
(2011) 08 DEL CK 0387
In the Delhi High Court
Case No : FAO (OS) No. 240 of 2008

Gail (India) Limited

APPELLANT

Vs

Geo Miller and Company Ltd.

RESPONDENT

Date of Decision : 30-08-2011

Acts Referred:

Contract Act, 1872 — Section 73, 74

Citation : (2011) 10 AD 162 : (2011) 3 ARBLR 299 : (2011) 183 DLT 16

Hon'ble Judges : Vikramajit Sen, J; Siddharth Mridul, J

Bench : Division Bench

Advocate : Jagjit Singh, for the Appellant; S.D. Singh and Rahul Singh, for the Respondent

Final Decision : Dismissed

Judgement

Vikramajit Sen, J.—The neat question which arises for our consideration in this Appeal is whether the Arbitrator as well as the learned Single Judge fell into error in awarding the sum of ` 22,29,840/-, avowedly withheld by the Appellant on account of liquidated damages. According to Mr. Jagjit Singh, learned Counsel for the Appellant, the Award was facially in excess of the jurisdiction and the powers reposed in the Arbitrator as it transgressed Clause 27 of the Contract dealing with compensation for delay (liquidated damages). Learned Counsel for the Appellant has relied on - (i) Bharat Coking Coal Ltd. Vs. Annapurna Construction, where Their Lordships had found that the Arbitrator had exceeded his jurisdiction inasmuch as it had not taken into consideration relevant clauses of the contract for purposes of determining the fact situation. (ii) West Bengal State Warehousing Corporation and Another Vs. Sushil Kumar Kayan and Others, the finding is to the effect that the Arbitrator rejected the plea that the value of the stolen goods should be restricted to their declared value. Clearly, however, this is not the factual matrix before us. (iii) Rajasthan State Mines and Minerals Limited Vs. Eastern Engineering Enterprises and Another, the Supreme Court opined that if the fundamental terms of an agreement are ignored by the arbitrator, he acts

in excess of his jurisdiction. This is again of No. relevance to the contentions raised before us. (iv) In Steel Authority of India Limited Vs. J.C. Budharaja, Government and Mining Contractor, the arbitrator awarded damages or compensation ignoring the prohibition contained in that contract. It was held that the Arbitrator had travelled beyond his jurisdiction.(v) Finally, the following paragraphs from Oil and Natural Gas Corporation Ltd. Vs. SAW Pipes Ltd., have been pressed for our consideration:

66. In *Maula Bux Vs. Union of India (UOI)*, the Court has specifically held that it is true that in every case of breach of contract the person aggrieved by the breach is not required to prove actual loss or damage suffered by him before he can claim a decree and the Court is competent to award reasonable compensation in a case of breach even if No. actual damages is proved to have been suffered in consequence of the breach of contract. The Court has also specifically held that in case of breach of some contracts it may be impossible for the Court to assess compensation arising from breach.

67. Take for illustration construction of a road or a bridge. If there is delay in completing the construction of road or bridge within stipulated time, then it would be difficult to prove how much loss is suffered by the Society/State. Similarly in the present case, delay took place in deployment of rigs and on that basis actual production of gas from platform B-121 had to be changed. It is undoubtedly true that the witness has stated that redeployment plan was made keeping in mind several constraints including shortage of casing pipes. Arbitral Tribunal, therefore, took into consideration the aforesaid statement volunteered by the witness that shortage of casing pipes was only one of the several reasons and not the only reason which led to change in deployment of plan or redeployment of rigs Trident-II platform B-121. In our view, in such a contract, it would be difficult to prove exact loss or damage which the parties suffer because of the breach thereof. In such a situation, if the parties have pre-estimated such loss after clear understanding, it would be totally unjustified to arrive at the conclusion that party who has committed breach of the contract is not liable to pay compensation. It would be against the specific provisions of Section 73 and 74 of the Indian Contract Act. There was nothing on record that compensation contemplated by the parties was in any way unreasonable. It has been specifically mentioned that it was an agreed genuine pre-estimate of damages duly agreed by the parties. It was also mentioned that the liquidated damages are not by way of penalty. It was also provided in the contract that such damages are to be recovered by the purchaser from the bills for payment of the cost of material submitted by the contractor. No. evidence is led by the claimant to establish that stipulated condition was by way of penalty or the compensation contemplated was, in any way, unreasonable. There was No. reason for the tribunal not to rely upon the clear and unambiguous terms of agreement stipulating pre-estimate damages because of delay in supply of goods. Further, while extending the time for delivery of the goods, Respondent was informed that it would be required to pay stipulated damages.

