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Foundations of Modern Contract law: Perspectives from a Comparative Lens

Term! Are you implied or imaginary? Contract Interpretation - Subjective and Objective

The Substantive and Formal Validity of Contracts – Simplifying the Identity Crisis

Dissecting the difference between Void, Voidable and Unlawful Contracts

Contract Law Diary

Determination of Contingent Contracts – Essentials & Enforcement

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Damages for Breach of Contract in India: Legal Principles

Liquidated Damages and Penalty: No distinction under Indian Contract Act, 1872

Specific Performance of Contract: An Analysis

Covid-19: An impetus to the era of Electronic Contracts

Avoiding the manual style of exposition of law, CLD analyses the fundamental concepts and principles of contract law.

Table of Contents

02
Foundations of Modern Contract law: Perspectives from a Comparative Lens

06
Term! Are you implied or imaginary? Contract Interpretation - Subjective and Objective

14
The Substantive and Formal Validity of Contracts – Simplifying the Identity Crisis

19
Dissecting the difference between Void, Voidable and Unlawful Contracts

29
Agreements in Restraint of Legal Proceedings: An Analysis

34
Determination of Contingent Contracts – Essentials & Enforcement

40
Damages for Breach of Contract in India: Legal Principles

49
Liquidated Damages and Penalty: No distinction under Indian Contract Act, 1872

58
Specific Performance of Contract: An Analysis

64
Covid-19: An impetus to the era of Electronic Contracts

Foundations of Modern Contract law: Perspectives from a Comparative Lens

1. Introduction

1.1 How do the laws of contract vary across jurisdictions? This question has attracted a significant amount of interest of the lawyers and corporate professionals over the time. The answer to this, can be explored by examining the two prominent legal systems of the world, i.e. - common law and civil law. However, before highlighting some distinguishing features between the common law and civil law systems qua contract law, it is worthwhile to note that there is substantial complexity and divergence within the common law and civil law traditions. This essentially means that, no two jurisdictions have identical contract laws, however one may infer classifications to identify broad patterns of variation. Let's discuss some of the important distinctions.

2. Conception of Contract Law

2.1 *Pacta sunt servanda* or the sanctity of contracts is a paramount principle of modern contract law, that universally constitutes a part of municipal legal systems. It signifies that once a party has negotiated a contract and agreed to be legally bound by it, subsequent developments will in principle not allow this party to avoid or modify its contractual obligations. *Pacta sunt servanda* enjoys

very long national traditions which have been elaborated by the courts and frequently translated into statutes by the legislature. No wonder courts and tribunals across jurisdictions apply *pacta sunt servanda* either as "a transnational principle of private law" or as "a cornerstone of the *lex mercatoria*."

2.2 The Continental approach to contracts expressed in the maxim *pacta sunt servanda* famously reflects the understanding, inherited from canon law, that a contract entails as much a moral as a legal obligation. The idea that morality requires parties to live up to their obligations, then, both shapes and complements the role of the State in the civil law of contract.

2.3 The distinction is simple, in common law systems contractual obligations exist in the form of legal obligations only, whereas, in civil law systems, contractual obligations entail a moral obligation as well.

3. Duty of Good Faith

3.1 Good faith is another cardinal principle recognized by many jurisdictions across legal systems. In some civil law countries, it plays a particularly prominent role. Some common law systems may imply a duty of good faith and fair dealing; yet other common law systems allocate more value to the four corners of the agreement that the parties struck without importing additional duties of good faith in most circumstances. In this context, some legal systems derive a range of obligations from this principle, including a duty to inform the counterparty within reasonable time of an anticipated impediment, a duty to grant a grace period before termination, or a duty to engage in good faith negotiations before modifying or terminating the agreement, or before requesting a court or tribunal to do so.

3.2 Of all topics in the comparative law of contracts, perhaps none has attracted as much interest in recent times as the duty of good faith. Scholars like *Zimmerman* and *Whittaker* have devoted entire commentaries on comparative concepts of good faith. The scope of enquiry for the distinction is: whether, and to what extent, good faith operates as a source of implied contractual duties of cooperation and collaboration beyond those expressly provided in the agreement?

3.3 There is consensus that civil law jurisdictions presently contemplate a more expansive application of the duty of good faith in contract law. There is no denying that common law systems too rely on the concept of good faith to read some terms into the contract, however, most observers would probably agree that U.S. courts (for example) use good faith to imply contractual duties with less frequency and gusto than their civilian counterparts do.

4. Interpretation and Policing of Contract Terms

4.1 The more interventionist role of the State in civil law systems also sheds light on other fundamental differences in the law of contracts. Take, for instance,

the difficult issue of whether exogenous changes in circumstances after the formation of a contract should affect the parties' obligations or the terms of the agreement. Civil law courts are generally more willing than common law courts to rewrite or discharge contracts ex post if the parties did not expressly contemplate this result.

4.2 Courts in Common law systems have always invited criticism when attempting to rewrite contractual terms in view of changed circumstances. The degree of judicial intervention on contract terms has been surprising in the common law context and drew considerable criticism, not least because of the consistent declarations by courts and tribunals that they would not rewrite the deal that the parties had made.

5. Contract Remedies

5.1 The interventionist approach of civil law systems vs. the non-interventionist approach of common law systems is clearly visible in terms of contract remedies and enforcement as well. At least in principle, civil law jurisdictions regard specific performance as the primary remedy for breach of contract. By contrast, the main consequence of a breach of contract in the common law is the obligation to pay damages.

5.2 In wider terms, it can be said that once a contract passes muster under the civil law's more stringent control of contract terms, the State is also more aggressive in enforcing the agreement, both by awarding stronger contract remedies for breach and by restricting the availability of discharge in bankruptcy. While the common law's lesser scrutiny of contract terms would suggest that it is more respectful of freedom of contract, the common law's treatment of contract remedies makes State support to contract enforcement in this tradition look far more subdued.

6. Overall Distinctions: Role of State, Party Intent and Freedom of Contract

6.1 The intent of the parties is also a pervasive principle that plays a significant role in the interpretation of contracts. When interpreting contracts, most civil law jurisdictions aim at giving legal force to what the parties intended to agree on – even if this may have been expressed imperfectly in the language of the contract. In some exceptional cases, civil law jurisdictions also empower a judge or arbitrator to amend contractual provisions if the parties are faced with a situation that they had not contemplated at the time of entering the contract. The intent of the parties also plays a significant role in contract interpretation in common law jurisdictions. In many common law jurisdictions, it is the objective intent of the contract that is given primacy, based on the language of the contract. In some common law jurisdictions, courts only look to evidence outside the contract if the language is ambiguous.

6.2 Pertinently, the civil-common law divide can be attributed to the distinct role of State in these systems. The conspicuous differences highlight that the State

plays a stronger role in the civil law and a weaker role in the common law. Overall, a common law system is less prescriptive than a civil law system. There is an extensive freedom of contract when setting up a contractual relationship between two parties. Few provisions are implied into the contract by law, although safeguards often are implied to protect private consumers. As a direct result, all terms that govern the relationship between the parties need to be clearly defined in the contract itself. Such necessities often result in a contract being longer than one in a civil law country.

6.3 In general, when it comes to common law contracts, almost everything is permitted that is not expressly prohibited by law. In a common law system, judicial decisions are binding owing to doctrine of stare decisis. Decisions by the highest court can only be overturned by that same court or, in certain cases, but not all, through legislation.

6.4 In contrast, the civil law system is a codified system of law that dates all the way back to the Roman legal system. A civil law system is generally more prescriptive than a common law system. There is visibly less freedom of contract than in a common law system. Many provisions are implied into a contract by law and parties cannot contract out of certain provisions. As a direct result, less importance is placed on setting out all the terms governing the relationship between the parties to a contract. Rather than be defined in the contract itself, such inadequacies or ambiguities tend to be remedied or resolved by operation of law.

Term! Are you implied or imaginary? Contract Interpretation - Subjective and Objective

1. Introduction

1.1 In order for a dispute to move towards resolution, the most essential aspect is deciphering the origin of the dispute. Considering that contracts are merely agreements enforceable under law, the most common contractual disputes revolve around the interpretation of the terms of these agreements. Thus, it is no surprise that one of the questions most frequently posed before the adjudicator in a contractual dispute, revolves around the intention of the parties while interpreting the term(s) of the contract.

1.2 A situation like this, more often than not, arises out of the disputed understanding of a fact between the parties, the intelligibility of which is imperative in order to affix the liability on one party. This article discusses internationally prevalent legal trends with respect to the scope of interpretation of contractual terms and the consequent disputes.

1.3 This article is divided into two parts, the *first* being the comparative analysis of the legal principles prevalent on the interpretation of commercial contracts across the globe; and *second,* an overview of the *status quo* in India.

2. The Legal Principles for Interpretation of a Commercial Contract

2.1 A contract is usually construed by the literal meaning which its terms bear. The primary reason for the same is that a contract is an agreement enforceable under law,[1] and a valid contract presupposes free consent of both the parties to the contract through valid execution.[2] Two or more persons are said to consent when they agree upon the same thing in the same sense[3]. Therefore, when parties enter into a contractual relationship, the terms of the contract are paramount in determining the most accurate reflection of the combined understanding of the parties.

2.2 As established above, more often than not, the contours of the more popular contractual controversies between parties are usually concerned with the interpretation of commercial contracts. This section sets forth certain judicial pronouncements relevant to the same.

2.3 England

2.3.1 The Moorcock test

2.3.1.1 To begin with, we refer to the landmark judgment of the Moorcock, **('Moorcock Judgement')**[4] in which the Court of Appeal (Bowen, L.J.), dealt with the implied warranty on the part of the owners of the jetty to take reasonable care of a ship named 'The Moorcock', in respect of a contract made for the use of the jetty to discharge the cargo ship. It was observed that:

> *"In business transactions such as this, what the law desires to effect by the implication is to give such business efficacy to the transaction as must have been intended at all events by both parties who are business men; not impose on one side all the perils of the transaction, or to emancipate one side from the all chances of failure, but to make each party promise in law as much, at all events, as it must have been in the contemplation of both parties that he should be responsible for in respect of those perils or chances."*

2.3.1.2 The principle thus propounded was that of 'business efficacy' i.e. a term will be implied into a contract only to the extent required to give the contract efficacy in the business sense. It means that the term must give efficacy to the business transaction in view of what must have been the intended outcome of the transaction by both parties.

2.3.2 The Officious Bystander Test of 'Oh, of course!'

[1] Section 2(h) of the Indian Contract Act, 1872.
[2] Section 14 of the Indian Contract Act, 1872.
[3] Section 13 of the Indian Contract Act, 1872.
[4] The Moorcock (1889) 14 PD 64.

2.3.2.1 In another landmark case of *Shirlaw v Southern Foundries,*[1] **('Shirlaw Judgement')** it was held that a term can only be implied from the terms of the contract if it is utterly evident and needs no express mention. MacKinnon, L.J., observed as under:

> *"Prima facie that which in any contract is left to be implied and need not be expressed is something so obvious that it goes without saying; so that, if, while the parties were making their bargain, an officious bystander were to suggest some express provision for it in their agreement, they would testily suppress him with a common 'Oh, of course!' At least it is true, I think, that, if a term were never implied by a judge unless it could pass that test, he could not be held to be wrong."*

2.3.2.2 In *Reigate v Union Manufacturing Co, (Ramsbottom) Ltd.*[2] **('Reigate Judgement')**, Scrutton L.J., discussed the developments in respect of these principles and observed as under:

> *"The first thing is to see what the parties have expressed in the contract; and then an implied term is not to be added because the Court thinks it would have been reasonable to have inserted it in the contract. A term can only be implied if it is necessary in the business sense to give efficacy to the contract; that is, if it is such a term that it can confidently be said that if at the time the contract was being negotiated someone had said to the parties, "What will happen in such a case," they would both have replied, "Of course, so and so will happen; we did not trouble to say that; it is too clear." Unless the Court comes to some such conclusion as that, it ought not to imply a term which the parties themselves have not expressed."*

2.3.2.3 These landmark authorities shed light on what is essential while determining the question of interpretation. In none of them did the Court ask: "What did both parties intend?" If asked, each party would have said that they never gave it a thought, otherwise one would have intended something different from the other. Nor did the Court ask: "Is the term necessary to give business efficacy to the transaction?" If asked, the answer would have been: "It is reasonable, but it is not necessary".

2.3.2.4 It is thus evident that the courts implied a term according to whether or not it was reasonable in all the circumstances to do so. Very often it was conceded that there indeed was an implied term. The only question was with respect to the extent to which it was implied. Questions about whether it was an absolute warranty of fitness, or only a promise to use reasonable care could not be solved by inquiring into what the parties intended, or what was necessary, but only into what was reasonable, an aspect which was to be decided as matter of law, not as matter of fact.[3]

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[1] Shirlaw v. Southern Foundries (1926) L.D. (1939) 2 KB 206.
[2] Reigate v. Union Manufacturing Co, (Ramsbottom) Ltd., [1918] 1 K.B. 592.
[3] Liverpool City Council v. Irwin MANU/UKHL/0008/1976 : (1976) Q.B. 319.

2.3.3 'Mere reasonableness' or 'necessity'?

2.3.3.1 In 1969, Lord Reid put it assuredly when he said: "… no warranty ought to be implied in a contract unless it is in all the circumstances reasonable"[1]. The aforesaid judgment was later carried in appeal to the House of Lords in *Liverpool City Council v Irwin,*[2] **('Liverpool City Council Judgment')**. It was clarified that the touchstone for interpreting commercial documents, cannot be 'mere reasonableness' as Lord Denning had observed, but 'necessity', a concept which tilted more towards the *Moorcock test* or the test of 'business efficacy':

> *"I cannot agree… that it is open to us in the court at the present day to imply a term because subjectively or objectively we as individual judges think it would be reasonable so to do. It must be necessary in order to make the contract work as well as reasonable so to do, before the court can write into a contract as a matter of implication some term which the parties have themselves, assumedly deliberately, omitted to do."*

2.3.3.2 Pursuant to the trend requiring the establishment of what is reasonable and what is necessary, Lord Denning, M.R., in *Shell U.K. Ltd. vs. Lostock Garage Ltd.*[3] ***('Shell U.K. Ltd. Judgment')*** propounded two categories of implied terms:

(A) The first category- 'common relationships'

- The first category comprehends all those relationships which are of common occurrence. Such as the relationship of seller and buyer, owner and hirer, master and servant, landlord and tenant, carrier by land or by sea, contractor for building works, and so forth. In all those relationships the courts have imposed obligations on one party or the other, admitting that they are "implied terms". These obligations are not founded on the intention of the parties, actual or presumed, but on more general considerations.[4]
- In such relationships the problem is not to be solved by asking what the parties intended or would they have had unhesitatingly agreed to it, but instead, asking if the law has already defined the obligation or the extent of it. "If so, let it be followed. If not, look to see what would be reasonable in the general run of such cases."[5]

(B) The second category- 'uncommon relationships'

- The second category comprehends those cases which are not within the first category. These are cases 'not of common occurrence', in which from the particular circumstances a term is to be implied.

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[1] Young & Marten Ltd. v. McManus Childs Ltd. [1969] 1 A.C. 454, 465.
[2] *Supra* note vii.
[3] Shell UK Ltd. v. Lostock Garages Ltd, [1976] 1 WLR 1187.
[4] Luxor (Eastbourne) Ltd. v Cooper [1941] A.C. 108, 137.
[5] *Supra* note vii.

- In these cases the implication is based on an intention imputed to the parties from their actual circumstances.[1] Such an imputation is only to be made when it is necessary to imply a term to give efficacy to the contract and make it a workable agreement in such manner as the parties would clearly have done if they had applied their mind to the contingency which arose. These are the "officious bystander" types of cases.[2] In such cases a term is not to be implied on the ground that it would be reasonable: but only when it is necessary and can be formulated with a sufficient degree of precision. [3]

2.3.3.3 It was further observed that in cases which do not follow in either of the categories, there can be no implied term.[4]

2.3.3.4 The next development was in *Investors Compensation Scheme Ltd. v West Bromwich Building Society*[5] **('ICS Ltd. Judgment')** where Lord Hoffmann, in his majority opinion, prefaced his explanation of reasons with some general remarks.

2.3.3.5 It was held that the 'interpretation' is the meaning that the contract conveys to a person having all the background knowledge, which further includes anything which affects the way in which the language of the document is understood by a reasonable man. The background may not merely enable the reasonable man to choose between the possible meanings of words which are ambiguous but even (as occasionally happens in ordinary life) to conclude that the parties must, for whatever reason, have used the wrong words or syntax.[6]

2.3.3.6 Lord Hoffmann, then on the Privy Council,[7] dealt with the implied terms of the contract in the context of the Articles of Association of a company. It was held that the Court does not have the power to add new terms and widen the scope of the terms in order to improve the contract, but only to ascertain the true meaning of the instrument. It was further observed that the meaning does not necessarily envelope the actual intention of the parties but is the meaning which the instrument would convey to a reasonable person having all the background knowledge which would reasonably be available to the audience to whom the instrument is addressed.[8]

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[1] *Supra* note xi.
[2] Lister v. Romford Ice and Cold Storage Co. Ltd. [1957] A.C. 555, 594.
[3] Supra note vii.
[4] Esso case, [1966] 2 Q.B. 514, 536-541.
[5] Compensation Scheme Ltd. v. West Bromwich Building Society MANU/UKHL/0054/1997 : (1998) 1 All ER 98.
[6] Mannai Investments Co. Ltd. v. Eagle Star Life Assurance Co. Ltd. MANU/UKHL/0004/1997 : [1997] A.C. 749.
[7] Attorney General of Belize and Ors. v. Belize Telecom Ltd. and Anr. MANU/UKPC/0001/2009 : (2009) 1 WLR 1988.
[8] Investors Compensation Scheme Ltd. v. West Bromwich Building Society MANU/UKHL/0054/1997 : [1998] 1 WLR 896, 912-913.

