

(2002) 06 MAD CK 0060

In the Madras High Court

Case No : Original Side Appeal No. 102 of 1993

Macbrite Engineers by Prop. Mr. P.N. Shamra

APPELLANT

Vs

Tamil Nadu Sugar Corporation Ltd.

RESPONDENT

Date of Decision : 07-06-2002

Acts Referred:

Contract Act, 1872 — Section 74

Citation : AIR 2002 Mad 429 : (2003) 1 LW 420 : (2002) 2 MLJ 636

Hon'ble Judges : R. Jayasimha Babu, J;A. Kulasekaran, J

Bench : Division Bench

Advocate : G. Vimal, for G.V.S. Iyer, for the Appellant; P. Punniyakoti, for the Respondent

Final Decision : Allowed

Judgement

A. Kulasekaran,J.

1. Plaintiff is the appellant.

2. The suit was filed for recovery of a sum of Rs.1,87,322.40 together with interest on Rs.1,11,335.75 at 19.5% per annum, from the date of

plaint till the date of realisation. The factual matrix of the case is as follows:-

The defendant has placed orders on 20.2.1985 and 28.2.1985 for supply of five machines with the plaintiff, subject to the terms and conditions

that if supply was not effected on or before 15.3.1985, penalty of 1% on the total value of the supply would be imposed for every three days of

delay subject to the maximum of 10%. The plaintiff has also intimated by letter dated 5.3.1985 that the penalty clause was not agreeable to them

as the machines ordered are special in nature, however, agreed to supply the same within the stipulated period and the defendant has sent a reply

dated 15-03-1985 intending to relax the penalty clause provided the machines were kept ready for inspection within three months. The Plaintiff has sent a letter dated 14-06-1985 and sought for further extension and not to apply penalty clause. On 1.7.1985, the defendant has sent a letter to the plaintiff extending the time for supply of the machines upto 15.7.1985, in default they would impose penalty clause. On 2.7.1985, the plaintiff informed the defendant that the machines were ready for inspection. The inspection was also done by the defendant. The defendant has sent a letter dated 7.8.1985 demanding to rectify some defects pointed by the Engineers, before despatching the machines, which were rectified. The machines were supplied between 29.8.1985 and 23.1.1986. It is the case of the defendant that there was delay of 44 to 215 days. The defendant settled the bills after deducting the penalty amount of 10%. Hence, the suit is filed.

3. The Trial court framed the below mentioned issues:-

- i) Whether the defendants have accepted the amendment clause by their letter dated 15.3.1985?
- ii) Whether the defendants can withhold the suit claim by way of liquidated damages?
- iii) Whether the plaintiff is entitled to loading charges of Rs.11,800/=?
- iv) Whether the plaintiff is entitled to the suit claim?
- v) Whether the plaintiff is entitled to interest as it is a commercial transaction?
- vi) To what relief are the parties entitled?

4. The plaintiff examined PW1 and marked Exs.P1 to P21. No oral evidence was let in by the defendant, but marked Ex.D1. The Trial court has decided all the issues against the plaintiff.

5. Learned counsel appearing for the appellant/plaintiff argued that in the very first letter dated 5.3.1985, the plaintiff has communicated to the defendant that the penalty clause was not agreeable, that penalty clause was not binding on the plaintiff as the same was illegal, unlawful and onerous and that the delay in supply of machines was due to severe power cut in their area and curfew was clamped by Government for ten days which was beyond their control, however, the machines were supplied in the year 1985 itself; and that even if the plaintiff had supplied the

machines earlier, the defendant could not have used as no electricity connection in their factory. The learned counsel further argued that the

defendant has not let in evidence to show the alleged loss or damages suffered by them due to delay in supply of machines whileso, the penalty

levied was unjustifiable. The learned counsel for the appellant/plaintiff further argued that time was not the essence of the contract. It is also

submitted on behalf of the plaintiff that crane charges and lorry detention charges incurred by the plaintiff were to be reimbursed by the defendant

as they have not provided crane to unload the machines which were brought to their factory. The learned counsel for the appellant/plaintiff further

submitted that advocate notice dated 3.4.1980 was sent calling upon the defendant to pay the entire amounts. The defendant though sent reply

dated 16.2.1989 stating that the matter was under examination failed to comply with, without any valid reasons.