68. From the aforesaid discussions, it can be held that:-

(1) Terms of the contract are required to be taken into consideration before arriving at the conclusion whether the party claiming damages is entitled to the same;

(2) If the terms are clear and unambiguous stipulating the liquidated damages in case of the breach of the contract unless it is held that such estimate of damages/ compensation is unreasonable or is by way of penalty, party who has committed the breach is required to pay such compensation and that is what is provided in Section 73 of the Contract Act.

(Emphasis supplied).

(3) Section 74 is to be read along with Section 73 and, therefore, in every case of breach of contract, the person aggrieved by the breach is not required to prove actual loss or damage suffered by him before he can claim a decree. The Court is competent to award reasonable compensation in case of breach even if No. actual damage is proved to have been suffered in consequence of the breach of a contract.

(4) In some contracts, it would be impossible for the Court to assess the compensation arising from breach and if the compensation contemplated is not by way of penalty or unreasonable, Court can award the same if it is genuine pre-estimate by the parties as the measure of reasonable compensation.

2. We had considered the law on this subject in *Bharat Sanchar Nigam Limited v. BWL Limited*, 2011 IV AD (Delhi) 302 and we remained steadfast to our appreciation of the law in that decision.

3. Both *Maula Bux Vs. Union of India (UOI)*, (Three-Judge Bench) as well as *Saw Pipes Ltd. (Two-Judge Bench)* are constrained to charter a course in consonance with the enunciation of law by the Constitution Bench in *Fateh Chand Vs. Balkishan Das*, After reproducing Section 74 of the Indian Contract Act, 1872, the Constitution Bench had expounded the law in the following words:

8. ...

The section is clearly an attempt to eliminate the somewhat elaborate refinements made under the English common law in distinguishing between stipulations providing for payment of liquidated damages and stipulations in the nature of penalty. Under the common law a genuine pre-estimate of damages by mutual agreement is regarded as a stipulation naming liquidated damages and binding between the parties: a stipulation in a contract in terrorem is a penalty and the Court refuses to enforce it, awarding to the aggrieved party only reasonable compensation. The Indian Legislature has sought to cut across the web of rules and presumptions under the English common law, by enacting a uniform principle applicable to all stipulations naming amounts to be paid in case of breach, and stipulations by way of penalty.

9. The second clause of the contract provides that if for any reason the vendee fails to get the sale-deed registered by the date stipulated, the amount of Rs. 25,000/- (Rs. 1,000/- paid as earnest money and Rs. 24,000/- paid out of the price on delivery of possession) shall stand forfeited and the agreement shall be deemed cancelled. The covenant for forfeiture of Rs. 24,000/- is manifestly a stipulation by way of penalty.

10. Section 74 of the Indian Contract Act deals with the measure of damages in two classes of cases (i) where the contract names a sum to be paid in case of breach and (ii) where the contract contains any other stipulation by way of penalty. We are in the present case not concerned to decide whether a covenant of forfeiture of deposit for due performance of a contract falls within the first class. The measure of damages in the case of breach of a stipulation by way of penalty is by Section 74 reasonable compensation not exceeding the penalty stipulated for. In assessing damages the Court has, subject to the limit of the penalty stipulated, jurisdiction to award such compensation as it deems reasonable having regard to all the circumstances of the case. Jurisdiction of the Court to award compensation in case of breach of contract is unqualified except as to the maximum stipulated; but compensation has to be reasonable, and that imposes upon the Court duty to award compensation according to settled principles. The section undoubtedly says that the aggrieved party is entitled to receive compensation from the party who has broken the contract, whether or not actual damage or loss is proved to have been caused by the breach. Thereby it merely dispenses with proof of "actual loss or damages"; it does not justify the award of compensation when in consequence of the breach no legal injury at all has resulted, because compensation for breach of contract can be awarded to make good loss or damage which naturally arose in the usual course of things, or which the parties knew when they made the contract, to be likely to result from the breach.

