

IN THE HIGH COURT OF KERALA AT ERNAKULAM

PRESENT:

THE HONOURABLE MR. JUSTICE A.HARIPRASAD

MONDAY, THE 9TH DAY OF FEBRUARY 2015/20TH MAGHA, 1936

SA.No. 207 of 2003 ()

AGAINST THE JUDGMENT AND DECREE IN A.S.NO. 109/1999 of ADDITIONAL DISTRICT
COURT, NORTH PARAVUR DATED 10-09-2002

AGAINST THE JUDGMENT AND DECREE IN O.S.NO. 342/1997 of MUNSIF COURT, NORTH
PARAVUR DATED 11-03-1999

APPELLANT(S)/(APPELLANTS - DEFENDANTS):

1. ABDU, SON OF KATHIRU, THEKKUMPURAM
MURI, CHENDAMANGALAM VILLAGE, PARAVUR TALUK
NOW RESIDING AT KUZHIKKADAVIL PALLITHAZHAM MURI
PARAVUR VILLAGE, PARAVUR TALUK.
2. SOFIA BEEVI, WIFE ABDU,
THEKKUMPURAM MURI, CHENDAMANGALAM VILLAGE
PARAVUR TALUK, NOW RESIDING AT KUZHIKADAVIL
PALLITHAZHAM MURI, PARAVUR VILLAGE, PARAVUR TALUK.

BY ADVS.SRI.T.K.VENUGOPALAN
SRI.SHIBU JOSEPH

RESPONDENT(S)/(RESPONDENTS - PLAINTIFFS):

1. PADMANABHAN, SON OF PAPPU,
PALACKAPARAMBIL, KEDAMANGALAM MURI, PARAVUR VILLAGE
PARAVUR TALUK.
2. DIVAKARAN, SON OF KRISHNAN, ETTMMEL,
PARAVOOTHARA MURI, PARUR VILLAGE, PARAVUR TALUK.

R1 & R2 BY ADV. SRI.T.K.RADHAKRISHNAN
R1 & R2 BY ADV. SMT.K.L.SREEDEVI

THIS SECOND APPEAL HAVING BEEN FINALLY HEARD ON 09-02-2015, THE
COURT ON THE SAME DAY DELIVERED THE FOLLOWING:

“C.R.”

A.HARIPRASAD, J.

S.A. No.207 of 2003

Dated this the 9th day of February, 2015

JUDGMENT

Following substantial questions of law are framed in this second appeal:

i. Whether the respondents/plaintiffs are entitled to seek return of advance money from the appellants/defendants paid pursuant to Ext.A1 agreement for sale of property?

ii. Whether the provisions in Section 74 of the Indian Contract Act, 1872 (in short, “the Act”) adversely affect such a claim?

2. Heard the learned counsel for the appellants and the respondents.

3. Facts of the case, shortly stated, are as follows: Appellants are the defendants in a suit for return of amount paid pursuant to Ext.A1 agreement to assign property. Appellants are the owners of property described in Ext.A1. The respondents agreed to purchase property and an amount of ₹75,000/- was paid to the appellants on the date of execution of Ext.A1, ie., 15.12.1994 as advance purchase price. Parties have agreed to complete the transaction as provided in Ext.A1. Fact remains that the

transaction did not go through as agreed to between the parties. Finally the respondents filed the suit seeking return of advance money paid pursuant to Ext.A1. The suit was resisted by the appellants contending that the respondents were responsible for the breach of contract. It is also submitted that on account of the breach committed by the respondents, the appellants suffered pecuniary loss. Therefore, they are entitled to forfeit the advance money of ₹75,000/- paid by the respondents as per the terms in Ext.A1.

4. The trial court found that the appellants are not entitled to forfeit the advance amount received by them. Case put forward by the appellants that they suffered damage on account of wrongful breach committed by the respondents was negated by the trial court. The appellants preferred an appeal before the lower appellate court, wherein the learned Judge found that even if the respondents are held liable for the breach of contract, the appellants are not entitled to forfeit the advance amount received pursuant to Ext.A1. The lower appellate court therefore dismissed the appeal confirming the decree and judgment passed by the trial court.