2.3.3.7 The abovementioned judgment highlighted that the question of implication arises when the instrument does not expressly provide for what is to happen when some event occurs, and the most usual inference in such a case is that nothing is to happen. *"If the parties had intended something to happen, the instrument would have said so. Otherwise, the express provisions of the instrument are to continue to operate undisturbed. If the event has caused loss to one or other of the parties, the loss lies where it falls."*

2.4 Australia

2.4.1 The development of the trend with respect to the interpretation of contracts in Australia was analogous to the development in England through the judgment in *B.P. Refinery (Westernport) Proprietary Limited v. The President Councillors and Ratepayers of the Shire of Hastings*[1] **('B.P. Refinery Judgment').** On the implication of the terms of contraction five conditions were laid down and a reference was made to the Moorcock Judgment, the Reigate Judgment and the Shirlaw Judgment. For a term to be implied, the following conditions (which may overlap) must be satisfied:

"(1) it must be reasonable and equitable;
(2) it must be necessary to give business efficacy to the contract, so that no term will be implied if the contract is effective without it;
(3) it must be so obvious that "it goes without saying";
(4) it must be capable of clear expression; and
(5) it must not contradict any express term of the contract."

2.4.2 In *Con-Stan Industries of Australia Pty Ltd v Norwich Winterthur (Australia) Ltd*.[2] **('Con-Stan Industries Judgment')** the Court, in a joint judgment, set out the criteria for implying terms by custom derived from earlier authorities. The criteria included the existence of a custom or usage, evidence that the custom relied on is so well known and acquiesced in that everyone making a contract in that situation can reasonably be presumed to have imported that term into the contract, elimination from inclusion of a term which is contrary to the express terms of the agreement and being bound by a custom even without any knowledge of it.

2.4.3 Further, the Australian Court in the case of *Codelfa Construction Pty Ltd v. State Rail Authority of NSW,*[3] **('Codelfa Construction Judgment")** while upholding the English Law precedents emphasized that it is not enough for it to be reasonable to imply a term; it must be necessary to do so to give business efficacy to the contract.

2.5 India

[1] B.P. Refinery (Westernport) Proprietary Limited v. The President Councillors and Ratepayers of the Shire of Hastings [1977] UKPC 13.
[2] Con-Stan Industries of Australia Pty Ltd v. Norwich Winterthur (Australia) Ltd., (1986) 160 CLR 226.
[3] Codelfa Construction Pty Ltd v. State Rail Authority of NSW, (1982) 149 CLR 337(AustLII).

2.5.1 The parallel development in India is succinctly captured by the Supreme Court in *Dhanrajamal Gobindram v Shamji Kalidas and Co.*[1] **('Dhanrajamal Gobindram Judgment')**. It was held that:

> *"19. ...Commercial documents are sometimes expressed in language which does not, on its face, bear a clear meaning. The effort of Courts is to give a meaning, if possible...Viscount Simonds summarised at p. 158 all the Rules applicable to construction of commercial documents, and laid down that effort should always be made to construe commercial agreements broadly and one must not be astute to find defects in them, or reject them as meaningless."*

2.5.2 In *Union of India v D.N. Revri & Co. and Ors.*[2] **('D.N. Revri Judgment')**, the Supreme Court while principally following the *Moorcock test* emphasized on interpreting commercial contracts in such a manner as to give efficacy to the contract rather than to invalidate it. It dissuaded courts from applying strict rules of construction and promoted the adoption of a common sense approach not thwarted by a narrow, pedantic and legalistic interpretation.

2.5.3 Following a similar approach, in *Satya Jain (Dead) Through L.Rs. and Ors. v. Anis Ahmed Rushdie (Dead) through L.Rs. and Ors.*[3] **('Satya Jain Judgment')**, the Supreme Court reiterated the well-established principle of the test of 'business efficacy' to achieve the result of the consequences intended by the parties acting as prudent businessmen. While doing so, the Supreme Court again placed reliance on the *Moorcock Test*.

2.5.4 More recently, in 2017, in *Nabha Power Ltd. (NPL) v. Punjab State Power Corporation Ltd. (PSPCL) and Ors.*[4] ***('Nabha Power Judgment')***, after

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[1] Dhanrajamal Gobindram v Shamji Kalidas and Co. MANU/SC/0362/1961 : (1961) 3 SCR 1020.

[2] Union of India v. D.N. Revri & Co. and Ors. MANU/SC/0003/1976 : (1976) 4 SCC 147.

[3] Satya Jain (Dead) Through L.Rs. and Ors. v. Anis Ahmed Rushdie (Dead) through L.Rs. and Ors. MANU/SC/1063/2012 : (2013) 8 SCC 131.

[4] Nabha Power Ltd. (NPL) v. Punjab State Power Corporation Ltd. (PSPCL) and Ors. (05.10.2017- SC): MANU/SC/1291/2017.

comparing the views of all the three jurisdictions and relying on the *Moorcock test* and *"The Officious Bystander Test",* the Court held that:

a) A contract should be read according to its express bare provisions;
b) The concept of implied terms must be introduced only when there is a strict necessity for it;
c) Commercial courts ought to be mindful of the ever changing technical expertise of legal drafting and must not aim to imply terms into a contract unnecessarily.

3. Conclusion

3.1 In India, the recent judgments on the interpretation of contractual terms essentially seem to highlight the requirement of focusing only on the bare language of the provisions, paving way for simple and evident interpretations. This recognition is without any doubt a step forward in the contemporary era where the profoundly technical drafting methods escalate the possibility of unwarranted confusion while interpreting contracts. The Courts have cautioned commercial courts against unnecessary indulgence in implying terms into a contract and upsetting the balance which the drafters may have intended. The Courts have successfully established a progressive trend by emphasizing on liberal construction and highlighting that the scope of implying terms into a contract is only introduced when it is strictly necessary, thus favouring a potential decline in the disputes originating from varying interpretations of an express contractual term.

The Substantive and Formal Validity of Contracts – Simplifying the Identity Crisis

1. Introduction

1.1 Though formal and substantive validity, as modern day concepts, majorly find their application in arbitration agreements, they are no strangers to the realm of contract law. This does not come as a surprise considering that arbitration agreements are merely agreements between parties that are enforceable under the applicable law.[1] The 'validity' of contracts is often a matter of dispute between litigating parties, and is mostly used as a point of defence to bolster a claim for damages/breach of contract. This note is an attempt to distinguish between the concepts of substantive validity and formal validity of a contract by examining transnationally accepted 'Conflict of Laws' principles.

2. Formal Validity

2.1 A contract is formally valid if it satisfies the formal requirements of either the *lex loci contractus* (law of place where the contract is entered into) or the *proper law* of the contract.[2] Proper Law is the law which the parties have agreed upon,

[1] Section 2(h) and Section 28 of the Indian Contract Act, 1872.
[2] Van Grutten v. Digby, (1862) 54 ER 1256, 1259.

and governs, besides the formal validity of the contract, its essential validity, its interpretation, effect, and the rights and obligations of the parties.[1]

2.2 The concept of formal validity has established firm ground in various international conventions and treaties. The abovementioned criterion for formal validity was adopted in the 1980 Rome Convention on the Law Applicable to Contractual Obligations (**"the 1980 Convention"**). Article 9(1) of which states that a contract concluded between parties of the same country, will be formally valid if it satisfies the formal requirements of the law which governs it under the applicable law or the *lex loci contractus*, i.e. the law of the country where it is concluded.

2.3 Though the definition of formal requirements does not find a mention in the 1980 Convention, the *Giuliano-Lagarde Report* offers guidance on what formal validity encompasses,[2] that is to say, "*every external manifestation required on the part of a person expressing the will to be legally bound, and in the absence of which such expression of will would not be regarded as fully effective*".[3]

2.4 It would include requirements such as the requirement of having two signatories to a contract, the contract to be made in duplicate or the contract to be in writing.[4] It would also include matters such as the method of execution of a document, affixing of a seal, presence of a witness or certification by a notary.[5] However, it would not include special requirements that have to be fulfilled, which may be regarding where an act is to be valid against third parties or where there are persons under a disability to be protected.

2.5 Article 9(2) of the 1980 Convention provides that when the parties are in different countries, the contract will be considered formally valid if satisfies the formal requirements of the applicable law or the law of either of those countries. Thus, the 1980 Convention favors upholding the formal validity of the contract, if it satisfies the formal requirements of the proper law or the *lex loci contractus* or the law of the country where the persons were present at the time of the conclusion of the contract.

2.6 Article 11 of the Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June, 2008 on the law applicable to contractual obligations (2008) Regulations ("**2008 Regulations**") is by and large the same in substance as Article 9 of the 1980 Convention,[6] except the addition of a third alternative connecting factor of the law of the country, which is, where either of the parties had his habitual residence at the time of the conclusion of the

[1] Halsbury's Laws of England (3rd Edn., Vol. 7), paragraph 137, page 72.
[2] C. Otero García-Castrillón, P. Torremans, U. Grušić, C. Heinze, L. Merrett, A. Mills, …L. Walker (Eds.), (2017). Cheshire, North & Fawcett: Private International Law ("Cheshire").
[3] Report on the Convention on the law applicable to contractual obligations by Mario Giuliano, Professor, University of Milan, and Paul Lagarde, Professor, University of Paris I.
[4] *Ibid.*
[5] McEleavy, P., Collins of Mapesbury, L. (Ed.), & Harris, J. (Ed.) (2015). *Dicey, Morris & Collins on the Conflict of Laws* (15th ed.) Sweet & Maxwell.
[6] Cheshire.

contract. The same was added as the rules governing formal validity under the 1980 Convention were regarded as being too restrictive in light of the significant escalation in the number of cross-border contracts.[1]

2.7 Another important provision to be discussed while discussing the concept of formal validity is Article 11 of the United Nations 1980 Convention on Contracts for the International Sale of Goods, 1980 (**"1980 Convention"**). Article 11 sets out the principle of freedom from 'form' requirements and provides that a contract for the international sale of goods does not need to be concluded in writing and does not need to be in compliance with any other requirements of form.[2]

2.8 Both, the 1980 Convention and the 2008 Regulations adopt a policy of avoiding the invalidation of contracts on the basis of formal defects by a validation rule of alternate reference.[3] However, a contract that fails to fulfill the formal requirements of the various alternative laws, would be invalid.

2.9 On the other hand, Article 11 of the 1980 Convention establishes the theory of *consensualism*[4], purporting that a contract is not subject to any specific formal requirements. Thus, an international contract of sale of goods governed by the 1980 Convention is not subject to any formal requirements, including those forming part of the domestic laws of the contracting states.

2.10 In the Indian context, examples of formal validity of a contract would include the requirement of an arbitration agreement to be in writing,[5] for an agreement made without consideration to be in writing[6] or for an actionable claim to only be transferred by an agreement in writing. [7]

3. Substantive or Material Validity

3.1 The 1980 Convention precedents emphasize on the rule that the legality of a contract depends largely upon the law of the place of intended performance, but that the legality of the making of the agreement, i.e., giving a particular consideration for a particular promise, is controlled by the *lex loci actus*.[8] The former aspect is where the concept of material validity comes in.

3.2 The term 'material validity' covers situations where something in the nature of the contract makes it wholly or partially invalid[9] and would include matters such as formation, absence of consideration, fraud, duress, mistake and

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[1] *Ibid.*

[2] Article 11: A contract of sale need not be concluded in or evidenced by writing and is not subject to any other requirements as to form. It may be proved by any means, including witnesses.

[3] *Ibid*.

[4] Existing or made by mutual consent without an act of writing a consensual contract.

[5] Section 7, The Arbitration and Conciliation Act, 1996.

[6] Section 25 Indian Contract Act, 1872.

[7] Section 130(1), Transfer of Property Act, 1882.

[8] Foote, Private International Jurisprudence. (4th ed., 1914.), 359-363.

[9] McEleavy, P., Collins of Mapesbury, L. (Ed.), & Harris, J. (Ed.) (2015). *Dicey, Morris & Collins on the Conflict of Laws 32-107* (15th ed.) Sweet & Maxwell.

legality of a contract. Prior to the incorporation of the 1980 Convention, in the English Courts, the validity of a contract (or a term) depended on the governing law of the contract, and a contract which was void under its governing law was void, even if it was valid under the *lex loci contractus*. Conversely, if it were valid under its governing law, it would be regarded as valid even if it were invalid under the *lex loci contractus*.

3.3 The principle that the legality of a contract was determined by its governing law was criticised on the ground that it gave parties the power to implicate validity to an agreement by choosing the governing law as per their convenience, which, save for such choice, would be illegal and void.[1]

3.4 However, pursuant to the incorporation of the 1980 Convention, under Article 8(1), material validity and the existence and validity of a contract, or a term thereof, is governed by the putative applicable law. The Guiliano and Lagarde Report explains that the putative applicable law is applied "*to avoid the circular argument that where there is a choice of the applicable law no law can be said to be applicable until the contract is found to be valid*."[2]

3.5 Article 8(2) serves as a safeguard and allows a party to rely on the law of the country in which it has habitual residence to establish that it did not consent; however, Article 8(2) is restricted only to contest the existence and not the validity of consent.[3] Article 10 of the 2008 Regulations is virtually identical to Article 8 of the 1980 Convention. [4]

3.6 Additionally, Article 4 of the 1980 Convention governs only the formation of the contract of sale and except as otherwise provided, does not concern itself with the validity of the contract or any of its provisions, which is determined by the applicable law[5].

3.7 As established hereinabove, substantive validity of a contract would include the formation of a contract such as offer, acceptance and consideration,[6] the validity of consent to the contract[7] and the issue of illegality to be decided in accordance with the applicable law. A contract or any term thereof, lacking material or substantive validity may be wholly or partially invalid.

3.8 In the Indian context, a contract would be considered to be substantially or materially invalid if it does not fulfill the conditions laid down under Section 10 of the Indian Contract Act, 1872 (**"1872 Act"**) and/or is in restraint of trade, is opposed to public policy or in restraint of legal proceedings[8].

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[1] McEleavy, P., Collins of Mapesbury, L. (Ed.), & Harris, J. (Ed.) (2015). *Dicey, Morris & Collins on the Conflict of Laws 32-124* (15th ed.) Sweet & Maxwell.

[2] Cheshire.

[3] Carolina Saf, *A Study on the Interplay between the Conventions Governing International Contracts of Sale*, Queen Mary and Westfield College, September 1999

[4] Cheshire.

[5] Ulrich Drobnig, *The American Journal of Comparitive Law,* Vol 40. No. 3 (Summer, 1992), pp. 635-644.

[6] Cheshire.

[7] *Ibid.*

[8] Section 27 of Indian contract Act, 1972.

4. Conclusion

4.1 The formation and validity of contracts are of vital importance to their execution. Issues revolving around these aspects arise in many contractual disputes and can have a decisive impact on the course of resolution of claims for breach or damages. As highlighted in the preceding paragraphs, formal validity concerns itself with the 'form' of the contract and substantive validity with the substance, i.e., the 'essential' validity of its provisions. With different laws governing the determination of validity and different outcomes of invalidity, it becomes imperative for a draftsman to ensure that the contract upholds the test of both, form and substance.

Dissecting the difference between Void, Voidable and Unlawful Contracts

1. Introduction

1.1 The law relating to formation of contracts in India is governed by the Indian Contract Act, 1872 (**'1872 Act'**). As per Section 2(h) of the 1872 Act, an agreement which is enforceable by law is a contract. Typically, contracts are:

a) Valid, wherein an agreement is made with free consent between competent parties for a lawful consideration and a lawful object; or

b) Void, wherein the agreement is not enforceable by law; or

c) Voidable, wherein the agreement is enforceable by law at the option of one or more of the parties but not at the option of the other; and

d) Illegal, wherein the agreement is forbidden under the law. It is a general principle that all illegal agreements are void but not all void agreements are illegal.

1.2 An agreement is only binding amongst the parties if it is enforceable, which can only be possible after the agreement meets all the necessary conditions as prescribed under the 1872 Act. These conditions, also specifies the grounds under which a certain type of agreement may not be enforceable or

valid, either absolutely or under the discretion of one of the parties. In situations, when it's absolutely invalid, then the contract is said to be void, and when one of the parties to a contract has the option to leave the contract, then it is said to be voidable in nature. This article aims to discuss the difference between such void and voidable contracts and the repercussions thereof.