6. The learned counsel for the defendant contended that time was extended at the request of the Plaintiff on several occasions, but, the machines

were not supplied within the time extended. The learned counsel further argued that as per the covenant in agreement of supply of the machines,

they have deducted 10% in the net amount towards penalty, no valid evidence was let in by the plaintiff to make the defendant liable, a sum of

Rs.11,800/- towards crane and lorry detention charges and justified the judgment passed by the learned Single Judge.

7. Learned Single Judge, relying on Exs.P1 to P5, held that delivery was effected beyond the stipulated period, hence the plaintiff was liable to pay

penalty. The plaintiff has sent a letter Ex.P6 dated 5.3.1985 disputing the penalty clause and the defendant has sent a reply Ex.P7 dated 15.3.1985

agreeing to relax the condition provided that the supply of machines were completed within the further extended three months. Ex.P8 dated

14.6.1985 letter was sent by the plaintiff to the defendant mentioning various reasons for the delay. Under Ex.P9 dated 01-07-1985, the

defendant has extended the time till 15.7.1985. The learned Single Judge, relying on Exs.P1 to P5, P8 and P9 has come to the conclusion that

application of penalty clause was by the defendants was valid since the supply of machines was not completed before the last extended period i.e.,

15.7.1985 and no evidence was produced to justify that a sum of Rs.11,800/- in respect of crane charges and also lorry detention charges were

payable by the defendants.

8. The learned counsel for the appellant/Plaintiff relied on the following decisions:-

I) Fateh Chand Vs. Balkishan Das, wherein in Para-16 it was held thus:-

There is no evidence that any loss was suffered by the plaintiff in consequence of the default by the defendant, save as to the loss suffered by him

being kept out of possession of the property. There is no evidence that the property had depreciated in value since the date of the contract

provided; nor was there evidence that any other special damage had resulted. The contract provided for forfeiture of Rs.25,000/- consisting of

Rs.1,000/- paid as earnest money and Rs.24,000/- paid as part of the purchase price. The defendant has conceded that the plaintiff was entitled to

forfeit the amount of Rs.1,000/- which was paid as earnest money. We cannot however agree with the High Court that 13 per cent of the price

may be regarded as reasonable compensation in relation to the value of the contract as a whole, as that in our opinion is assessed on an arbitrary

assumption. The plaintiff failed to prove the loss suffered by him in consequence of the breach of the contract committed by the defendant and we

are unable to find any principle on which compensation equal to ten percent to the agreed price could be awarded to the plaintiff. The plaintiff has

been allowed Rs.1,000/- which was the earnest money as part of the damages. Besides, he had use of the remaining sum of Rs.24,000/- and we

can rightly presume that he must have been deriving advantage from that amount throughout this period. In the absence therefore of any proof of

damage arising from the breach of the contract, we are of opinion that the amount of Rs.1,000/- (earnest money) which has been forfeited, and the

advantage that the plaintiff must have derived from the possession of the remaining sum of Rs.24,000/- during all this period would be sufficient

compensation to him. It may be added that the plaintiff has separately claimed mesne profits for being kept out of possession for which he has got

a decree and therefore the fact that the plaintiff was out of possession cannot be taken into account in determining the damages for this purpose.

The decree passed by the High Court awarding Rs.11,250/- as damages to the plaintiff must therefore be set aside.

In this case, 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. Section 74 undoubtedly says that 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. Incidentally, in this case, the Apex Court has observed that there is no principle on which compensation equal to 10% of the agreed price could be awarded to the plaintiff even where he has failed to prove any loss suffered by him.