5. Learned counsel for the appellants contended that the view taken by the lower appellate court cannot be justified. Attention of this Court is drawn to paragraph 8 of the lower appellate court's judgment wherein the learned Judge observed that the appellants were not

responsible for breach of the agreement. It also found that the respondents were not ready and willing to perform their part of the contract. Still the lower appellate court held that the appellants are not entitled to forfeit a sum of ₹75,000/- which was paid as part of purchase price agreed upon between the parties. Learned counsel for the appellants submitted that this finding of the court below cannot be justified in view of the fact that the appellants are entitled to get reasonable compensation for the breach as per Section 74 of the Act.

6. In answer to this argument, learned counsel for the respondents contended that the appellants cannot claim compensation since they failed to establish any damage on account of non-performance of the contract by the respondents. It is an admitted case that none of the parties had approached the trial court with a suit for specific performance of the contract. It is apposite to note here that if a party to a contract for sale of property files a suit for return of advance money, it presupposes the fact that the party is treating the contract as rescinded. In other words, a party claiming return of advance money cannot claim specific performance as he has not kept the contract alive. In the case on hand, the appellants also did not file any suit for specific performance and there is no dispute raised by them regarding the rescission of the contract by the respondents. Therefore, this can be viewed essentially as a suit for money only.

7. The cardinal distinction between Sections 73 and 74 of the Act

is to be borne-in-mind in this context. Section 73 of the Act deals with compensation for loss or damage caused by breach of contract. The Section reads as follows:

“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.”*

It can be seen that the first paragraph of the Section deals with compensation for loss or damage caused by the breach of contract. It further states that where a contract is broken, the party who suffered from the breach of contract is entitled to receive compensation from the party who has broken the contract. The compensation can be recovered for loss or damage under the following circumstances: (i) that arose in the usual course of things from such breach or (ii) which the parties knew at the time they made the contract as likely to result from such breach. It is important to note that the second paragraph of the Section provides that no compensation is payable for any remote or indirect loss or damage. The third paragraph of the Section applies the same principles where breach occurs when an obligation resembling those created by contract has been incurred. It is noteworthy that we are not concerned with these limbs of the Section. In contradistinction to Section 73 of the Act, it can be seen from the caption to Section 74 of the Act itself that it deals with compensation for breach of contract, where penalty is stipulated for in the contract itself. Section 74 of the Act reads as follows:

“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.”

The principle in Section 74 of the Act is that a party to a contract may agree at the time of contracting that in the event of a breach, the party in default shall pay a stipulated sum of money to the other or may agree that in the event of breach by one party, any amount paid by him to the other shall be forfeited. If the sum is a genuine pre-estimate of damages likely to flow

from the breach, it is called 'liquidated damages'. If it is not a genuine estimate, but an amount intended to secure performance of the contract, it may be a penalty.

8. The question usually falls for decision is whether a clause in an agreement amounts to penalty capable of being enforced. The law in Section 74 of the Act has been vividly explained by a Constitution Bench of the Supreme Court in **Fateh Chand v. Balkishan Dass (AIR 1963 SC 1405)** in the following words:

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

The decision of the Apex Court in **Maula Bux v. Union of India (AIR 1970**

SC 1955) differentiates the terms “earnest money” and “advance amount paid towards purchase price”. The earnest money becomes a part of the purchase price when the transaction goes forward. It is forfeited when the transaction falls through by reason of fault or failure of the vendee. The forfeiture of earnest money under a contract for sale of property, either movable or immovable, if the amount stipulated is reasonable, does not fall within Section 74 of the Act. But, if forfeiture is of the nature of penalty, Section 74 of the Act applies.

9. No party has a contention in this case that ₹75,000/- paid as per Ext.A1 is earnest money. The terms of Ext.A1 make it clear that the said amount would be taken as part of purchase price, if the transaction proceeded as agreed to between the parties. The objectionable clause in Ext.A1 is that if on account of the breach committed by the purchasers (respondents) the transaction could not go forward, then the appellants in this case could forfeit the entire ₹75,000/- towards the loss sustained by them on account of the breach. On a reading of Ext.A1, it can be seen that this clause is only a penalty clause in *terrorem*. Unless the appellants establish damage sustained by them on account of the breach by the respondents, they cannot claim any compensation from the respondents.