2. When would a contract be considered Void?

2.1 Void Agreements are those agreements which are unenforceable in the eyes of law. It is not necessary that void agreements are unenforceable from the very beginning, a contract may cease to be enforceable by law even at a later stage. 'Void' means that the agreement does not have any legal force or effect, the validity of which may be ascertained by any person whose rights are affected at any time or at any place directly or indirectly.[1] The Hon'ble Supreme Court of India in the case of Kalawati v. Bisheshwar[2] ('**Kalawati Judgement**') defined the term void as:

> *"void that is, non-existent from its very inception and a ban against its recognition. Indeed when it is said that such a transaction is not to be recognised for any purpose whatsoever it postulates that the transaction does exist and is valid but is not to be recognised…"*

2.2 Void-ab-initio

2.2.1 A contract is considered to be void ab initio when the same is unenforceable from the time it has been entered between the parties. In the case of Mohiri Bibi v. Dharmodas Ghose[3] ('**Mohiri Bibi Judgement**')_the High Court of Calcutta went ahead and said that any contract with minor is void ab initio since the minor is not competent to contract.

2.2.2 The words not enforceable by law do not refer towards the disability of any party to sue arising under any procedural laws, like law of limitation or civil procedure. The unenforceability contemplated, is one arising under the provisions of a substantive law. It may be declared void by this 1872 Act, or by any other law.

2.3 Void due to impossibility of performance

2.3.1 A contract becomes void when after the making of the contract, the obligations enumerated under the contract becomes impossible to perform for reasons which are beyond the control of the parties.[4] The Hon'ble Supreme Court in the case of Sushila Devi and Ors. v. Hari Singh and Ors.[5] ('**Sushila Devi Judgement**') while discussing the term 'impossibility' held that:

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[1]Purna Chandra Behera vs. Dibakar Behera and Ors.
[2] Kalawati v. Bisheshwar, 1968 SCR (1) 223.
[3]Mohori Bibi v. Dharmodas Ghose (1903) 30 Cal 539.
[4]Satyabrata Ghose vs. MugneeramBangur and Company and Ors. (16.11.1953 – SC)
[5]Sushila Devi and Ors. vs. Hari Singh and Ors. *(AIR 1954 SC 44)*

"The impossibility contemplated by Section 56 of the Contract Act is not confined to something which is not humanly possible. If the performance of a contract becomes impracticable or useless having regard to the object and purpose the parties had in view then it must be held that the performance of the contract has become impossible. But the supervening events should take away the basis of the contract and it should be of such a character that it strikes at the root of the contract."

2.4 Void due to the provisions of the 1872 Act

2.4.1 Bilateral mistake of fact

2.4.1.1 Section 20 of the 1872 Act, contemplates a situation where there is a mistake with regard to the facts by both the parties. In such a situation the agreement is considered to be void. However, in order for an agreement to fall this provision, the following pre-requisites are essential:

a) The mistake must be committed by both the parties i.e. must be mutual; and

b) The mistake must be regarding some fact; and

c) The mistake must relate to a fact which is essential to the contract.

2.4.1.2 However, Section 22 of the 1872 Act clearly stipulates that a contract is not voidable merely because it was caused by one of the parties to it being under a mistake as to a matter of fact. In ***Tapline v. Jaine*** (**'Tapline Judgement'**)**,** wherein the buyer had brought a property in an auction with reference to a plan. The buyer howvever did not refer to the plan. Later the buyer discovered that a garden plot which he thought was a part of the property, in fact not included in the plan. It was held in this case that the buyer cannot revoke the contract on the grounds of the unilateral mistake made by him and was bound by the contract.

2.4.1.3 Various other examples of mistake as interpreted by the courts which have rendered the agreement to be void includes examples of a mistake as to the area of the land agreed to be sold[1], or a transfer of the rights of a mortgagee in the erroneous belief that there was a mortgage[2], or a transaction in the property in ignorance of an existing statutory notice to its effect[3], or a mining lease granted in the erroneous belief that the lessor was entitled to its sub-soil rights[4], or a sale of precious stone in the erroneous belief that they were emeralds when in reality they were pieces of glass[5], or a sale of goods stolen from the seller before the sale although neither side was aware of the theft[6], or a mutual mistake as to the number of cartons in which a consignment was

[1] Tarsem Singh v. Sukhminder Singh, (1998) 3 SCC 471.
[2] Ismail Allarakhia v. Dattatraya R Gandhi AIR 1916 Bom 209.
[3] Nursing Dass Kothari v. Chuttoo Lall Misser AIR 1923 Cal 641; Hemumal Harpalmal v. Committee of Management, Hyderabad AIR 1920 Sind 59.
[4] Ram Chandra Misra v. Ganesh Chandra Gangopadhya AIR 1917 Cal 786.
[5] Fateh Chand v. Lachhmi Narain AIR 1920 Oudh 31, 57 IC 481.
[6] Governor-General-in-Council v. Kabir Ram, AIR 1948 Pat 345.

packed as the liability was limited to a certain amount per carton[1], or sale of leased land where both parties wrongly believed seller had authority to sell.

2.4.2 Due to object or consideration being unlawful

2.4.2.1 Section 23 of the 1872 Act prescribes that an agreement shall be void for unlawfulness if it's object or consideration is unlawful at the time it is made, and hence, it does not become enforceable if the legal provision that makes it unlawful ceases to be effective.

2.4.2.2 However, the phrase 'forbidden by law' is not synonymous with the word 'void' and hence it is not necessary that whatever is void is also forbidden by law. The said principle was approved by the Hon'ble Supreme Court in Gherulal Parakh v. Mahadeodas[2] ('**Gherulal Judgement**') where the court held that:

> *" ....The provisions of Section 23 of the Contract Act indicate the legislative intention to give it a restricted meaning. Its juxtaposition with an equally illusive concept, public policy, indicates that it is used in a restricted sense; otherwise there would be overlapping of the two concepts. In its wide sense what is immoral may be against public policy covers political, social and economic ground of objection. Decided cases and authoritative text-books writers, therefore, confined it, with every justification, only to sexual immorality....."*

2.4.2.3 At this point, it is pertinent to understand how the judges have interpreted the aspect of unlawful object. Examples may include cases where an employee started a business in the name of another with the object of circumventing non-statutory service rules, and did not disclose his income from that business to the income tax authorities[3], or where the agreement was not unlawful because evasion of tax was not the object of the transaction[4], another case where the withdrawal of prosecution as a part of a comprehensive settlement in the Bhopal gas tragedy was not the object of the settlement but only a motive, and hence the settlement was not of unlawful nature[5], or cases where shares in a company were subscribed on the basis of certain assurances by the management to give contracts that were unlawful, but the purchase of shares was not unlawful as the collateral promise to award contracts was only a motive or expectation[6].

2.4.2.4 Hence, it is the inherent object of the agreement that must be seen, and not only the object of one or the other parties to it.

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[1] Bharat Electronics Ltd, Bangalore v. American Export Isbrandsen Lines Inc by their agents J M Baxi & Co, Madras AIR 1979 Mad 267.

[2] GherulalParakh v. Mahadeodas (AIR 1959 SC 781)

[3] Surasaibalini Debi v. Phanindra Mohan Majumdar AIR 1965 SC 1364.

[4] Surasaibalini Debi v. Phanindra Mohan Majumdar AIR 1965 SC 1364.

[5] Union Carbide Corpn v. Union of India, (1981) 4 SCC 584.

[6] Gurumukh Singh v. Amar Singh (1991) 3 SCC 79.

2.4.3 Due to being without consideration

2.4.3.1 Section 25 of the 1872 Act lays down that an agreement without consideration from the other party is void. Such consideration may be in kind or in cash. However, there are exceptions to this rule as well that:

a) an agreement in writing and registered under the law for the time being in force for the registration of documents, and is made on account of natural love and affection between parties standing in a near relation to each other; or

b) a promise to compensate, wholly or in part, a person who has already voluntarily done something for the promisor, or something which the promisor was legally compellable to do; or

c) a written agreement to pay wholly or in part a debt barred by limitation.

2.4.3.2 This clearly means, this rule applies only to agreements, but not to gifts[1], or documents like a deed of advancement[2], or a receipt that merely evidences payment[3]. Agreements those are considered valid without consideration are those of agency[4] and agreements recognised by custom, such as ante-adoption contracts[5].

2.4.4 Due to it being uncertain

2.4.4.1 Section 29 of the 1872 Act lays down that if the essence of the contract is uncertain, and in future as well it is not competent of being made certain, then such a contract is void. Mere uncertainty or ambiguity which can be effortlessly removed by proper interpretation does not make a contract unenforceable.

2.4.4.2 Hence, agreements whose meaning is not certain, for example, as decided by the courts, may include agreements where the extension of the time of a delivery is postponed until a certain state of affairs recurs[6], or agreement where either one party or a third party was to determine the share of the other[7], or where the agreement provides for the payment of rent without specifying the amount[8], or where the agreement provides for a sale at a concession rate without defining the term[9], or where the agreement stipulates that an unborn daughter is to be given away according to the

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[1] Gopal Saran Narain Singh v. Sita Devi AIR 1932 PC 34; Bai Hiradevi v. Official Assignee of Bombay AIR 1955 Bom 122.

[2] Ibrahim Bhura Jamnu v. Isa Rasul Jamnu AIR 1916 Bom 159.

[3] Saleh Muhammad v. Ramrattan Tiwari AIR 1924 Nag 156.

[4] Section 185 of the Indian Contract Act 1872.

[5] Jupudi Venkata Vijaya Bhaskar v. Jupudi Kesava Rao (decd) AIR 1994 AP 134.

[6] Keshavlal Lallubhai Patel v. Lalbhai Trikumlal Mills Ltd AIR 1958 SC 512.

[7] Uttam Singh Dugal & Co (Pvt) Ltd, New Delhi v. Hindustan Steel Ltd, Bhilai Steel Project, Bhilai AIR 1982 MP 206.

[8] Muthiah Chettiar v. Periyan Kone AIR 1920 Mad 115.

[9] Tirumala Chetty Rangayya Chetty v. Kandalla Srinivasa Raghavacharlu AIR 1929 Mad 243.

wishes of any another party[1], or where the agreement is an award directing payment after making deductions which are yet to be finalised[2], or where the agreement does not indicate clearly the identity of the an arbitrator[3], or the agreement which allows a company to pay when it is in a position to do so[4].

2.4.5 Wagering contract

2.4.5.1 Wagering agreements have not been defined under the 1872 Act. A wager is an agreement to give money or it's equivalent worth upon the occurrence of an uncertain event.[5]. Hence, the parties to the contract must have the common intention to gamble.[6]

2.4.5.2 A wagering agreement is one by which parties mutually agree that, depending on the occurrence of an uncertain event in the future, one may and the other may lose, however, both parties cannot either win or lose under the contract.[7] If one of the parties is able to control the occurrence of the future event, then it is not a wager. In the case of *Carlill v. Carbolic smoke Ball Co*.[8] ('**Carbolic Judgement**'), it was held that:

> *"It is essential to a wagering contract that each party may under it either win or fail, whether he will win or fail remaining dependent on the issue of the event and therefore being unknown till that issue is known. If either of the parties wins but cannot lose, it is not a wagering contract."*

2.5 Restraining contract

2.5.1 Section 27 of 1872 Act ensures that any agreement which is made to restrain any person from carrying out a lawful profession, trade or business of any kind is to that extent void. Hence, a promise to not to compete in a locality in return of an amount is unenforceable[9]. A situation where the agreement between parties where the one would sell specified goods for 14 days in the month, and the other for 16 days in a month is also in partial restraint of trade.[10]

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[1] Atma Ram v. Banku Mal AIR 1930 Lah 561.
[2] Kovuru Kalappa Devara v. Kumar Krishna Mitter AIR 1945 Mad 10.
[3] ITC Classic Finance Ltd v. Grapco Mining & Co Ltd AIR 1997 Cal 397; Teamco (Pvt) Ltd v. T M S Mani AIR 1967 Cal 168; Delhi and Finance Housing and Construction Ltd v. Brij Mohan Shah AIR 1956 Punj 205; Luxmi Chand Baijnath v. Kishanlal Sohonlal AIR 1955 Cal 588 ; Ganpatrai Gupta v. Moody Bros Ltd (1950) 85 Cal LJ 136.
[4] Puspabala Ray v. Life Insurance Corpn of India AIR 1978 Cal 221.
[5] Gherulal Parakh v Mahadeodas Maiya AIR 1959 SC 781.
[6] Ibid.
[7] Boppana Venkataratnam v. Kamalakara Hanumantha Rao AIR 1935 Mad 135; E Sassoon v. Tokersey Jadhawjee (1904) ILR 28 Bom 616.
[8] Q.B.256(Court of Appeal) 1893.
[9] G Hurry Krishna Pillai v. M Authilachmy AmmalAIR 1916 LB 51 (FB); Parasullah v. Chandra Kant AIR 1918 Cal 546.
[10] Mohamed v. Ona Mahomed Ebrahim AIR 1922 LB 9.

2.5.2 Furthermore, Section 26 of 1872 Act provides any kind of absolute or partial[1] restrain in the marriage of any person other than a minor are void[2].

2.5.3 As well as, according to the Section 28 of the 1872 Act, any kind of bar peruse the legal proceedings is a type of void contract. The examples of such types pf contracts as adjudicated by the courts may include an agreement that the client cannot sue his barrister advocate for fees[3], or a clause in a deed which created a right of maintenance that no suit for the recovery of arrears of maintenance of more than one month could be filed[4], or a clause that no award made between the parties would be challenged[5], or an agreement that the liquidated damages quantified shall not be challenged[6], or a rule of a club restricting members from challenging the election process[7].

3. When would a contract be considered Voidable?

3.1 Voidable contracts are those agreement which is enforceable by law at the option of one or more of the parties thereto, but not at the option of the other.[8] An agreement becomes voidable when it is without free consent, in simple terms, means giving consent to a person for the performance of an act at one's own will. When one party rescinds a contract voidable at his option, the other party need not perform any promise contemplated in the contract, and the party rescinding the contract must restore as far as may be to the other party any benefit he may have received under it. A contract is said to have been entered without free consent under the following circumstances:

3.2 Coercion

3.2.1 Section 15 of the 1872 Act, defines coercion as any act which includes threat, unlawful detention or causing a threat of detaining property of the other party with the view of obtaining his consent and the act which is prohibited by Indian Penal Code, 1860 ('**1860 Code**'). The Hon'ble Delhi High Court in the case of Kishan Lal Kalra vs. N.D.M.C.[9] ('**Kishan Kalra Judgement**') held that:

> *"10. A person is not bound by any act done by him under duress or coercion. The threat of detaining under MISA was clearly an act of coercion which would fall within the mischief of Section 15 of the Indian Contract Act...."*

3.2.2 Other examples of coercion as expressed by the courts through various judgements include where a person was arrested in an execution by the order

[1] U Ga Zan v. Hari Pru AIR 1914 MB 156.
[2] Shahzada v. Mahomed Rasul AIR 1934 Pesh 22.
[3] Nihal Chand Shastri v. Dilawar Khan AIR 1933 All 417.
[4] Saroj Bandhu Bhaduri v. Jnanada Sundari Debya AIR 1932 Cal 720.
[5] Coringa Oil Co Ltd v. Koegler (1875) ILR 1 Cal 466.
[6] Bharat Sanchar Nigam Ltd v. Motorola India Pvt Ltd., (2009) 2 SCC 337.
[7] Tapash Majumder v. Pranab Dasgupta AIR 2006 Cal 55.
[8] Swiss Timing Limited vs. Organising Committee, Commonwealth Games, 2010 AIR 2014 SC 3723.
[9] Kishan Lal Kalra vs. N.D.M.C., AIR 2001 Delhi 402.

of a court which did not had jurisdiction[1], or where a person claiming a share in the property took the law into his own hands and took over the family jewellery[2], or where the account books of a person were unlawfully detained by the former agent who had been dismissed earlier[3], or where coparcenary property was attached to compel the payment of a fine due from one of the member belonging to same coparcenary[4].

3.3 Undue Influence

3.3.1 Section 15 of the 1872 Act, defines undue influence where, *first* the relations subsisting between the parties are such that one of the parties is in a position to dominate the will of the other, and *second* such position is used to obtain an unfair advantage over the other. Both the conditions must have to be established by the person seeking to avoid the said transaction.[5]

3.3.2 Undue influence means the domination of a weak mind (party) by a stronger mind to an extent which causes the behaviour of the weaker party to act as what has been suggested by the stronger party[6].

3.4 Fraud

3.4.1 Section 17 of the 1872 Act defines fraud as when a party to the contract, or with his connivance his agent, with intent to deceive the other party or his agent, or to induce him to enter into a contract, or by providing such facts and information which are not true, or made such promises without any intention of fulfilling it.

3.4.2 A mere false statement is not fraud[7] even if deliberately made. A contract is voidable at the discretion of the party on whom the fraud is played only if such statement causes the said party to consent to the contract.

3.5 Misrepresentation

3.5.1 Section 18 of the 1872 Act lays down that when a party has entered into the contract, and other party commits an act with the intent to deceive, or breaches the duty, or causes mistake without having intention of the same, then it amounts to misrepresentation.