II) In *Maula Bux Vs. Union of India (UOI)*, , it is held that

8. ... 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 case of breach even if no actual damage is proved to have been suffered in consequence of the breach of contract. But the expression "whether or not actual damage or loss is provided to have been caused thereby" is intended to cover different classes of contracts which come before the Courts. In case of breach of some contracts it may be impossible for the Court to assess compensation arising from breach, while in other cases compensation can be calculated in accordance with established rules. Where the Court is unable to assess the compensation, the sum named by the parties if it be regarded as a genuine pre-estimate may be taken into consideration as the measure of reasonable compensation, but not if the sum named is in the nature of a penalty. Where loss in terms of money can be determined, the party claiming compensation must prove the loss suffered by him.

In this case, the Supreme Court has held that in every case of breach of contract the person aggrieved by the breach is not required to prove the actual loss or damage suffered by him before he can claim a decree, and 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 contract. It is also held by the Apex Court that in case of breach of some contracts it may be impossible for the court to assess

compensation arising from breach, while in other cases compensation can be calculated in accordance with established rules. Where the court is unable to assess the compensation the sum named by the parties, if it be regarded as a genuine pre-estimate may be taken into consideration as the measure of reasonable compensation, but not if the sum named is in the nature of a penalty. Where loss in terms of money can be determined, the party claiming compensation must prove the loss suffered by him. The Supreme Court has further held that the claimant is not entitled to any interest prior to the date of the suit.

III. In *State of U.P. Vs. Chandra Gupta and Co.*, a Division Bench of the Allahabad High Court, following the judgment of the Apex Court in

Maula Bux Vs. Union of India (UOI), and the judgment in *Union of India (UOI) Vs. Rampur Distillery and Chemical Co., Ltd.*, has held that

sec.74 entitles a person complaining of breach of contract to get reasonable compensation and does not entitle him to realise anything by way of

penalty. If a contract is not duly performed but still no damage is suffered on account of non-performance, the promisee would not be entitled to

get damages. In paragraphs 18 and 19 of the above said judgment, it has been held that,

After having heard counsel for the parties, we are inclined to accept the submission advanced on behalf of the respondent. Section 74 of the

Indian Contract Act entitles a person to get reasonable compensation and does not entitle him to realise anything by way of penalty. If a contract is

not duly performed but still no damage is suffered on account of non-performance, the promisee would not be entitled to get damages.

A similar question regarding the right of the Union of India to forfeit the security came up for consideration before the Supreme Court in *Maula Bux*

Vs. Union of India (UOI), . In that cause, Maula Bux had entered into a contract with the Government of India for the supply of certain goods and

had deposited certain amount of security for the due performance of the contract. It was stipulated in the contract that the amount of security was

to stand forfeited in case the appellant neglected to perform his part of the contract. On Maula Bux committing default in the supply, the

Government did not only rescind the contract but also forfeit the security deposit. Holding that a case of forfeiture of earnest money was different

from forfeiture of security deposit for due performance of the contract, the Supreme Court held that u/s 74 only reasonable amount can be

forfeited if a contract is not performed. But, where under the terms of the contract the party in breach has undertaken to pay a sum of money or to

forfeit a sum of money which he has already paid to the party complaining of a breach of contract, the undertaking is of the nature of penalty. It

further held that the amount deposited by way of security for guaranteeing the due performance of the contract could not be regarded as earnest

money. Applying the law to the facts of the present case, we find that as the defendant, admittedly, did not suffer any damage it was not entitled to

forfeit the security deposit, inasmuch as forfeiture of security would amount to imposition of penalty. This case was followed by the Supreme Court

in Union of India (UOI) Vs. Rampur Distillery and Chemical Co., Ltd., . It was held in this case that the party to a contract taking security deposit

from the other party to ensure due performance of the contract is not entitled to forfeit the security deposit on the ground of default, when no loss is

caused to him in consequence of such default. We, accordingly, find that the learned Civil Judge was not right in holding that the forfeiture of

security by the defendant in the instant case was justified. We, therefore, hold that the plaintiff is entitled to get a decree for the sum of Rs.6,650

under this head.