11. Before turning to the question about the compensation which may be awarded to the Plaintiff, it is necessary to consider whether Section 74 applies to stipulations for forfeiture of amounts deposited or paid under the contract. It was urged that the section deals in terms with the right to receive from the party who has broken the contract reasonable compensation and not the right to forfeit what has already been received by the party aggrieved. There is however no warrant for the assumption made by some of the High Courts in India, that Section 74 applies only to cases where the aggrieved party is seeking to receive some amount on breach of contract and not to cases where upon breach of contract an amount received under the contract is sought to be forfeited. In our judgment the expression "the contract contains any other stipulation by way of penalty" comprehensively applies to every covenant involving a penalty whether it is for payment on breach of contract of money or delivery of property in future, or for forfeiture of right to money or other property already delivered. Duty not to enforce the penalty clause but only to award reasonable compensation is statutorily imposed upon courts by Section 74. In all cases, therefore, where

there is a stipulation in the nature of penalty for forfeiture of an amount deposited pursuant to the terms of contract which expressly provides for forfeiture, the court has jurisdiction to award such sum only as it considers reasonable, but not exceeding the amount specified in the contract as liable to forfeiture.

4. We must immediately advert to Clause 27 of the Contract, which is at the fulcrum of this fight, and hence requires reproduction:

27.0 Compensation for Delay (Liquidated Damages)

27.1 Time is the essence of the contract. In case the Contractor fails to complete the work within the stipulated period then, unless, such failure is due to force majeure as defined in Clause 26 hereinabove or due to owner's default, the contractor shall pay to the owner by way of compensation for delay and not as penalty, a sum @ 1/2% (half percent) of the value of contract for delay per week on pro-rata or part thereof subject to a maximum of 10% (ten percent) of the value of contract. The parties agree that this is a genuine pre-estimate of the loss/damage which will be suffered on account of delay/breach on the part of the contractor and the said amount will be payable on demand without there any being any proof of the actual loss or damages caused by such delay/breach.

The decision of the Engineer in charge in regard to applicability of compensation for delay shall be final and binding on the contractor.

27.2 All sums payable by way of compensation under any of the conditions and shall be considered as reasonable compensation without reference to the actual loss or damage which shall have been sustained.

The Clause ordains firstly that time is of the essence which is significant because it runs counter to the assumption that in building or construction contracts time is not usually or normally of the essence. Secondly, it postulates that if delay or failure is due either to force majeure or to the owners' default, compensation will not be imposable. Thirdly, it reiterates the legal position obtaining in India that a penalty cannot be inflicted, which appears to be what has actually transpired. Fourthly, the clause stipulates a ceiling of damage at ten per cent of the value of the contract. Fifthly, only half per cent of the value of the contract can be imposed for each week's delay. Sixthly, it reiterates that these liquidated damages are in the nature of a genuine pre-estimate of loss, thus obviating the need to compute, with exactitude, the actual damages suffered by the owners. Lastly and seventhly, it gives finality to the decision of the Engineer Incharge with regard to the applicability of compensation. It appears to us that all these concomitants have not occurred in the circumstances of the present case.

5. We have perused the Award which had been unsuccessfully assailed by the Appellant before the learned Single Judge. The Claim with which we are concerned has been formulated and tabulated by the Arbitrator thus:

Withheld as liquidated damages.

In (Rupees)

Value of Civil contract 4 withheld for delay @ 9.78% of 86,60,000

8,46,948

Value of mechanical work withheld for delay @9.78% of 1,41,40,000

13,82,892

Total withheld as LD

22,29,840

6. The findings in the Award, so far as delay is concerned, are as follows:

4. The Claimants also submitted that various other reasons such as delay in approval of basic engg. Package, quality plan, data sheets and approval of vendor also contributed to delay from time to time.