3.5.2 The Hon'ble High Court of Punjab and Haryana in the case of Rattan Lal Ahluwalia v. Jai Janinder Parshad[8] ('**Rattan Judgement**') while laying down the distinction between fraud and misrepresentation held that:

> *"In cases of fraud and misrepresentation there is misstatement or false state-merit, of fact(s) which misleads the party on whom the same is*

[1] Banda Ali v. Banspat Singh (1882) ILR 4 All 352.
[2] Hla Maung v. Mo Toke AIR 1929 LB 38.
[3] P M Muthiah Chetti v. Muthu K R A R Karuppan Chettiar AIR 1927 Mad 852.
[4] Bansraj Das v. Secretary of State AIR 1939 All 373.
[5] Ladli Parshad Jaiswal v. Kamal Distillery Co Ltd AIR 1963 SC 1279.
[6] Rambali Prasad Singh v. Kishori Kuer AIR 1937 Pat 362.
[7] Kamal Kant Paliwal v. Prakash Devi Paliwal AIR 1976 Raj 79.
[8] Ahluwalia v. Jai Janinder Parshad, AIR 1976 P H 200.

perpetrated. The principal difference between fraud and misrepresentation is that in the case of fraud the person making the suggestion, does not believe it to be true, while in the case of misrepresentation he believes to be true"

3.6 Hence, it can be said that misrepresentation differs from fraud, although in both the cases it is a misstatement of fact which misleads the promisee, while in the former the person making the statement believes it to be true, in the latter he does not[1].

4. Rights conferred by a Void contract versus rights conferred by Voidable contract

4.1 Apart from the above stated difference between Void and Voidable contracts some other major differences between them are as follows:

Ground	Void Contract	Voidable Contracts
Legal right of the parties	Agreement is not enforceable	Agreement is enforceable upon the consent of the party from whom consent had earlier not been received.
Status of contract	The contract is automatically unenforceable.	The party whose consent had not been obtained has to rescinded the contract in order to make it unenforceable.
When can it be made valid	Of the agreement being such that it is forbidden under law hence those contracts cannot be made valid under any situations.	Consent of the parties can make the contract valid

5. Conclusion

5.1 When parties enter a contract with one another, they must ensure that the contract will be enforceable in the courts in future. If the terms or conditions of the agreement as agreed by the parties are such that the agreement may turns out to be void, then it brings the party to the earlier stage, as like the contract has never existed in the eyes of law. Hence, a careful perusal of each covenant in the contract is necessary, to ensure the contract will hold the waters during it's performance.

[1] Rattan Lal Ahluwalia v. Jai Janider Parshad AIR 1976 P & H 200.

5.2 Hence, a void contract, is invalid from the very start. It does not require one party to back out or challenge its validity. However, with a voidable contract, it does not become invalid until one party asserts a legal reason for cancelling or revoking the same. This means, without one party raising a legal objection that his consent was obtained through coercion, or undue influence, Fraud or misrepresentation, the contract as entered between the parties would remain valid.

Agreements in Restraint of Legal Proceedings: An Analysis

1. Introduction

1.1 The Indian Contract Act, 1872 **(the "Act")** explicitly provides for certain conditions which render an agreement void. One such provision being Section 28 of the Act, which discusses certain scenarios under which an agreement would be declared as void. These include the following kinds of agreements:

a. Which restrict absolutely any party from enforcing his rights as provided under the contract through the usual legal proceedings;

b. Which limits the time within which he may enforce any such rights;

c. Which extinguishes the rights of any party provided under the contract on expiry of specified period which will restrict any party from enforcing such rights;

d. Which discharges any party from any liability under the contract on expiry of specified period which will restrict any party from enforcing such rights.

1.2 The above instances can be divided into two broad categories, i.e. agreements by which a party is restricted absolutely from enforcing his legal rights arising under a contract by way of employing the usual legal proceedings and

agreements which limit the time within which the contractual rights may be enforced.

2. Evolution of Section 28 of the Act

2.1 Even though the scope of Section 28 has evolved over a period of time, it essentially revolves around the common law principle that an agreement purporting to oust the jurisdiction of the courts is illegal and void on grounds of public policy. In 1997, after the recommendations derived from the 97th Report of the Law Commission of India, Section 28 witnessed a complete alteration.[1]

2.2 Before the amendment, Hon'ble Supreme Court of India followed a different trend by holding valid even those contracts which incorporated such restrictive covenants. In the case of *Food Corporation of India v. New India Assurance Co. Limited*,[2] **("Food Corporation of India Judgement")** the Apex Court held with respect to a clause in an insurance policy stipulating that the insured will not have any right under the insurance policy after the expiry of six months as valid. Similarly, in the case of *Vulcan Insurance Co. v. Maharaj Singh*[3] **("Vulcan Insurance Judgement"),** the Apex Court held the impugned clause in the insurance policy which stated that the insurer would not be liable for any loss if the claim was made after the expiry of 12 months from the happening of the loss as valid.

2.3 The position was entirely reversed after the introduction of the 1997 Amendment. The amendment propounded the principle laid down in *Hyman v. Hyman*[4] **("Hyman Judgement")** where it was held that Courts will not enforce contracts which frustrate Acts of Parliament. In this case, a clause in a separation deed provided that the wife would not apply to the divorce-court for maintenance and it was held that it was void as being contrary to public policy.

2.4 However, the amendment was certainly not welcomed with fervor. It invited vehement criticism from certain sectors, especially banking and financial institutions, owing to provisions of the new amendment which restrained them from including such clauses in a bank guarantee, etc., which had the effect of extinguishing the right of any party on the expiry of a stipulated period. In view of the criticism and hardship faced by the banking and financial institutions, the Banking Laws (Amendment) Act, 2012 was promulgated which introduced Exception 3 to Section 28, relieving banks from the above mentioned restriction. The exception has been discussed in detail in the following sections of the article.

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[1] Pollock & Mulla, The Indian Contract and Specific Relief Acts, 14th Edition, Published by LexisNexis.
[2] Food Corporation of India v. New India Assurance Co. Limited, (1994) 3 SCC 324.
[3] Vulcan Insurance Co. v. Maharaj Singh, (1976) 1 SCC 943.
[4] Hyman v. Hyman, [1929] AC 601.

3. Agreement Limiting Time Period For Enforcement Of Contractual Rights

3.1 Under Section 28 of the Act, any agreement which puts forth the condition of a shorter time period as compared to the limitation provided under the guiding law for the enforcement of contractual rights is held to be void. For example, an agreement providing a shorter time period than the period of limitation prescribed by the law for filing a suit for breach of contract is void under Section 28 of the Act.

3.2 The Supreme Court in the case of *MG Brothers Lorry Services v. Prasad Textiles*[1] **("MG Brothers Judgement")** rendered an agreement void as it prescribed a lesser time period for filing a suit than what was provided under Section 10 of the Carriers Act, 1865 **(the "Carriers Act")**, defeating the provision under Section 10 of the Carriers Act as well as Section 28 of the Act. Further, the Hon'ble High Court of Delhi in the case of *National Highway Authority of India v. Mecon- Gea Energy Systems India Limited*[2] **("NHAI Judgement***")* held that a clause which limits the time period for any party to make a reference to Arbitration is void.

3.3 In *Oriental Insurance Co. Ltd. v Karur Vysya Bank Ltd.*[3] **("Oriental Insurance Judgement"),** a clause affixing a one year limitation on the introduction of a recovery suit under a policy of life insurance after the death of the assured was also held to be void.

3.4 However, in *National Insurance Co. v. Sujir Ganesh Nayak*,[4] **("National Insurance Co. Judgement")** the Court held that the curtailment of the period of limitation is not permissible in view of Section 28 but extinction of the right itself unless exercised within a specified time is permissible and can be enforced. This view followed pursuant to the decision of the Hon'ble Bombay High Court in *Hirabhai v. Manufacturers Life Insurance*,[5] **("Hirabhai Judgement")** where a clause propounding that "no suit shall be brought against the company in connection with the said later policy than one year after the time when the cause of action accrues" was held to be valid. The justification provided by the Hon'ble Court in this regard was that the effect of the agreement was not to limit the time but to provide for surrender of rights if no action was brought within that time.

3.5 It would be relevant to consider that any agreement extending the period of limitation will not be rendered void under this provision, however, it is still likely to be held void under Section 23 of the Act, as such an agreement will be in the nature of defeating the provisions of the Limitation Act, 1963[6] **("Act of 1963")**.

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[1] MG Brothers Lorry Services v. Prasad Textiles, (1983) 3 SCC 61.
[2] National Highway Authority of India v. Mecon- Gea Energy Systems India Limited, (2013) SCC OnLine Del 1273.
[3] The Oriental Insurance Company v. Karur Vysya Bank Limited Karur, AIR 2001 Mad 489.
[4] National Insurance Co. v. Sujir Ganesh Nayak, AIR 1997 SC 2049.
[5] Hirabhai v. Manufacturers Life Insurance, (1912) 14 BOMLR 741.
[6] Gobardhan v. Dau Dayal, AIR 1932 All 273.

4. Agreement providing for Jurisdiction

4.1 An agreement which prescribes jurisdiction to a court not having jurisdiction, is a void agreement. Jurisdiction cannot be decided against ordinary law. Thus, an agreement which ousts the jurisdiction of all other courts and renders the same to a court which does not have jurisdiction is a void contract.

4.2 However, this does not amount to taking away the liberty of the parties to confer jurisdiction to one court in cases where two or more courts have jurisdiction to try the case. This prescription is not in contravention to Section 28 of the Act. The prerequisites of such a clause in a contract include it being clear, unambiguous, explicit and not vague. In the case of *A.B.C. Laminart Pvt. Ltd. v. A.P. Agencies, Salem*[1] **("A.B.C Laminart Judgement")** the Hon'ble Supreme Court held as follows:

> *"When the clause is clear, unambiguous and specific accepted notions of contract would bind the parties and unless the absence of ad idem can be shown, the other Courts should avoid exercising jurisdiction. As regards construction of the ouster clause when words like 'alone', 'only ', 'exclusive' and the like have been used there may be no difficulty. Even without such words in appropriate cases the maxim 'expressio unius est exclusio alterius' - expression of one is the exclusion of another may be applied. What is an appropriate case shall depend on the facts of the case."*

4.3 While agreements which completely prohibit legal recourse are void under Section 28 of the Act, it is important to note that an agreement whereby the parties to a suit agree to bind themselves by a judgement passed by the court of first instance, cutting off the bridge to any future recourse like an appeal, is valid and binding. An important authority in this regard is *Munshi Amir Ali v. Maharani Inderjit Koer*[2] **("Munshi Amir Judgement")**. It has also been followed by the Hon'ble Allahabad High Court in *Anant Das v. Ashburner & Co*.[3] **("Anant Das Judgement")**. However, with respect to arbitration, it has been held that imposing a restriction which binds the party by an arbitral award by preventing further recourse in the form of an appeal renders the agreement void.[4]

5. Exceptions to the applicability of Section 28

5.1 The first exception provided under Section 28 grants validity to those agreements which choose arbitration as their preferred mode of dispute resolution. The second exception in the quoted section provides that an agreement will not be in contravention to Section 28 if a party agrees to refer an already existing dispute to arbitration.

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[1] A.B.C. Laminart Pvt. Ltd. v. A.P. Agencies, Salem, (1989) 2 SCC 163.
[2] Munshi Amir Ali v. Maharani Inderjit Koer, 9 B.L.R. 460.
[3] Anant Das v. Ashburner & Co., (1878) ILR 1 ALL 267.
[4] Rambilas Mehto v. Babu Durga Bijai Prasad Singh, AIR 1965 Pat 239.

5.2 The reason behind the exceptions lie in the fact that in either case, there is no compromise in the rights of any party as long as the case is decided on merits. In *Union Construction Co. Pvt. Ltd. v Chief Engineer, Eastern Command*,[1] **("Union Construction Co. Judgement")** the court held that a lawful agreement, to refer a matter to arbitration, can be made a condition precedent to going to the courts without it being in violation of Section 28.

5.3 The third exception was introduced in order to safeguard the rights of banking and financial institutions. It allowed them to add prescriptive clauses, in which the right of a party to make a claim against the other party gets extinguished after the expiry of specified period. Banks are known to use such clauses in bank guarantee agreements. However, the exception provides that the specified period should not be less than one year. The fixation of this minimum time period welcomes some questions such as the validity of bank guarantees which were made for a period of less than one year. Further, this period of one year has to be calculated from the date of occurring or non-occurring of a specified event for extinguishment or discharge of a party from liability.

5.4 In *Kerala Electrical & Allied Engineering Co. Ltd. v. Canara Bank & Others*,[2] (**"Kerala Electrical Co. Judgement**") the liability of the bank with respect to the guarantee was supposed to expire in a period of six months after the expiry of the period of duration of the guarantee. It was also stated that the plaintiff's rights under the guarantee would be forfeited by the end of those six months. It was held that since there was an extinction of the right of the plaintiff under the contract and a discharge of the defendants from liability, the time limit imposed could not be hit by Section 28 and was thus, valid.

6. Conclusion

6.1 The evolution of Section 28 of the Act has witnessed several transcendent additions right from the amendment in the year 1997 to the amendment brought about in the year 2013. While the purpose of these amendments brought in by the legislature was indeed based on providing clarity and eliminating any and all unnecessary possibilities of potential ambiguity, they have served manifold purposes by protecting every party's right to approach the Courts for grievance redressal.

6.2 The amendments have thus, passed the test of time and established a rather bold presence throughout the regime of contract enforcement. It is, however, essential to keep up with the ever changing needs of the society and while Section 28 has been successful hitherto, the possibility of future amendments to introduce more value and importance to the provision is always on the table.

[1] Union Construction Co. Pvt. Ltd. v. Chief Engineer, Eastern Command, AIR 1960 All 72.
[2] Kerala Electrical & Allied Engineering Co. Ltd. v. Canara Bank & Others, AIR 1980 Ker 151.

Determination of Contingent Contracts – Essentials & Enforcement

1. Introduction

1.1 The Indian Contract Act, 1872 ('**1872 Act**') codifies the way in which a party enters into a contract, executes a contract and implements provisions of a contract and effects of breach of a contract. The contractual capacity of the parties is restricted in certain situations, otherwise it is the prerogative of every individual to contract. Hence, the basic framework of contracting is covered under the 1872 Act.

1.2 As per the 1872 Act, once the contract formalizes, the next stage is reached, i.e. – the fulfilment of the object the parties had in mind while executing the contract. However, the performance as mostly understood, is not the only way in which a contract is discharged to fulfil the object. Sometimes, the contract may require the fulfilment of a condition precedent for the discharge of the obligations vested upon the parties under the contract. In this article, we seek to analyse the concept of absolute contracts and contingent contracts.

2. Concept: Absolute and Contingent Contracts

2.1 An absolute contract is one where a party making the promise undertakes to perform the contract in any event, without any condition. For example, to pay a sum of money on the expiry of a time or on the death of a person. These kinds of contracts are absolute contracts because these events are of a certain nature. In these circumstances, the time, or person in question will expire, and the money will become payable.

2.2 On the contrary, a contingent contract is one where the obligation to perform by the party making the promise arises only upon occurrence of specified event. It is a sort of conditional contract, where the condition is of uncertain nature. For example, a contract to pay money on the destruction of a house by fire. Since, such an event may, or may not happen. These kinds of contract contemplate a happening or non-happening of a future event.

2.3 The word contingent ordinarily means '*subject to something occurring or not occurring'*. It is imperative to say that uncertainty is the hall-mark of what is to come i.e. the future and therefore, the entire concept of a contingent contract is based on estimating the chances of an uncertainty becoming certain, then calculating the results if the event doesn't happen and lastly, measuring the potentiality to deal with its consequences.

2.4 At this point, it is imperative to analyse the kinds of agreements the courts have interpreted as contingent, to better understand the key features of such kind of contracts. Examples of contracts held to be contingent contracts are:

- Contracts of insurance[1];
- to sell shares of a bank held by the plaintiff at the agreed price within a specified time from the conversion of the bank into a financial corporation, or in default to buy them[2];
- by a mother to make up the shortfall to the younger son, if the older son did not pay an amount agreed to be paid by him[3];
- to sell property when a mortgage was redeemed[4];
- between a tenderer and his sub-contractor executed in anticipation of acceptance of tender[5];
- by a guardian to sell property subject to the court approving the transaction[6];
- made during the pendency of a suit in which the plaintiff had claimed possession, whereby it was agreed that if the plaintiff succeeded in the suit, he would accept a sum of money, instead of possession[7];
- commission payable on success of litigation[8];

[1] Chandulal Harjivandas v. CIT, AIR 1967 SC 816.
[2] Jethalal C Thakkar v. RN Kapur AIR 1956 Bom 74
[3] Comr of Wealth Tax, Mysore v. Vijayba, Dowger Maharani Saheb, Bhavnagar AIR 1979 SC 982.
[4] Ramzan v. Hussaini AIR 1990 SC 529.
[5] Uttar Pradesh Rajkiya Nirman Nigam Ltd v. Indure (Pvt) LtdAIR 1996 SC 1373.
[6] Narain Pattor v. Aukhoy Narain (1885) ILR 12 Cal 152.
[7] Ismal Mahamad v. Daudbhai Musabhai (1900) 2 Bom LR 118.
[8] N. Pedanna Ogeti Balayya v. Kota V. Srinivasayya Setti Sons, AIR 1954 SC 26.