It is further held in the above decision that as the Government did not suffer any damage in consequence of default, it was not entitled to forfeit

security deposit inasmuch as forfeiture of security deposit would amount to imposition of penalty.

10. The above said judgments were relied on by the counsel for the appellant/plaintiff to say that under sec.74, the court is competent to award

reasonable compensation in case of breach.

11. The learned counsel appearing for the appellant/plaintiff has argued that admittedly electricity connection was given to the defendant's factory

premises only on 5.6.1986 whereas the machines were supplied in the year 1985 itself and no evidence was let in by the defendant to show the

actual loss sustained by them; that the sum named is in the nature of penalty and it is the bounden duty of the defendant to prove the loss suffered

by them and that in the absence of such proof, withholding 10% of the bill value

of the machines supplied by way of penalty is unreasonable and unsustainable in law. The learned counsel for the respondent advanced argument sustaining the dismissal of the suit by the learned Single Judge.

12. The relevant section in the Indian Contract Act relating to the facts of the present case is section 74 which runs as follows:-

When a contract has been broken, if a sum is named in the contract as the amount to be paid in case of such breach or if the contract contains

any other stipulation by way of penalty, the party complaining of the breach is entitled, whether or not actual damage or loss is proved to have

been caused thereby, to receive from the party who has broken the contract reasonable compensation not exceeding the amount so named or, as

the case may be, the penalty stipulated for.

Explanation-A stipulation for increased interest from the date of default may be a stipulation by way of penalty.

Exception-When any person enters into any bail-bond, recognizance or other instrument of the same nature, or under the provisions of any law, or

under the orders of the Central Government or of any State Government, gives any bond for the performance of any public duty or act in which the

public are interested, he shall be liable, upon breach of the condition of any such instrument, to pay the whole sum mentioned therein.

Explanation-A person who enters into a contract with Government does not necessarily thereby undertake any public duty, or promise to do and

act in which the public are interested.

13. Section 74 provides for measuring 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. In the latter case, the measure of damage is by section 74, reasonable

compensation not exceeding the penalty stipulated for. In the Judgment of the Apex Court in Fateh Chand Vs. Balkishan Das, it was observed that

sum stipulated should be paid as damages unless exorbitant, unconscionable or inequitable. Whether a stipulated sum is penalty or liquidated

damages is a question of construction to be decided upon the terms and inherent circumstances as they existed at the time of the contract and not

the breach thereof. The essence of a penalty is a payment of money stipulated as in terrorem of the offending party, the essence of liquidated

damages is a genuine covenanted pre-estimate of damages.

14. The Supreme Court has observed that 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. Section 74 of the Indian Contract Act 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 damage"; 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.

15. The words "reasonable compensation" give a wide discretion to the Court in the assessment of damages. The only restriction is that the Court

cannot decree damages exceeding the amount previously agreed upon by the parties. The discretion of the Court in the matter of reducing the

amount of damages agreed upon is left unqualified by any specific limitation, though, of course, the expression "reasonable compensation" used in

the section necessarily implies that the discretion so vested must be exercised with care, caution, and on sound principles.

16. In view of the above said observation made by the Apex court of India, considering the circumstances of the case and passage of time

between the inception of the contract and of its breach, we estimate that the defendant is entitled to compensation of 1% of the value of the order

placed by the defendant to the plaintiff without any interest. The appellant has not produced any materials to satisfy that they have incurred the

expenses of Rs.11,800/= towards crane and lorry detention charges. Hence, the claim of the appellant in respect of the same is rejected. The

defendant shall pay the balance amount after deducting the compensation of 1%

mentioned supra and also the said sum of Rs.11,800/= within a period of three months from the date of this judgment.

17. In the result, the appeal is allowed to the extent indicated above and the judgment and decree passed by the learned Single Judge is set aside.

No costs.