On going through the documents attached to the Statement of Claim, I hold that delay has taken place on these counts which has a cascading effect on the progress of the work.

It is apparent that various reasons as above, such as the major delay in release of mobilization advance and delay in commencement of work due to Claimants inability to carry out necessary extra work arising out of shifting of site agitation and unusual monsoon etc. had serious implications on the completion of the contract which was required to be completed within a short period of 10 months. Accepting these realities, EIL, Engineer Incharge of the Respondents, had recommended extension for delay upto 22.10.1998 (actual date of completion). It is worthwhile to mention here that in terms of Clause No. 27.1 of Tender documents dealing with liquidated damages, the decision of the Engineer Incharge regarding the applicability of compensation for delay, shall be final and binding on the contractor.

I hold that because of delays beyond control of the Claimants for which Respondents were fully responsible and because of the recommendations of the Engineer Incharge for extension of delay, the liquidated damages amounting to Rs. 22,29,840/- cannot be imposed on the Claimants by the Respondents.

7. The learned Single Judge has concluded that Clause 27 of the Contract has not been violated, and we think rightly so. The Claim of the Respondent, simply stated, is for payment of amounts illegally withheld by the Appellant. No evidence has been led before the Engineer Incharge or the Arbitrator, or for that matter before the learned Single Judge (as it could not have been done), disclosing that the Engineer Incharge had computed "actual loss or damage caused by such delay/breach." In order to justify the withholding of this payment, it was essential for the Appellant to provide proof before the Arbitrator that the Engineer Incharge had consciously gone into this question and was satisfied that the loss or damage had actually occurred in circumstances where

the owner/Appellant was not blameworthy, and also that force majeure had not occurred. There is not even a shred or iota of proof sustaining this claim. It is wholly insufficient for the Appellant to merely assert that delay had occurred. The appropriate adjudicating forum was legally bound to arrive at an informal conclusion. Clause 27 accords finality to the decision of the Engineer Incharge in clear contradistinction to the Arbitrator whose jurisdiction with regard to this determination has been removed. The decision of the Engineer Incharge has been rendered impervious to any challenge before the Arbitral Tribunal. Stipulations such as those articulated in Clause 27 are variously termed as "excluded" or "exempted" matters which, simply stated, remove their consideration or determination from the Arbitral Tribunal or the Court and place them in the exclusive province of the nominated/indicated adjudicator that the party claiming liquidated damages was not itself responsible for the breach of the contract and that the said claimant was not acting in terrorem by enforcing a penalty. This does not, however, mean that even in the absence of any determination, the principal can unilaterally withhold amounts masquerading them to be within the domain of damages.

8. In other words, had the Engineer Incharge made a determination of damages which were payable by the Respondent to the Appellant because of delay caused by and attributable to the Respondent, and if such exercise has been rendered futile by a contrary conclusion of either the Arbitral Tribunal or the learned Single Judge, the decision of the Engineer Incharge would have to be upheld since it holds the field. This is not what has happened in the case before us.

9. Furthermore, admittedly, the Contract was delayed for a period of eleven weeks. If Clause 27 is to be applied, only 5.5 per cent of the value of the Contract could have been ascertained as damages, not unilaterally and without authority by the Appellant, but we reiterate by the Engineer Incharge. The highhandedness of the Appellant is manifest from the fact that the sum of ` 22,29,840/- corresponds to ten per cent of the value of the subject contract which was accordingly incorrect and, therefore, unsustainable by any determination.

10. For these manifold reasons, we find No. error in the impugned Order or in the impugned Award. The Arbitrator has awarded interest at the rate of eighteen per cent per annum which has been reduced by the learned Single Judge to eight per cent per annum, predicated on Krishna Bhagya Jala Nigam Ltd. Vs. G. Harischandra Reddy and Another,

11. The Appeal is wholly devoid of merit and is dismissed with costs of ` 50,000/-. Public Sector Undertakings such as the Appellant should not needlessly exhaust the scarce time of the courts by filing frivolous appeals. Costs should have been punitive but we restrict them to the aforesaid sum. The amount deposited by the Appellant with the Registrar-General of this Court be released to the Respondent forthwith.