- to sell a certain property if the seller did not repay to the purchaser the money borrowed by him[1];
- to purchase shares if the purchaser was appointed a selling agent of the products of the company[2];
- in an ante-nuptial agreement to give land to the bridegroom when the marriage took place[3];
- to sell a portion of land after it was demarcated[4];
- to sell goods as might arrive[5];
- a sale of land subject to the title of the vendor being approved by the purchaser's lawyer[6];
- a sale of goods subject to revision and confirmation by mail only in case of telegraphic error[7];
- to sell flats on the thirteenth floor provided that the requisite sanction was obtained[8];
- to sell land provided the requisite statutory sanction was obtained[9]; and
- that a seller of property will discharge the loan, redeem the mortgage and hand over title deeds redeemed to the purchaser[10].

2.5 The above agreements give an insight, that whenever the foundation of a contract is based upon the possibility of a future event, which is entirely outside of the scope and beyond control of the parties, the courts have been reluctant to enforce such contracts.

2.6 The 1872 Act has a specific chapter[11] dealing with contingent contracts consisting of Section 31 to Section 36. The Act defines a contingent contract as '*a contingent contract is a contract to do or not to do something, if some event, collateral to such contract does or does not happen.'*[12] As a matter of fact, every contingent contract is thus a contract, primarily which includes an agreement that is made with the free consent of parties competent to contract, for a lawful

[1] Asvath Narayan Astaputre v. Chimabai Gopalrao Sadekar AIR 1926 Bom 107.
[2] Re Jaunpur Sugar Factory Ltd, AIR 1925 All 658 .
[3] Ma E Tin v. Ma Byaw, AIR 1928 Rang 286 (2).
[4] Kirpal Das Jivraj Mal v. Manager, Encumbered Estates AIR 1936 Sind 26.
[5] Bisseswarlal Brijlal v. Jaidayal Udairam AIR 1949 Cal 407.
[6] Panem Venkanarayana Sastry v. Rajupalli China Yella Reddy AIR 1959 AP 256 ; Sreegopal Mullick v. Ram Churn Nasker (1884) ILR 8 Cal 856; Krishnaji Gopinath Rele v. Ramchandra Kashinath Mastakar AIR 1932 Bom 51; W P Abro v. Promotho Nath Mukerjee AIR 1914 Cal 777; Treacher & Co Ltd v. Mahomedally Adamji Peerbhoy (1911) ILR 35 Bom 110.
[7] B Shushil Chandra Das v. (Firm) Sukhamal BansidharAIR 1922 All 219.
[8] Baij Nath v. Ansal and Saigal Properties (Pvt) LtdAIR 1993 Del 285.
[9] Bishambhar Nath Agarwal v. Kishan Chand AIR 1998 All 195; Balu Baburao Zarole v. Shaikh Akbar Shaikh Bhikan AIR 2001 Bom 364; Rameshwarlal v. Dattatraya AIR 2010 MP 187.
[10] J P Builders v. A Ramadas Rao (2011) 1 SCC 429.
[11] Chapter III, Indian Contract Act, 1872.
[12] Section 31, Indian Contract Act, 1872.

consideration and with a lawful object.[1] Like any other contract, it is also a contract to do or not to do something. However, due to its contingent nature of performance it is neither absolute nor unconditional and is to be performed upon happening for any specific event[2].

3. Essentials of Contingent Contract

3.1 Upon perusal of the definition of a contingent contract as encapsulated under section 31 of the 1872 Act, the essential ingredients of contingent contract are as follows:

3.1.1 There must be a collateral valid contract to do or abstain from doing something;

The provisions provide that the contingency contemplated by the contract must be collateral to the contract. This means, the contract must have been in existence, but it's performance cannot be demanded unless the contemplated event happens or, does not happen.

3.1.2 Performance of the contract must be conditional;

Further, the condition for which the contract has been entered into must be a future event, and shall most importantly be uncertain. However, if the performance of the contract is dependent on a future event, but certain and sure to happen, then it'll not be considered as a contingent contract. It is also essential that the event on whose happening or non-happening the performance of the contract is dependent should not be a part of the consideration of the contract.

3.1.3 The event should not be at the discretion of the promisor.

Lastly, the event so considered as for contingency should not at all to be dependent on the promisor. It should be totally a futuristic and uncertain event.

4. ENFORCEMENT OF A CONTINGENT CONTRACT

4.1 Section 32 to Section 36 of the 1872 Act provides for provisions relating to the enforcement of a contingent contract and the same are as follows:

4.1.1 When Enforcement depends upon the happening of an event[3]

The provisions lay down two basic principles. First, a contract to do an act on the happening of the future uncertain event cannot be enforced, unless and until that event happens. Second, if the happening of that event has turned out to be impossible, the contract becomes void.

4.1.2 When performance depends upon the non-happening of an event[4]

In situations where the performance of the contract depends upon the non-happening of the event, it is imperative that the parties wait till the happening of that event becomes next to impossible. Hence, the time

[1] Section 10, Indian Contract Act, 1872.
[2] Commissioner of Excess Profits Tax v. Ruby General Insurance Co. Ltd. AIR 1957 SC 669.
[3] Section 32, Indian Contract Act, 1872.
[4] Section 33, Indian Contract Act, 1872.

when it can be assured, the event can no more happen, then only the performance of the contract can be demanded.

4.1.3 When performance is linked with human conduct[1]

When the event for which the parties are waiting, is linked with the future conduct of a person, then in such cases, the event shall be considered to have become impossible if the person so concerned, does something which makes the event impossible to be carried out in the specified time.

In an English case, Frost v. Night[2] ('**Frost**'), the defendant promised to marry the plaintiff on the death of her father. While the father was still alive, defendant married another woman. It was held, it has become impossible that the defendant can marry the plaintiff legally, thus, the plaintiff was entitled to sue to the defendant for damages.

4.1.4 When performance is contingent upon an event happening within the fixed time[3]

Another type of contingent contracts are those which stipulates to do or not to do anything when the uncertain event happens within a fixed time. Such a contract is void if the event does not happen and the time lapses. It is also void if before the time fixed, the happening of the event becomes impossible.

4.1.5 When the performance is contingent on an event not happening within the fixed time[4]

Contingent contracts may be enforced by law when the fixed time has expired, and such event has not happened, or before the time fixed has expired, if it becomes certain to the parties that such event will not happen.

4.1.6 When the performance is contingent upon an impossible event[5]

These provisions are self-explanatory in nature. Meaning, pursuant to the execution of contingent agreement, if the performance of the same is hindered by an impossible event, whether known or unknown to the parties, then such an agreement shall be void.

5. Conclusion

5.1 Contingent contracts have all the feathers of a contract, except the only difference, that in contingent contract enforceability depends upon a contingency which may happen or may not happen. If the contingency is not fulfilled, contingent contract becomes void. Thus, essentially every contingent contract is a contract primarily to do or not to do something. A contract is said

[1] Section 34, Indian Contract Act, 1872.
[2] Forst v. Knight, (1872) 7 Exch 111.
[3] Section 35, Indian Contract Act, 1872.
[4] *Ibid.*
[5] Section 36, Indian Contract Act, 1872.

to be contingent only when the essential elements of a contingent contract as discussed above are encapsulated therein. The entire concept of a contingent contract is based on estimating the chances of an uncertainty becoming certain, then calculating the results if the event doesn't happen and lastly measuring the potentiality to deal with its consequences.

5.2 The provisions of the 1872 Act and the jurisprudence in this aspect laid down by the various judgements of the courts helps in understanding that agreements whose foundation depend upon uncertainty cannot be enforced, unless the contingency is something which is possible. The Supreme Court of Indian in the recent judgement in NAFED v. Alimenta S.A[1] ('NAFED') has held that in cases where the contract agreement is based on contingency i.e. occurrence of some event which renders the contract void, section 32 of the 1872 Act will come into force and none of the parties will be held liable for the damages.

[1] NAFED v. Alimenta S.A, *Civil Appeal No. 667 of 2012.*

Damages for Breach of Contract in India: Legal Principles

1. Introduction

1.1 Section 37[1] of the Indian Contract Act, 1872 ('Act') provides that "*The parties to a contract must either perform, or offer to perform, their respective promises, unless such performance is dispensed with or excused under the provisions of this Act, or of any other law.*" But what happens when one party to a contract fulfils its promise and the other party fails to come through? In such a case, how is the first party to be compensated for the loss or injury suffered by it owing to the actions or inactions of the second party? How do different types of clauses in a contract affect such compensation and quantum of damages? And what are the basic principles governing the approach of Courts when it comes to

[1] **37. Obligation of parties to contracts.**—The parties to a contract must either perform, or offer to perform, their respective promises, unless such performance is dispensed with or excused under the provisions of this Act, or of any other law.
Promises bind the representatives of the promisors in case of the death of such promisors before performance, unless a contrary intention appears from the contract.

awarding such compensation? These are a few questions which this article focuses on answering.

1.2 The term "*Breach of Contract*" is not defined under the Act. However, the Black's Law Dictionary defines breach of a contract as "*Failure, without legal excuse, to perform any promise which forms the whole or part of a contract*". If a party to a contract does not fulfil its contractual promise or has given information to the other party that it will not perform its duty as stipulated in the contract or if by its action and conduct it seems to be unable to perform the contract, it is said to have breached the contract.

2. Consequences of Breach of Contract

2.1 The concept of damages under a contract dates to the very inception of contractual relationships. In the Indian law, Chapter VI i.e. Section 73 to Section 75 of the Act deal with the consequences of breach of contract. The failure to perform its obligations under the contract by a party may provoke a lawsuit, in which an aggrieved party asks a court to award financial compensation by way of damages for the loss caused by the breach. Such damages may be unliquidated (Section 73[1]) or liquidated (Section 74[2]). Unliquidated damages are awarded by the courts on an assessment of the loss or injury caused to the party suffering such breach of contract. On the other hand, in certain contracts, the parties thereto may agree in advance to the payment of a certain sum on breach of the said contract. When such stipulations are made in the contract, they are known as liquidated damages.

3. Unliquidated Damages

3.1 Section 73 of the Act, which provides for compensation in case of breach of a contract, is broadly based on the rules laid down by the English Court of Exchequer in the matter of *Hadley Vs. Baxendale*[3] wherein it was held that:

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[1] **73. Compensation for loss or damage caused by breach of contract.—**When a contract has been broken, the party who suffers by such breach is entitled to receive, from the party who has broken the contract, compensation for any loss or damage caused to him thereby, which naturally arose in the usual course of things from such breach, or which the parties knew, when they made the contract, to be likely to result from the breach of it.

Such compensation is not to be given for any remote and indirect loss or damage sustained by reason of the breach.

Compensation for failure to discharge obligation resembling those created by contract.—When an obligation resembling those created by contract has been incurred and has not been discharged, any person injured by the failure to discharge it is entitled to receive the same compensation from the party in default, as if such person had contracted to discharge it and had broken his contract.

Explanation.—In estimating the loss or damage arising from a breach of contract, the means which existed of remedying the inconvenience caused by the non-performance of the contract must be taken into account.

[2] **74. Compensation for breach of contract where penalty stipulated for.—**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 an act in which the public are interested.

[3] Hadley Vs. Baxendale reported at (1854), 9 Exch. 341, 156 E.R. 145.

> "*Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonable be considered either arising naturally i.e., according to the usual course of things from such breach of contract itself, or such as may reasonable be supposed to have been in contemplation of both parties at the time they made the contract, as the probable result of it.*"

3.2 The Court further observed that where special circumstances are communicated, a defendant will be liable for damages that may have been reasonably contemplated by the parties acquainted with such special circumstances.

4. General Damages and Special Damages

4.1 Section 73 of the Act contemplates two types of damages – (i) General; and (ii) Special Damages. General damages are those which arise naturally in the usual course of things which need not be proved by the Plaintiff. On the other hand, special damages are those which arise owing to special circumstances which the parties knew of when they made the contract. For every case of special damages, the burden of proof lies with the Plaintiff to show that such special circumstances existed and that the same were within the knowledge of the Defendant.

5. The approach of Courts

Facts: The Plaintiff, Hadley, was a miller. His mill had stopped because of a breakage of the mill's crankshaft. The Plaintiff contacted the manufacturer of the crankshaft, W. Joyce & Co. who agreed to make a new shaft from the pattern of the old one. The Plaintiff, thought his servant, engaged the Defendant, Baxendale (a common carrier), to transport the crankshaft to W. Joyce & Co. where it would be repaired and then subsequently, transport it back. The Defendant then made an error causing the crankshaft to be returned to the Plaintiff a week later than agreed. During such time, the Plaintiff's mill was out of operation. Therefore, the Plaintiff sued the Defendant and contended that the Defendant had displayed professional negligence and attempted to claim for the loss of profit resultant from the unexpected week-long closure of the mill. The Defendant per contra contended that such an action was unreasonable as he had not known that the delayed return of the crankshaft would necessitate the mill's closure and thus, that the loss of profit failed to satisfy the test of remoteness.

Issue: Whether the loss of profits resultant from the mill's closure was too remote for the Plaintiff to be able to claim?

Held: The Court found for the Defendant, viewing that a party could only successfully claim for losses stemming from breach of contract where the loss is reasonably viewed to have resulted naturally from the breach, or where the fact such losses would result from breach ought reasonably have been contemplated of by the parties when the contract was formed. Here, while the breach by Defendant was the actual cause of the lost profits of Plaintiff, it cannot be said that under ordinary circumstances such loss arises naturally from this type of breach. There is a multitude of reasons for a miller to send a crank shaft to a third party. Defendant had no way of knowing that his breach would cause a longer shutdown of the mill, resulting in lost profits. Further, the Plaintiff never communicated the special circumstances to Defendant, nor did the Defendant know of the special circumstances.

5.1 There can be no cause of action for breach of contract unless damage has actually been suffered. The onus to prove that the Plaintiff has suffered damages and the measure thereof lies on the Plaintiff. With regard to Section 73 of the Act, the Court which is seized of the case does not *simpliciter* assess the pecuniary liability which already exists. The Court first has to decide whether the Defendant is liable and if it comes to that conclusion, only then will the Court be required to assess the extent of that liability and the damages which it must award to the Plaintiff.

5.2 Damages are awarded as pecuniary compensation for the injury which a party sustains as the result of a default by the other party. The party to be entitled to compensation must have done something to his own prejudice in the performance of his part of the contract. To maintain a suit for damages for alleged breach of contract, the Plaintiff should have performed his part of the contract, put forward any accounts of the alleged loss and claim damages on that basis alone. No plaintiff can maintain an action for damages for breach of contract unless he can aver and prove that he has performed or has at all times been ready to perform his part of the contract. It is also the duty of Plaintiff in such circumstances to mitigate the damages.

5.3 Damages are awarded to a party to place it in the same position in which it would have been in the absence of injury which it complains. Therefore, damages must be commensurate with the injury sustained.[1] The two principles on which damages under Section 73 of the Act are to be awarded are well established. First, the party to the contract which has proved a breach has to be placed, as far as possible in monetary terms, in as good a situation as if the contract had been performed. However, this principle is qualified by the second principle which imposes a duty upon the plaintiff of taking all reasonable steps to mitigate the losses consequent on the breach and debars him from claiming any part of the damage which is caused due to his neglect to take such steps[2]. This second principle is embodied in the explanation appended to Section 73 of the Act.

6. Liquidated Damages

6.1 The Black's Law Dictionary defines the term "Liquidated Damages" as "An amount contractually stipulated as a reasonable estimation of actual damages to be recovered by one party if the other party breaches; also if the parties to a contract have agreed on Liquidated Damages, the sum fixed is the measure of damages for a breach, whether it exceeds or falls short of the actual damages." However, under Section 74 of the Act, Liquidated Damages are restricted up to a maximum of the sum so named in the Contract and the courts cannot grant any amount by way of damages in excess of such sum. The said section deals with a scenario wherein the parties to a contract have agreed in advance, such

[1] Calicut Engineering works (P) Ltd. Vs. Batliboy Ltd. reported at (2007) 1 Cal LT 466 (470) (HC).
[2] Murlidhar Chiranjilal Vs. Harishchandra Dwarkadas & Anr. reported at AIR 1963 SC 366.

agreement being embodied in the contract itself, upon the penalty for the breach of the contract i.e. liquidated damages. The main principle behind this section is to promote certainty in commercial contracts.

6.2 The opening phrase of Section 74 of the Act reads "*when a contract has been broken*". Therefore, a valid contract between two parties and a breach thereof by a party thereto is a prerequisite before claiming damages under Section 74 of the Act.

6.3 Further, the operative part of Section 74 of the Act reads "*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.*"

7. Liquidated Damages and Penalty

7.1 Originally when the Act was enacted in the year 1872, Section 74 only provided for enforceability of clauses which prescribed for "*Liquidated Damages*". The Section was amended to how it reads today, in the year 1899, to incorporate enforceability of penal clauses. Further, by way of the said amendment, an explanation was appended to Section 74 along with four illustrations [Illustrations (d) though (g)][1] which help distinguish between a genuine pre-estimate of the damages and a penalty. A penalty would be a sum of money, which is stipulated in order to dissuade a party from breaching a contract.