10. Learned counsel for the respondents contended that the appellants failed to prove any loss or damage on account of the non-performance of contract. The case put forward by the appellants is that

they intended to sell the property to respondents for meeting their daughter's marriage expenses. Following dates are relevant for appreciating this contention. Ext.A1 agreement was executed on 15.12.1994. The time stipulated for performance of the contract as per Ext.A1 was six months. That is, on 14.06.1995 the time fixed in the contract had expired. The respondents have a case that the parties had agreed orally to extend the time, which is a fact disputed by the appellants. However, fact remains that the suit for return of advance money was filed almost at the end of three years from the date of execution of Ext.A1. Learned counsel for the appellants argued that this itself shows that the respondents were responsible for the breach of contract. Fact of the matter is that the suit was not barred by law of limitation. Learned counsel for the respondents argued that the date of marriage in the family of the appellants was 15.09.1996. It shows that it was more than one year and five months after the time stipulated for performance of the contract. Further, learned counsel contended that there is no challenge to the contention of the respondents that the appellants purchased another property in May, 1996. That will cut at the root of the case of the appellants that they suffered financial difficulties and loss on account of non-fulfillment of the obligations under Ext.A1 by the respondents. It has not been established that the appellants suffered any prejudice by non-performance of the contract and they did not take any step to enforce the

contract. Learned counsel for the respondents relied on a decision in **M/s.Kailash Nath Associates v. Delhi Development Authority and another (2015 (1) SCALE 230)** wherein the Supreme Court considered the scope of Sections 73 and 74 of the Act, interalia, other provisions and held as follows:

“On a conspectus of the above authorities, the law on compensation for breach of contract under Section 74 can be stated to be as follows:

1. Where a sum is named in a contract as a liquidated amount payable by way of damages, the party complaining of a breach can receive as reasonable compensation such liquidated amount only if it is a genuine pre-estimate of damages fixed by both parties and found to be such by the Court. In other cases, where a sum is named in a contract as a liquidated amount payable by way of damages, only reasonable compensation can be awarded not exceeding the amount so stated. Similarly, in cases where the amount fixed is in the nature of penalty, only reasonable compensation can be awarded not exceeding the penalty so stated. In both cases, the liquidated amount or penalty is the upper limit beyond which the Court cannot grant reasonable compensation.

2. *Reasonable compensation will be fixed on well known principles that are applicable to the law of contract, which are to be found inter alia in Section 73 of the Contract Act.*

3. *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.*

4. *The Section applies whether a person is a plaintiff or a defendant in a suit.*

5. *The sum spoken of may already be paid or be payable in future.*

6. *The expression “whether or not actual damage or loss is proved to have been caused thereby” means that where it is possible to prove actual damage or loss, such proof is not dispensed with. It is only in cases where damage or loss is difficult or impossible to prove that the liquidated amount named in the contract, if a genuine pre-estimate of damage or loss, can be awarded.*

7. *Section 74 will apply to cases of forfeiture or earnest money under a contract. Where, however, forfeiture takes place under the terms and conditions of a public auction before agreement is reached, Section 74 would have no application.”*

11. Applying the above legal aspects and also the principles laid down by the Constitution Bench in **Fateh Chand's** case (supra), I am of the view that the court below is justified in finding that the appellants are not

entitled to appropriate the advance amount paid by the respondents as per the terms in Ext.A1. Learned counsel's submission that the lower court should have directed to return the advance money without interest is also not acceptable for the reason that only 6% interest is allowed in favour of the respondents/plaintiffs. Considering the period elapsed from the date of the suit, I am of the view that no injustice has been worked out against the appellants. I find no reason to interfere with the judgment and decree in the appeal.

In the result, the appeal is dismissed. Considering the entire facts, there is no order as to costs.

All pending interlocutory applications will stand dismissed.

A. HARIPRASAD, JUDGE.

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A.Hariprasad, J.

S.A.No.207 of 2003

JUDGMENT

9th February, 2015