'an agreement to sell' is an executory contract and implies a conditional sale.

d) Price

The consideration of a contract of sale is termed as 'price'. It is defined under section 2 (10) to mean the money consideration for a sale of goods. If the consideration is not in terms of money, it may be a contract other than that of sale. For example, when goods are exchanged for goods, it is a contract of barter or exchange.

Modes of determination of price

The price is an essential element in every contract of sale of goods. It may be fixed by one or the other of the following modes:⁴¹

- i. It may be fixed by the contract itself. This is the most usual way of fixing the price. When the parties make a contract of sale, they generally also make a mention of the price which has to be paid for the goods.
- ii. It may be left to be fixed in manner thereby agreed. The parties may not fix the price by the contract but may leave it to be determined according to the manner agreed. It may, for example, be agreed that the market price prevailing on the date of the supply of goods will be the price to be paid, or the price as determined by a third party will be the price for the goods. Section 10 (1) provides that if a third party who is supposed to make the valuation cannot or does not make such valuation, the agreement is thereby avoided. The proviso further clarifies that if the goods or any part thereof have already been delivered to, and appropriated by, the buyer, he shall pay a reasonable price therefor. Section 10 (2) further points out in case the third party is prevented from making the valuation by the fault of the seller or the buyer, the party not in fault may maintain a suit for damages against the party in fault.

In *Aluminium Industries Ltd. V. Minerals and Metals Trading Corpn.*,⁴² the agreement stipulated that the price prevailing on the date of delivery will be the price to be paid by the buyer. Subsequently, the seller issued delivery note for the goods but without any valid reason delayed the delivery of the goods. The seller then demanded increased price which occurred due to delayed delivery. It was held that the seller was at fault in delaying the delivery of the goods and, therefore, he could not compel the buyer to pay increased price of the goods.

- iii. It may be determined by the course of dealing between the parties. When the parties have neither themselves fixed the price nor agreed upon some manner for determining the same, one may take recourse to the course of dealing

⁴¹ S. 9.

⁴² AIR 1998 Mad 239.

between the parties. For example, if the buyer has been previously paying to a particular seller the price prevailing on the day of the supply of goods, the course of dealing suggests that in subsequent transactions also the prevailing market price will be paid.

Where the price is not determined according to any of the above stated manners, section 9 (2) provides that the buyer shall pay the seller a reasonable price. What is reasonable price is a question of fact dependent on the circumstances of each particular case.

An important point which may be noted here is that a contract of sale which provides for the future fixation of price either by the parties themselves or by a third party is not void by virtue of section 29 of the Indian Contract Act, 1872. Such a contract is capable of being made certain and hence does not attract the said section 29.