7.2 The courts should not generally categorise liquidated damages as penalties because liquidated damages reduce uncertainty and held in reducing litigation. The terminology used for these damages, penal or liquidated, is not the decisive factor though it is one of the factors to be taken into consideration

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[1] (d) A gives B a bond for the repayment of Rs. 1,000 with interest at 12 per cent. at the end of six months, with a stipulation that, in case of default, interest shall be payable at the rate of 75 per cent. from the date of default. This is a stipulation by way of penalty, and B is only entitled to recover from A such compensation as the Court considers reasonable.

(e) A, who owes money to B a money-lender, undertakes to repay him by delivering to him 10 maunds of grain on a certain date, and stipulates that, in the event of his not delivering the stipulated amount by the stipulated date, he shall be liable to deliver 20 maunds. This is a stipulation by way of penalty, and B is only entitled to reasonable compensation in case of breach.

(f) A undertakes to repay B a loan of Rs. 1,000 by five equal monthly instalments, with a stipulation that in default of payment of any instalment, the whole shall become due. This stipulation is not by way of penalty, and the contract may be enforced according to its terms.

(g) A borrows Rs. 100 from B and gives him a bond for Rs. 200 payable by five yearly instalments of Rs. 40, with a stipulation that, in default of payment of any instalment, the whole shall become due. This is a stipulation by way of penalty

while determining the real nature if these damages whether they are penal or liquidated[1].

7.3 Section 74 of the Act was framed to deal with the doctrine of penalty and liquidated damages as understood in the law in England. In the matter of *Fateh Chand Vs. Balkishan Das*[2], the Hon'ble Supreme Court of India has observed:

> "*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 terrors 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.*"

7.4 The test was the agreement to pay damages for the breach of Covenant or contract unconscionable and extravagant, such as no Court ought to allow to be entered into. No hard-and-fast rule can, however, be laid down as to what may or may not be unconscionable or extravagant to insist upon in the circumstances of the particular case.[3]

8. Proof of Damage or Loss or Injury and the approach of Courts

8.1 The excerpt from Section 74 "*whether or not actual damage or loss is proved to have been caused thereby*" is perhaps the source of a highly debated over controversy, as diverging views and interpretations have been expressed by the Courts over a considerable period of time. The provision 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.[4]

8.2 The expression "*whether or not actual damage or loss is proved to have been caused thereby*" in Section 74 is intended to cover different classes of contracts

[1] Bharat Sanchar Nigam Limited Vs. Reliance Communication Ltd. reported at (2011) 1 SCC 394.
[2] Fateh Chand Vs. Balkishan Das reported at AIR 1963 SC 1405.
[3] Khagaram Das Vs. Ramsankar Das Pramanik reported at (1915) ILR 42 Cal 652.
[4] ibid. p. ix.

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.[1]

8.3 The jurisprudence on the subject seemed to have culminated into the following guidelines being formulated by the Division Bench of the Hon'ble Supreme Court of India in the matter of *Oil and Natural Gas Corporation Ltd. Vs. SAW Pipes Ltd.*[2]:

> "*(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.*
>
> *(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 consequences 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.*"

8.4 However, in the matter of *Kailash Nath Associates Vs. Delhi Development Authority*[3], a Division Bench of the Hon'ble Supreme Court of India differed from the earlier pronouncement in the matter of *ONGC Vs. SAW Pipes (Supra)* and observed that "*Since Section 74 awards reasonable compensation for damage or loss caused by a breach of contract, damage or loss caused is a sine qua non for the applicability of the Section.*" In light of such observation, the Hon'ble Supreme Court further held that "*compensation can only be given for damage or loss suffered. If damage or loss is not suffered, the law does not provide for a windfall.*"

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[1] Maula Bux Vs. Union of India reported at (1969) 2 SCC 554.
[2] Oil and Natural Gas Corporation Ltd. Vs. SAW Pipes Ltd. reported at (2003) 5 SCC 705.
[3] Kailash Nath Associates Vs. Delhi Development Authority reported at (2015) 4 SCC 136.

9. Conclusion

9.1 The finding delivered in the matter of Kailash Nath Associates Vs. DDA (Supra) has led to a lot of debate in as much as it seems to be contrary to the law laid down in the earlier judgments of larger benches of the Hon'ble Supreme Court as well as the judgment delivered by the coordinate bench in the matter of ONGC Vs. Saw Pipes (Supra). It is also true that judicial comity and legal propriety require that a Court cannot overrule an earlier judgment of a coordinate bench. In view of the author, the correct position of law has been summarised by the Hon'ble Calcutta High Court in the following words:

> "*It does not appear that the law laid down in such aspect on ONGC has been completely re-written in Kailash Nath Associates. Indeed, the law written by a two-Judge Bench of the Supreme Court could never have been overruled by another Bench of similar strength. At the highest, paragraph 43.6 of the report in Kailash Nath Associates succinctly enunciates the law without deviating from what was recognised to be the law in Saw Pipes. The law continues to be as it was when Saw Pipes was written: that unless it is difficult or impossible to prove the quantum of damages suffered by a party claiming liquidated damages, the extent of the damages suffered would be required to be proved*"[1]

[1] MBL Infrastructures Limited vs Ircon International Limited reported at 2018 (1) Arb LR 168 (Cal).

Liquidated Damages and Penalty: No distinction under Indian Contract Act, 1872

1. Legislative History

1.1 Common Law created a distinction in the enforcement of the contractual clauses of 'Penalty' and 'Liquidated Damages'. Clauses creating obligations to be followed in case of a breach, in the nature of 'terrorem', were referred to as penalty. They were construed to be unenforceable and in such cases it was held that only reasonable compensation would be payable. The conundrum began when the Indian Contract Act, 1872 ('**Act**') was promulgated and Section 74 of the Act only provided for the enforceability of clauses which prescribed for 'liquidated damages'.

1.2 However, a few years later, in 1899, Section 74 was amended to also include the enforceability of clauses which were in the nature of penalty, within its ambit. Following such codification, the common law principles on the said subject stood excluded, so far as Indian legal jurisprudence was concerned on the subject.

2. Section 73 and 74 of the Act and Judicial Approach

2.1 The bare reading of Section 74 of the Act makes it clear that it does not create any distinction between the concepts of 'penalty' and 'liquidated damages'.

2.2 The Courts in numerous cases dealt with individual cases of penalty and liquidated damages; however, there was no clear exposition of law on the question of whether there was any distinction between the two concepts after the introduction of the amended Section 74 of the Act; until the question arose in *Union of India* v. *Raman Iron Foundry*[1] ('**Raman Iron Foundry**'). In the said case, the court held that '*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*'.

2.3 Intriguingly, the court proceeded to hold that even if there was a stipulation for liquidated damages in a contract, the party would be entitled to only 'reasonable compensation' and that it stood at the same footing as 'unliquidated damages'. Per chance, the said judgment of the Supreme Court was overruled in a later judgment in the case of *H.M. Kamaluddin Ansari and Co.* v. *Union of India* ('**Kamaluddin Ansari**'), however, only in respect of the other dispositions of law (relating to permissibility of passing negative injunction).[2]

2.3.1 Stable ground - Kailash Nath Associates v. Delhi Development Authority[3] ('Kailash Nath'):

2.3.1.1 The above conundrum is now considered to be settled, so far as the principles under Section 73 and 74 of the Act are concerned, owing to *Kailash Nath*, wherein the following was held:

a. Section 74 applies a **UNIFORM PRINCIPLE** to all amounts to be paid in case of breach provided as a stipulation in a contract (whether in the nature of Liquidated Damages/Penalty),

b. Damage or loss having been **CAUSED BY SUCH BREACH** is a sine qua non for the applicability of Section 74,

c. Where it is possible to prove actual damage or loss, such **PROOF IS NOT DISPENSED WITH,**

d. Only in cases where damage/ loss is **Difficult Or Impossible To Prove**, that the liquidated amount (if a **GENUINE PRE-ESTIMATE** of damage or loss fixed by both the parties and found so by the court) can be awarded,

e. In all other cases, **REASONABLE COMPENSATION** can be awarded on the well known principles (to be found in Section 73 of the Act, *inter alia*), not exceeding the liquidated amount stipulated in the contract.

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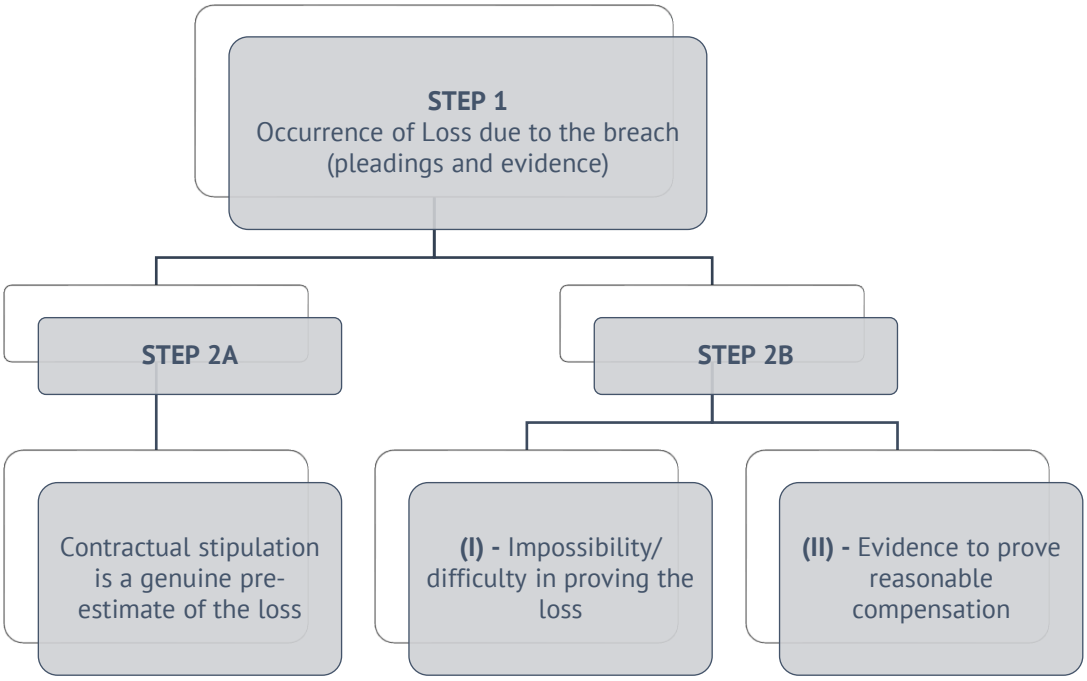
[1] Union of India v. Raman Iron Foundry, (1974) 2 SCC 231.

[2] H.M. Kamaluddin Ansari and Co. v. Union of India, (1983) 4 SCC 417.

[3] Kailash Nath Associates v. Delhi Development Authority, (2015) 4 SCC 136.

2.3.1.2 Thus, following are the tests to be applied by the arbitral tribunals and courts while adjudging cases of entitlement over the liquidated amount under a contract:



2.3.2 Claim of loss *sine qua non* for claim of compensation:

2.3.2.1 The Division Bench of the High Court of Delhi in its judgment dated 18.09.2017 in the case of *Mahanagar Telephone Nigam Limited* v. *Finolex Cables Limited* ('**MTNL**')[1] held that assuming the clause for liquidated

[1] Mahanagar Telephone Nigam Limited v. Finolex Cables Limited, FAO(OS)-227/2017.
Facts: Contract was executed by MTNL with FCL for supply of Jelly Filled Cables (four types). One out of four sizes required approval of Telecom Engineering Centre. Purchase Order dated 20.12.1990 was issued with date of delivery as 20.05.1991. Performance Bank Guarantee was submitted. FCL admittedly failed to deliver the fourth variant within the stipulated time. MTNL kept extending delivery period (approval was received from TEC on 05.08.1991) and requested for extension of PBGs (which was honoured by FCL). Eventually, MTNL raised claim for LDs and invoked the PBGs (available under this contract and other contracts). Arbitral Award dated 18.08.2009 was passed in favour of MTNL holding it could claim LD up to 10% of the ordered value. Single Judge vide Judgment dated 11.04.2017 (in OMP No 746 of 2009) held that sum of LDs were based on no evidence at all and that the invocation was unjustified.
Clause for Liquidated Damages:
"*17. Liquidated Damages*
17.1 The date of delivery of the stores stipulated in the acceptance of Purchase Order should be deemed to be the essence of the contract and delivery must be completed not later than the dates specified therein. Extension will not be given except in exceptional circumstances. Should, however, deliveries be made after expiry of the contract and be accepted by the Consignee, such deliveries will not deprive the Purchaser of his right to recover liquidated damages under Clause 17.2 below, where, however, supplies are made within 21 (twenty one) days of the contracted original delivery period, the consignee may accept the stores and in such cases the provisions of clause 17.2 will not apply.
17.2 Should the tenderer fail to deliver the stores or any consignment thereof within the period prescribed for delivery, the Chairman Cum Managing Director, MTNL, shall be entitled to recover ½% of the

damages was a genuine pre-estimate of the losses, MTNL was obliged to prove before the arbitral tribunal that it had suffered a loss (even though it may have not proven the loss). In fact, in the said case, the Arbitral Tribunal had found that no loss was suffered by MTNL. The Division Bench also upheld the finding of the Single Judge that the Arbitral Tribunal had failed to provide any explanation for providing the maximum limit as provided in the clause and instead, the Arbitral Tribunal should have assessed the reasonable compensation, even if MTNL had proved that it had suffered some loss.

2.3.2.2 Similar was the fate in the Judgment dated 07.07.2015 passed by the Single Judge of the High Court of Delhi in the case of *Tema India Limited* v. *Engineers India Limited*[1] ('**Tema India Limited**'); upheld in the Judgment dated 07.01.2016 by the Division Bench[2] and confirmed by the Supreme Court vide its Judgment dated 06.02.2018.[3] The finding of the Arbitral Tribunal that in a clause of the nature of price reduction, no loss needs to be shown, was set aside and it was reiterated that loss ought to have been claimed to have been suffered due to the delayed delivery (which had not been claimed by EIL). It was also held that evidence ought to have been led to quantify 'reasonable compensation'.

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undelivered stores value of the Order placed; for each week of delay or part thereof, subject to a maximum of 10% of the value of the Order placed."

[1] Tema India Limited v. Engineers India Limited, 2015 (221) DLT 348.

Facts: EIL placed a purchase order dated 27.02.2008 for supply of nine heat exchangers – high pressure from TEMA (for Chennai Petroleum Corporation Limited). Delivery period was of 17 months to be completed on or before 26.07.2009. There was a delay in delivery and it happened on 16.04.2010. On 14.05.2020 payment was released by EIL and thereafter, on 12.08.2010, refund was claimed on the ground of Clause 12 (Price Reduction Clause). TEMA claimed Force Majeure clause and did not refund the amount. EIL invoked arbitration. Arbitral Tribunal vide Award dated 22.10.2012 held that force majeure was not applicable. However, as Clause 12 was merely a price reduction clause and not by way of liquidated damages or penalty, no proof of loss was required and awarded 10% (maximum) of the total ordered value.

Clause for Liquidated Damage:

"*12. Delayed Delivery:*

The time and date of delivery of materials/equipment as stipulated in the Order shall be deemed to be the essence of the contract. In case of delay in execution of the order beyond the date of delivery stipulated in the order or any extensions sanctioned, the Purchaser may at his option either.

(i) Accept delayed delivery for Criminal items i.e. Refrigeration Package, Reciprocating Compressor, Centrifugal Compressor, Pump Multistage Centrifugal (feed Pump), HP Heat Exchangers (Screw Plug/Breach Lock), at prices reduced by a sum equivalent to one (1%) of the total order value for every week of delay or part thereof, limited to a maximum of ten percent (10%) of the total order value.

(ii) For all items other than critical items, accept delayed delivery at prices reduced by a sum equivalent to one (1%) of the total value of delayed equipment/item for every week of delay or part thereof, limited to a maximum ten percent (10%) of the total order value.

(iii) Cancel the order in part of full and purchase such cancelled quantities from elsewhere on account and at risk and cost of the Seller, without prejudice to its right under (i) & (ii) above in respect to goods delivered."

[2] FAO No. 487 of 2015.

[3] Special Leave Petition (C.) No. 11478 of 2016.

2.3.3 Genuine Pre-Estimate of Losses:

2.3.3.1 Going one step back from *Kailash Nath*, the Supreme Court had an opportunity to consider a contract in which it was stipulated that the liquidated damages provided in the contract were a genuine pre-estimate of the losses likely to be suffered by a party if a breach was committed by the other party (and that the said imposition was not by way of penalty). This was in the judgment of *Oil Natural Gas Corporation* v. *Saw Pipes*[1] ('**ONGC**'), wherein, the Arbitral Tribunal had held that as ONGC had failed to establish the loss suffered, it was not entitled to any claim for damages. Supreme Court in this case held that when parties had expressly agreed that the liquidated

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[1] Oil Natural Gas Corporation v. Saw Pipes, 2003) 5 SCC 705.

Facts: Vide letter dated 28.10.1996 the Respondent informed the Petitioner of their inability to supply pipes as per the agreed schedule and sought for extension of 45 days. The Petitioner vide letter dated 04.12.1996 allowed the extension, subject to imposition of liquidated damages for delay. Payment for the supply was made by Petitioner after deducting liquidated damages, which was disputed by Respondent and hence, matter referred to arbitration. Arbitral Tribunal held that reason for delay did not fall under 'Force Majeure' and hence, imposition of liquidated damages was justified. However, held that as the Petitioner failed to establish the loss suffered by it due to the said breach, the act of withholding the amounts was illegal. AT allowed recovery of the amount with interest at the rate of 12% from 01.04.1997 till filing of SOC and at the rate of 18% pendente lite till payment.

Clause for Liquidated Damage:

"*11. Failure and Termination Clause/Liquidated Damages:-*

Time and date of delivery shall be essence of the contract. If the contractor fails to deliver the stores, or any installment thereof within the period fixed for such delivery in the schedule or at any time repudiates the contract before the expiry of such period, the purchaser may, without prejudice to any other right or remedy, available to him to recover damages for breach of the contract:-

(a) Recovery from the contractor as agreed liquidated damages are not by way of penalty, a sum equivalent to 1% (one percent) of the contract price of the whole unit per week for such delay or part thereof (this is an agreed, genuine pre- estimate of damages duly agreed by the parties) which the contractor has failed to deliver within the period fixed for delivery in the schedule, where delivery thereof is accepted after expiry of the aforesaid period. It may be noted that such recovery of liquidated damages may be upto 10% of the contract price of whole unit of stores which the contractor has failed to deliver within the period fixed for delivery, or

(e) It may further be noted that clause (a) provides for recovery of liquidated damages on the cost of contract price of delayed supplies (whole unit) at the rate of 1% of the contract price of the whole unit per week for such delay or part thereof upto a ceiling of 10% of the contract price of delayed supplies (whole unit). Liquidated damages for delay in supplies thus accrued will be recovered by the paying authorities of the purchaser specified in the supply order, from the bill for payment of the cost of material submitted by the contractor or his foreign principals in accordance with the terms of supply order or otherwise.

(f) Notwithstanding anything stated above, equipment and materials will be deemed to have been delivered only when all its components, parts are also delivered. If certain components are not delivered in time the equipment and material will be considered as delayed until such time all the missing parts are also delivered.

12. Levy of liquidated damages (LD) due to delay in supplies.

LD will be imposed on the total value of the order unless 75% of the value ordered is supplied within the stipulate delivery period. Where 75% of the value ordered has been supplied within stipulated delivery period. LD will be imposed on the order value of delayed supply(ies). However, where in judgment of ONGC, the supply of partial quantity does not fulfill the operating need, LD will be imposed on full value of the supply order."

damages stipulated were 'pre-estimated genuine liquidated damages' and not by way of penalty; then there existed no ground for the Arbitral Tribunal to construe otherwise. It also held that the nature of the contract was such that it was difficult for ONGC to prove loss and hence, a pre-estimate had been agreed to by the parties. The court also observed that there was no evidence to suggest that the said quantum was unreasonable.

2.3.3.2 This ground of difficulty or impossibility to prove the loss has been assailed but adopted and upheld in clauses of liquidated damages relating to (I) Procurement of cables to be laid down by MTNL for its telecommunication network;[1] and also in the case of (II) Power Purchase Agreements.[2] In the

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[1] Mahanagar Telephone Nigam Limited v. Haryana Telecom Ltd., 2017 (163) DRJ) 425. (Upheld by Judgment dated 08.10.2018 in *Haryana Telecom Ltd.* v. *Mahanagar Telephone Nigam Limited* in FAO (OS) No. 205 of 2017).

Facts: MTNL floated a tender dated 04.03.1994 for procurement of 55 LCKM of underground Jelly Filled Telephone Cables. HTL's offer was accepted. Purchase orders dated 16.08.1994, 21.09.1994, 29.09.1994 and 18.10.1994 were issued by MTNL. HTL delayed the deliveries by about 1 to 8 months. Extension was allowed subject to imposition of LDs. Purchase Order dated 16.08.1994 was amended on 13.03.1995 whereby delivery time was extended upto 26.03.1995, with application of liquidated damages. The Arbitral Tribunal held that the clause is penal in nature and it was only enforceable to the extent of loss proved. No loss or injury was proved on record and hence, withholding payment of price was unconscionable.

Clause for Liquidated Damages:

"*CLAUSE-16: LIQUIDATED DAMAGES*

16.1 The date of delivery of the stores stipulated in the acceptance of tender should be deemed to be the essence of the contract and delivery must be completed not later than the dates specified therein. Extension will not be given except in exceptional circumstances. Should however, deliveries be made after expiry of the contract delivery period without prior concurrence of the purchaser, and be accepted by the consignee, such deliveries will not deprive the purchaser of his right to recover liquidated damages under clause 16.2 below. However, when supply is made within 21 days of the contracted original delivery period, the consignee may accept the stores and in such cases the provision of clause 16.2 will not apply. The grace period of 21 days shall be applicable only for delivery of stores and not for inspection.

16.2 Should the tenderer fails to deliver the stores or any consignment thereof within the period prescribed for delivery the Chairman and Managing Director. MTNL shall be entitled to recover ½% of the value of the delayed supply for each week of delay or part thereof, subject to maximum of 10% of the value of the delayed Supply, provided that delayed portion of the supply does not in any way hamper the commissioning of the system. Where the delayed portion of supply materially hampers installation and commissioning of the system, Liquidated damages (not as a penalty) shall be levied as above on the total value of the Contract"

[2] S.L.P. (C.) No. 4289-4290 of 2019 (pending before the Supreme Court) against Judgment dated 18.01.2018 in *NTPC Vidyut Vyapar Nigam Limited* v. *M/s Saisudhir Energy Limited* reported at 2018 (248) DLT 141.

Facts: Petitioner was designated as a nodal agency with an object to deploy 20,000 MW of grid connected by solar power by 2022. PPA dated 24.01.2012 was executed in furtherance of above Mission (though competitive bidding) with SEL for purchase of power at fixed rates for 25 years, with commissioning date for 20MW as 26.02.2012. SEL completed commissioning of 10 MW on 26.04.2013 and remaining 10 MW on 24.07.2013. SEL made a request for extension and the same was rejected. The Arbitral Tribunal by majority award held that claims of liquidated damages was illegal as no loss was suffered by Petitioner and hence, it was held that SEL was entitled to return of the performance bank guarantee. Yet taking cognizance of the delay, it was held that SEL was liable to pay 20% of the amount

matter of *NTPC Vidyut Vyapar Nigam Limited v. M/s Saisudhir Energy Limited* ('**NTPC**') (relating to Power Purchase Agreements), the Division Bench of the High Court of Delhi specifically held that in a project of this nature, if there was a delay then the same was going to cause loss (which was impossible to prove) and hence, the clause therein was held to be a genuine pre-estimate.

2.3.3.3 Taking leave from the dicta of the *ONGC*, it is intriguing to note the view of the High Court of Bombay in the Judgment dated 10.04.2018 in the case of *Titagarh Wagons Ltd.* v. *Chowgule and Company Private Limited*[1] ('**Titagarh Wagons**'). In this case, the clause referred to the expression 'penalty' and the court held that mere use of the word would not be decisive and the contractual provision is required to be interpreted.

3. Conclusion

3.1 The benchmark has clearly been established by the Judgment of the Supreme Court in the *Kailash Nath*. However, there is no fixed yardstick and

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specified in the original bank guarantee. The Single Judge deemed it appropriate to allow half of the claim made by Petitioner. The Division Bench carried out the calculation as per Clause 4.6,
Clause for Liquidated Damages:
"*4.6 Liquidated Damages for delay in commencement of supply of power to NVVN*
4.6.1 If the SPD is unable to commence supply of power to NVVN by the Scheduled Commissioning Date other than for the reasons specified in Article 4.5.1, the SPD shall pay to NVVN, Liquidated Damages for the delay in such commencement of supply of power and making the Contracted Capacity available for dispatch by the Scheduled Commissioning Date as per the following:
a. Delay upto one (1) month- NVVN will encash 20% of total Performance Bank Guarantee proportionate to the Capacity not commissioned.
b. Delay of more than one (1) month and upto two months- NVVN will encash 40% of the total Performance Bank Guarantee proportionate to the Capacity not commissioned. c. Delay of more than two and upto three months- NVVN will encash the remaining Performance Bank Guarantee proportionate to the Capacity not commissioned. 4.6.2 In case the commissioning of Power Project is delayed beyond three (3) months, the SPD shall pay to NVVN, the Liquidated Damages at rate of Rs.1,00,000/- per MW per day of delay for the delay in such remaining Capacity which is not commissioned. The amount of liquidated damages would be recovered from the SPD from the payments due on account of sale of solar power to NVVN.
4.6.3 The maximum time period allowed for commissioning of the full Project Capacity with encashment of Performance Bank Guarantee and payment of Liquidated Damages shall be limited to eighteen (18) months from the Effective Date. In case, the commissioning of the Power Project is delayed beyond eighteen (18) months from the Effective Date, it shall be considered as an SPD Event of Default and provisions of Article 13 shall apply and the Contracted Capacity shall stand reduced/amended to the Project Capacity Commissioned within 18 months of the Effective Date and the PPA for the balance Capacity will stand terminated.
4.6.4 However, if as a consequence of delay in commissioning, the applicable tariff changes, that part of the capacity of the Project for which the commissioning has been delayed shall be paid at the tariff as per Article 9.2 of this Agreement."

[1] Titagarh Wagons Ltd. v. Chowgule and Company Private Limited, 2018 (4) MahLJ 638 (Upheld by Supreme Court vide its Order dated 26.10.2018 in SLP No. 28040 of 2018.)
Clause for Liquidated Damage:
"*iii. In the event of delay in effecting delivery of rakes, a penalty at the rate of 0.50% per week to be charged upto a maximum of 5% on undelivered rakes as per the schedule mentioned. The penalty to be applicable even if there is a single wagon shortage in formation of a rake."*

accordingly, each case provides its own facts, pleadings and evidence which shall enable the adjudicating bodies to take case centric views in their respect. In reverence of the above, the final view of the Supreme Court in the case of *NTPC*, is a definite to watch out for.

Specific Performance of Contract: An Analysis

1. Introduction

1.1 The law of contract in India prescribes two methods of achieving the "compensation goal." The first one requires the breaching party to pay damages, either to enable the promisee to pay for substitute performance or to replace the net gains that the promised performance would have generated. The alternative arrangement to the above scheme requires the breaching party to perform its promise. This alternative arrangement is governed by the Specific Relief Act, 1963 (**the "SRA"**). However, this alternative arrangement in the form of specific performance is available only at the discretion of the court, which cannot be exercised arbitrarily, and is required to be guided by judicial principles.

1.2 The Court is not bound to grant such relief merely on the ground of it being lawful. The remedy of specific performance is an equitable relief, given by the Court of law to enforce upon the defaulting party, the duty of doing what was agreed under the contract. The court of law for the purpose of specific performance can order the execution of any action; though the right is usually enforced so as to complete a transaction that had been previously agreed to.

1.3 The reasons for the court to order specific performance can be profound, ranging from the fact that in some contracts the consequences of breach

cannot be compensated by money to the true amount of damages being indeterminable,[1] keeping in mind that specific performance is the exception and damages is the rule. However, the laws related to specific performance, have undergone a change due to an amendment in 2018, as discussed hereinafter.

2. Expressly Excluded Contracts

2.1 Section 14 of the SRA enumerates certain kinds of contracts for which the relief of specific performance cannot be granted. The said provision includes within its ambit contracts where a non-defaulting party to the contract has obtained substituted performance of the contact in accordance with Section 20 of the SRA (being one of the key amendment to SRA in 2018).

2.2 Further, contracts involving the performance of a continuous duty which the court cannot supervise are specifically excluded. In addition to the above, contracts which are dependent on the personal qualifications of the parties and the contracts which are by nature determinable are also excluded.

3. Remedy of Injunction v. Specific Performance

3.1 Injunction is a form of specific relief. It is an order of a court requiring a party to either do or refrain from doing a particular act, for a limited period or permanently.[2]

a. **Mandatory Injunction:** To do a specific act, or

b. **Prohibitory Injunction:** To refrain from doing a particular act for a limited period or without any limit of time.

3.2 Specific performance is the ideal method of compelling a party to perform its positive obligation under the contract. An injunction may often be issued to enforce the terms of a contract, which the Court would not enforce directly by an order/ direction for specific performance. The Court may in an appropriate case also grant injunctions in aid of specific performance, either temporarily, perpetually or mandatorily, in accordance with Section 37 and 39 of SRA.

3.3 The cardinal principles for grant of temporary injunction were considered in the case of *Dalpat Kumar v. Prahlad Singh*[3] ("**Dalpat Kumar Judgement**") wherein the Hon'ble Supreme Court held that a Court has to be satisfied that the non-interference by the Court would result in an "irreparable injury" to the party. The party seeking relief would have to satisfy the Court that it has not been left with any other remedy except being granted an injunction and requires protection from the consequences of the apprehended injury or dispossession. Further, the Hon'ble Supreme Court in case of *Ambalal*

[1] Section 10, Specific Relief Act, 1963.
[2] Adhunik Steels Limited v. Orissa Manganese & Minerals Private Limited AIR 2007 SC 2563.
[3] Dalpat Kumar v. Prahlad Singh, (1992) 1 SCC 719.

Sarabhai Enterprise Limited v. KS Infrastructure LLP Limited & Anr.[1] (**Ambalal Judgement**") reiterated the cardinal principle that a party seeking temporary injunction in a suit for specific performance will have to establish a strong *prima-facie* case on the basis of undisputed facts. Evidently, the conduct of the plaintiff is a relevant consideration for the purposes of seeking injunction.

4. Limitation

4.1 As per Article 54 of the Schedule to the Limitation Act, 1963 (**the "Act**"), the period available prior to filing a suit for specific performance of a contract is three years. The limitation for filing a suit for specific performance has been held to commence from the date fixed for performance. In cases, where no date is fixed for performance under the contract, the limitation period is said to commence from the date when the non-defaulting party takes note that the defaulting party has refused to perform its obligation under the contract.[2] Further, the Hon'ble Supreme Court has conclusively interpreted the term "*date fixed for performance*" as mentioned in Article 54 in the case of *Ahmadsahab Abdul Mulla (2) v. Bibijan*[3] ("**Ahmadsahab Judgement**").

4.2 Moreover, the Hon'ble Supreme Court of India in the case of *R Lakshmikantham v. Devarji*[4] ("**Lakshmikantham Judgement**") held that delay in filing a suit for specific performance is not a ground to deny relief, if the same was filed within the limitation period.

5. Specific Relief (Amendment) Act, 2018 ("Amendment Act")

5.1 The Amendment Act[5] introduces a paradigm shift in the prevalent law regarding contractual enforcement in India, shifting the focus from the previous default remedy of award of damages for breach of contract to enforcing specific performance of contracts. The major changes include:

5.1.1 **Amendment to Section 20:** Introduction of the remedy of substituted performance of a contract by a third party. The duty of computation of losses suffered was always cast on the party that suffered a breach and the amended Section 20 in fact is a statutory recognition of the said obligation. The SRA now enables the party that suffered the breach to sue for accepting performance from a third party and seeking recovery of the cost incurred in accepting such substituted performance from the party that committed breach. The pre-requisite for this remedy is that the party that suffers the breach is required to give a notice in writing, of not less than thirty days to the breaching party to remedy the breach. The statutory notice period of thirty days may also deter

[1] Ambalal Sarabhai Enterprise Limited v. KS Infrastructure LLP Limited & Anr., Civil Appeal No. 9346 of 2019.
[2] Shakuntala v. Narayan Gundoi Chavan, AIR 2000 SC 3921.
[3] Ahmadsahab Abdul Mulla (2) v. Bibijan, (2009) 5 SCC 462.
[4] R Lakshmikantham v. Devarji, Civil Appeal No. 2420 of 2018.
[5] The Specific Relief (Amendment) Act, 2018 No. 18 of 2018.

the occurrence of a breach of contract and parties may instead of litigating, choose to perform or re-negotiate the contract within the notice period. This would encourage continuation of contractual relationships and achieve the intended objectives of the contract.

5.1.2 **Substitution of Sections 10 and 14:** The former regime statutorily provided the remedy of specific performance in cases where compensation would not be an adequate relief or where there were no standards to ascertain the compensation which was due. The said provision has been replaced with a new provision which identifies only the following limited situations where specific performance cannot be enforced:

a. Contract made by a trustee in excess of his powers or in breach of trust [Section 11(2)].
b. Contracts where the substituted performance has been obtained by the non-defaulting party [Section 14(a)].
c. A contract, the performance of which involves the performance of a continuous duty which the court cannot supervise [Section 14(b)]
d. A contract which is so dependent on the personal qualifications of the parties that the court cannot enforce specific performance of its material terms [Section 14(c)].
e. A contract which is in its nature determinable [Section 14(d)].
f. When defaulting party itself has violated an essential term, or has become incapable of performance, or has acted fraudulently [Section 16(b)].
g. When the defaulting party fails to prove that he has performed his obligations or fails to show his readiness and willingness to perform his obligations [Section 16(c)].

5.1.3 **Insertion of Section 14A:** Grants power to the court of law to engage experts to assist it on any specific issue involved in the suit (technical or scientific).

5.1.4 **Insertion of Sections 20A & 20B:** Referring to the infrastructure project contracts, the court has now been refrained from granting an injunction in any suit, whereby it could cause hindrance or delay in the continuance or completion of the infrastructure project. The said amendment has been inserted as infrastructure projects have an inherent public interest involved in them. This has been fashioned as a special provision. The intent behind the said provision has been held to be in order to ensure that infrastructure projects are not delayed on account of pendency of Court proceedings with respect thereto and/or on account of orders in such Court proceedings.[1] Accordingly, a corresponding amendment has been made to Section 41 of the SRA, which defines the situation wherein injunctions cannot be granted.

[1] Order dated 22.08.2019 passed in CS (OS) No. 423 of 2019.

Further, a provision has been introduced for the designation of one or more Civil Courts as Special Courts to promote expeditious disposal of suits relating to infrastructure projects, given the element of public interest in such suits [Section 20B]. A timeline of 12 months has also been prescribed (extendable by 6 months) for concluding such proceedings under Section 20C.

5.2 The Amendment Act itself does not provide any guidance on whether the amendments would operate prospectively or retrospectively. A "saving clause" or a "transitory provision" is conspicuous by its absence. However, the Amendment Act is likely to be perceived as one modifying substantive rights since it provides for modifying the law of remedies. It is a well settled position that amendments to remedial provisions are always regarded as prospective and those being declaratory in nature, are considered retrospective.[1]

5.3 However, Courts have time and again reiterated the position that the amendments to substantive law do not apply to pending proceedings and apply only prospectively, while amendments to procedural law can apply to pending proceedings.[2] There is a brawny view that the SRA is in fact procedural as it provides a form of judicial distress. The same view has been upheld by courts in various decisions.[3] In the recent case of *Church of North India v. Ashoke Biswas*[4] ("**Church of North India Judgement**"), the Hon'ble Calcutta High Court sought to determine the applicability of the Amendment to the facts of the case, wherein the Amendment came into force during the pendency of the suit. The Court held that the Amendment would apply to the case at hand. Further, in *Radheshyam Kamila v. Kiran Bala*,[5] **("R. Kamila Judgement")** it was held that *"after the enforcement of the 1963 Act, the 1963 Act would apply to pending proceedings instituted under the Specific Relief Act 1877."* The same trend may also be adopted for the instant Amendment. It is thus, essential to adjacently consider the possibility of the Amendment having a retrospective operation.

5.4 In the absence of a clause catering to the question of whether the amendment will have retrospective or prospective operation, it is safe to say that the Courts will be at liberty to analyse the same. Thus, while the power to grant specific performance is no more discretionary, its applicability to pending suits may invite some discretion.

6. Conclusion

[1] Sukhram Singh & Anr. v. Smt. Harbheji, AIR 1969 SC 1114; Furthermore, as per Section 6 of the General Clauses Act, 1897, the rights and obligations accrued prior to the bringing into force a legislation or regulation, would not affect or repeal any right/ privilege/ obligation/ liability of the parties.

[2] KS Paripoornan v. State of Kerala, (1994) 5 SCC 593.

[3] Adhunik Steels Ltd. v. Orissa Manganese & Minerals Pvt. Ltd., (2007) 7 SCC 125.

[4] Church of North India v. Ashoke Biswas, C.O. No. 863 of 2019.

[5] Radheshyam Kamila v Kiran Bala, AIR 1971 Cal 341.

6.1 The Amendment Act has sought to minimize the scope of subjectivity in the suits seeking specific performance of contracts and statutorily ascertain the nature of contracts where specific performance can be granted. The Amendment Act has brought in a new aura to the flowing breeze by adding provisions which are intended to reduce litigations and ensure the performance of contractual work in a timely manner, along with the introduction of the concepts of substituted performance and the imposition of time limits for the disposal of cases.

6.2 Altering the nature of specific relief from an exceptional rule to a general rule is a certain step forward in the sphere of contractual enforcement. The success of this endeavour shall gradually see the light of day.

Covid-19: An impetus to the era of Electronic Contracts

1. Introduction

1.1. With the advancement of technology, the conventional ways of undertaking activities have vastly been replaced with technologically ameliorated methods. One such upgrade is the materialization of the concept of Electronic Contracts ("**E-Contracts"**), which have become increasingly germane amidst the worldwide lockdowns pursuant to the emergence of COVID-19. The consistent need to strive to the fore with time and espouse new modes of doing business, combined with the repercussions of a virus inflicted world, personifies the importance of augmenting the use of modern concepts like E-Contracts.

1.2. While Section 2(h) of the Indian Contract Act, 1872 ("**1872 Act**") defines a 'contract' as an agreement enforceable by law, the term 'E-contract' does not find a place under the 1872 Act. However, the lack of a separate mention does not preclude E-contracts from falling within the ambit of the 1872 Act. As discussed in ***ABC Laminart Pvt. Ltd. vs A.P. Agencies Salem*** **(ABC Laminart Judgement)**,[1] unlike the traditional paper-based contracts, an E-Contract is entered into between the parties through an electronic means such as the internet, a computer database, a software etc. Apart from the *sine qua non*

[1] Reported at AIR (1989) SC 1239.

difference in the modes of their execution, E-contracts are inherently similar to traditional contracts and equally recognized by law. E-Contracts have found their way into our daily routines, whether it be inadvertent or intentional. A few examples of E-Contracts includes:

- buying airplane/railway tickets online either through a government portal such as the IRCTC App or private portals such as Paytm, Make My Trip, etc.;
- purchasing products online using e-commerce platforms;
- ordering groceries or cooked food online;
- withdrawing cash from an ATM or transferring money through apps such as Google Pay, Paytm, etc.; and
- booking a cab or an auto-rickshaw online through apps such as Uber, Ola, etc.

2 Types of E-contracts

2.1 Email Contract:

2.1.1 Parties may enter a valid e-contract through email, i.e. by exchanging the terms and conditions of the contract or negotiating the same via email. These emails have the same value as that of letters exchanged between both the parties. In the case of ***Trimex International FZE Limited, Dubai v. Vendata Aluminium Ltd.*** **(Trimex International Judgement),**[1] the Hon'ble Supreme Court held that an electronic contract devoid of an electronic signature and registration may be enforceable as long as it abides by the essentials of a valid contract under the 1872 Act.

2.2 Click-wrap Contract:

2.2.1 It is a type of contract wherein the user expresses his consent towards the offer to contract on the perusal of the terms and conditions of the website, by either clicking on "Agree" or "Disagree" option so as to proceed further. This is generally the type of contract associated with privacy policies, user policies, etc. It is a standard form of contract, thus eliminating the scope of any kind of negotiation. It was held in ***LIC India vs. Consumer Education and Research Centre*** **(LIC India Judgement)**[2]*,* that in such adhesion contracts, the unequal bargaining power between the parties, strikes at the root of Article 14 of the constitution, and thus, they may be struck down by the courts.

2.3 Shrink-wrap Contract:

2.3.1 It is a license agreement wherein the terms and conditions are enumerated on the package of the product, generally a software, and the consumers are required to be mindful about the same prior to opening or using the product. As soon as the consumer unpacks the package, the terms and conditions become binding upon him. Warranties, limitations of liabilities and licenses

[1] Reported at 2010 (1) SCALE 574.
[2] Reported at (1995) 5 SCC 482.

are often covered under Shrink Wrap category agreements. The act of tearing or opening the product when the license agreement is on display, amounts to an act of acceptance of its terms on the part of the user as affirmed in the case of ***ProCD, Inc. v. Zeidenberg*** **(ProCD Judgement)**[1]**.** For example, installation of any software from CD, which generally contains terms and conditions on the pack and upon tearing of the pack, the user is deemed to have consented to the said terms and conditions.

2.4 Browse-wrap Contract:

2.4.1 In these kinds of contracts, there exists a hyperlink to the terms and conditions, displayed on the website. Once the user uses the website, he is deemed to have accepted the terms and conditions contained in the hyperlink on that specific website. For example, online shopping websites generally have a link to their terms and conditions, which are deemed to have been accepted when an order is placed, making the customer bound by such terms.

3 Validity of E-Contracts

3.1 Information Technology Act, 2000 ("2000 Act")

3.1.1 **Validity of Contracts formed through Electronic Means**: Section 10A of the Information Technologies Act, 2000 ("**2000 Act**") recognizes e-contracts and further elucidates that a contract cannot be deemed to be unenforceable merely because it is based on electronic communications, *vis-à-vis* the offer and acceptance. The validity of such contracts was upheld in the case of ***Dr. Mandeep Sethi v. Union Bank of India & Ors.*** **(Dr. Mandeep Sethi Judgement),**[2] which granted legality to electronic communications with respect to a contract.

3.1.2 There are, however, certain exceptions which do not gain validity if made via electronic means. Negotiable instruments (barring cheques), wills and testaments, documents for sale of immovable property, power of attorney and trust deeds are certain contracts that are required to be made and executed physically in order to be valid under law.

3.1.3 **Legal recognition to Electronic Records**[3] **and Electronic Signatures:**[4] Section 4 of the 2000 Act grants legal recognition to electronic records. Electronic records are thus acceptable when law requires certain information or matter to be either in the written or printed form. Additionally, an electronic signature is required to ascertain the acceptance of terms and conditions of the contract. As held in ***State of Punjab v. Amritsar Beverages Ltd.*** (**Amritsar**

[1] Reported at 86 F. 3d 1447 (7th Cir. 1996).
[2] Reported in AIR (2013) (P&H) 82.
[3] Section 4 of Information Technology Act, 2000.
[4] Section 5 of Information Technology Act, 2000.

Beverages Judgement),[1] electronic records are deemed as adequate means of evidence under Indian Law.

3.1.4 Terms relevant to E-Contracts in the 2000 Act:

- Originator[2]: Any person who sends, generates, stores or transmits any electronic message, or causes to do the same; and
- Addressee[3]: Any person who is intended by Originator to receive the electronic record; and
- Digital Signature[4] and Electronic Signature[5]: These are the types of signatures that are used to authenticate the electronic records;[6] and
- Attribution of Electronic Record:[7] An electronic record is attributed to its originator or any person authorized by him, if it is sent by them or by an information system programmed by them; and
- Acknowledgment of Receipt:[8] This provision elucidates in depth, the essentials of acknowledgment by the addressee, of receipt of an electronic record sent by the Originator.

3.2 The Indian Contract Act, 1872

3.2.1 **No explicit provision but enforceable if all the conditions required for a standard contracts are met:** Although there is no explicit provision providing for an e-contract, there also exists no provision under the 1872 Act, which prohibits the same. Except for the mode of execution, E-Contracts are treated in the same manner as that of traditional contracts. The essentials of an E-Contracts are same as that of a contract provided under the 1872 Act, namely, offer and acceptance, consideration, free consent, lawful object, intention to contract, competency of parties and legal enforceability.

3.2.2 However, Courts have time and again laid emphasis on the intention of the parties to contract being of prime importance for the validity of the contract instead of the means. In the recent case of ***Ambalal Sarabhai Enterprise Limited v. KS Infraspace LLP Limited*** **(Ambalal Sarabhai Judgement),**[9] the Hon'ble Supreme Court assessed the validity of an agreement entered into using a combination of emails and WhatsApp messages. The Court held that there was no evident intention to accept the proposal in the correspondence, making the agreement invalid.

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[1] Reported at (2006) 7 SCC 607.
[2] Section 2 (za) of Information Technology Act, 2000.
[3] Section 2 (b) of Information Technology Act, 2000.
[4] Section 2 (p) of Information Technology Act, 2000.
[5] Section 2 (ta) of Information Technology Act, 2000.
[6] Section 2 (r) of Information Technology Act, 2000.
[7] Section 11 of Information Technology Act, 2000.
[8] Section 12 of Information Technology Act, 2000.
[9] Reported in (2020) SCC OnLine 1.

3.3 **The Indian Evidence Act, 1872:**

3.3.1 **Section 65A, 65B governing the admission of an electronic evidence:** Section 65A of the Indian Evidence Act, 1872 ('**Evidence Act**') recognizes electronic documents and further states that the same are admissible in evidence, subject to the conditions prescribed by Section 65B. Further, Sections 80A, 80B, 85C of the Evidence Act deal with presumptions pertaining to electronic records and electronic signatures. The Hon'ble High Court of Delhi dealing with the issue of admissibility of electronic records in ***State v. Mohd. Afzal and Ors.*** **(Mohd. Afzal Judgement),**[1] held that electronic records are admissible as evidence and any challenge to them must be proved beyond doubt. Further, in the case of ***Harpal Singh & Ors. v. State of Punjab*** **(Harpal Singh Judgement)**,[2] the Apex Court held that computer generated electronic records are evidence, admissible at a trial if proved in the manner specified by Section 65B of the Evidence Act.

3.3.2 It was further observed in ***Anwar PV v. PK Basheer and Others*** **(Anwar PV Judgement),**[3] that Sub-section (1) of Section 65B makes admissible as a document, paper print-out of electronic records stored in optical or magnetic media produced by a computer, subject to the fulfilment of the conditions specified in Sub-section (2) of Section 65B.

4 Jurisdiction with respect to E-contracts

4.1 Generally, in deciding the jurisdiction of Courts in cases of contracts, the governing section of law is Section 20 of the Code of Civil Procedure, 1908 (**"1908 Code"**), which stipulates that the Courts within whose local limits, the cause of action arose or the place of residence of Defendant exists, will have jurisdiction.

4.2 Notwithstanding the above practice, in case of E-Contracts, Section 13 of the 2000 Act specifically deals with the issue of jurisdiction and lays down that an electronic record is deemed to be dispatched where the originator has his place of business; and is deemed to be received where the addressee has his place of business as noted in ***Union Of India v. M/S G.S. Chatha Rice Mills*** **(Chatha Rice Mills Judgement)**.[4] Therefore, in view of Section 13 of the 2000 Act, the place where the cause of action arose would be deemed to be the place of business of the Originator or of the Addressee, except where no specific clause of jurisdiction is provided. If there are more than one places of business, the principal place of business would be deemed to be the place where the cause of action has arisen.

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[1] Reported at 107 (2003) DLT 385.
[2] Criminal Appeal No. 2539 of 2014.
[3] Reported at (2014) 10 SCC 473.
[4] Reported at 2020 SCC OnLine SC 770.

4.3 Deliberating on the issue of territorial jurisdiction, the Hon'ble High Court of Delhi in ***Casio India Co. Limited v. Ashita Tele Systems Pvt. Limited*** **(Casio India Judgement),**[1] observed that since the domain name of the website could be accessed from anywhere, the jurisdiction could not be confined to the territorial limits of the residence of the defendant. Therefore, the law, in such cases, does not require proof that any deception occurred at the place in question. Accordingly, the fact that the website of defendant No. 1 could be accessed from Delhi, the same was deemed sufficient to invoke the territorial jurisdiction of the Hon'ble High Court at Delhi.

4.4 The issue of Jurisdiction has also been settled by the Hon'ble High Court of Allahabad in the noted judgment of ***P.R Transport Agency v. Union of India*** **(P.R Transport Agency Judgement),**[2] where the Petitioner contended that the communication pertaining to the contract took place on the internet and thus, the Court had no jurisdiction to entertain the matter. The Court relying on Section 13 of the 2000 Act observed that the place of business of the Petitioner was in Uttar Pradesh and therefore the Allahabad High Court undeniably had jurisdiction to entertain the dispute.

5 Conclusion

5.1 The fairly novel nature of electronic contracts inevitably opens doors to a plethora of unanswered questions, as well as possibilities. Unexplored questions regarding the security and legitimacy of E-contracts with cybercrime widely prevalent in the society; the evolving applicability of the Stamp Act, 1899 (**"1899 Act"**) on E-Contracts; an alleviated possibility of negotiation in standard form contracts, etc. are yet to achieve a uniform verdict across different courts in the country. However, considering the unstoppable pace with which technological advancements are gaining social acceptance, the possibility of delving into each question and reaching a better and more advanced verdict is certainly not bleak.

5.2 The introduction of E-Contracts paves way for a faster and more efficient route to enter into a contract without wasting valuable monetary and human resources. This concept also eliminates the requirement of physically meeting the other party and provides ease of business. The same has become even more relevant now since social distancing has become a norm in the wake of unprecedented Covid-19 situation. Consequently, two people sitting in two countries on the opposite sides of the globe can enter into E-Contracts, without having to physically travel anywhere in order to sign and execute the agreement. In the wake of the concerning ongoing pandemic, the provision of entering into a contract via electronic means is indisputably a boon to the world.

[1] Reported at 106 (2003) DLT 554.
[2] Reported at AIR 2006 All 23.