* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

\+ **CS(OS) No. 2049/2011**

% **18th August, 2015**

SHRI RANBIR SIGH & ANR. ..... Plaintiffs

Through: Mr. Rajan Khosla and Mr. Vivek Srivastava, Advocates

versus

SHRI BHUP SINGH & ORS. ..... Defendants

Through: Mr. V.P.Rana, Adv. for D-2 and 3.

CORAM:
HON'BLE MR. JUSTICE VALMIKI J.MEHTA

To be referred to the Reporter or not?

VALMIKI J. MEHTA, J (ORAL)

1. On 15.7.2015, the following Order was passed:-

> "1. This is a suit for recovery of money. Recovery of money which is sought is the amount paid under an Agreement to Sell dated 03.09.2008.
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> 2. It is the case of the plaintiff that defendant is guilty of breach of contract whereas it is the case of the defendant is that plaintiff is guilty of breach of contract.
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> 3. In law, even if a buyer is guilty of breach of contract and until and unless the seller proves it that he suffered loss on account of the breach of contract of Agreement to Sell and one of which case is if the value of the property declines only in such circumstances defendant can forfeit or appropriate the money paid by the plaintiff/buyer.

> 4. If the defendants suffer no loss the amount paid by the plaintiff/buyer cannot be forfeited. This is so held by the Constitution Bench judgment of the Supreme Court in **Fateh Chand v Balkishan Das, AIR 1963 SC 1405** and which judgment has been followed recently by the Supreme Court in the case of **Kailash Nath Associates v Delhi Development Authority, (2015) 4 SCC 136**.
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> 5. The suit was passed over on the request of the counsel for the defendant, and the main counsel for the defendant does not appear in spite of the pass over as he is stated to be busy in some other Court.
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> 6. Though this case is adjourned but it is made clear that no adjournment shall be granted on the next date of hearing. Counsel for the defendant also without prejudice to the rights of the defendant wants to contact the defendant if the amount which is to be paid to the plaintiff can be paid to the plaintiff with nominal rate of interest.
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> 7. List on 18th August, 2015, making it clear that no adjournment shall be granted to the defendants and defendant Nos.2 and 3 are bound to ensure representation on their behalf on the next date of hearing. ”

2. The aforesaid Order was passed because plaintiffs have filed this suit for recovery of Rs.24,02,360/- of which the principal amount is Rs.20,71,000/-.

3. The aforesaid order was passed that even assuming the plaintiffs/proposed buyers are guilty of breach of contract and have failed to go ahead with the agreement to sell by getting the sale deed executed in

favour of the plaintiffs, yet, in view of the two Supreme Court judgments stated in the Order dated 15.7.2015, the defendants/proposed sellers cannot forfeit the entire amount inasmuch as a seller is entitled to forfeit the amount paid as liquidated damages by virtue of Section 74 of the Indian Contract Act, 1872, the liquidated damages only as the upper limit of the amount which can be forfeited and that too after pleading and proving the loss and further that in case the amount forfeited is in the nature of penalty, forfeiture cannot be made.

4. The Constitution Bench of the Supreme Court in the judgment in the case of ***Fateh Chand Vs. Balkishan Dass, AIR 1963 SC 1405*** has held that mere breach of contract is not actionable but loss caused on account of breach of contract is actionable. This is also the language of Section 73 of the Indian Contract Act. Putting it differently, unless loss is caused, a seller who has received the amount under the agreement to sell is not entitled to forfeit the complete amount received. In a contract to sell an immovable property, only a nominal amount can be forfeited and if an amount higher than a nominal amount is sought to be forfeited, then in view of the fact that the nature of such a contract is such that loss can be proved (by difference in market value of the property on the date of breach as

compared to the agreed price) hence the issue of damages claimed by forfeiture of advance amount paid can only arise if loss is pleaded and proved by the seller who seeks to forfeit the advance amount paid by the buyer to the seller. The relevant paras in ***Fateh Chand*'s** case ***(supra)*** read as under:-

> **"8.** The claim made by the plaintiff to forfeit the amount of Rs 24,000 may be adjusted in the light of Section 74 of the Indian Contract Act, which in its material part provides:-
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> "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."
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> The section is clearly an attempt to eliminate the sometime 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: <u>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.</u> 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.
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> **10.** Section 74 of the Indian Contract Act deals with the measure of damages in two classes of cases (*i*) where the contract names a sum to be paid in case of breach and (*ii*) where the contract contains any other stipulation by way of penalty. We are in the present case not concerned to decide

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

15. Section 74 declares the law as to liability upon breach of contract where compensation is by agreement of the parties pre-determined, or where there is a stipulation by way of penalty. But the application of the enactment is not restricted to cases where the aggrieved party claims relief as a plaintiff. The section does not confer a special benefit upon any party; it merely declares the law that notwithstanding any term in the contract predetermining damages or providing for forfeiture of any property by way of penalty, the court will award to the party aggrieved only reasonable compensation not exceeding the amount named or penalty stipulated. The jurisdiction of the court is not determined by the accidental circumstance of the party in default being a plaintiff or a defendant in a suit. Use of the expression "to receive from the party who has broken the contract" does not predicate that the jurisdiction of the court to adjust amounts which have been paid by the party in default cannot be exercised in dealing with the claim of the party complaining of breach of contract. The court has to adjudge in every case reasonable compensation to which the plaintiff is entitled from the defendant on breach of the contract. Such compensation has to be ascertained having regard to the conditions existing on the date of the breach.

16. There is no evidence that any loss was suffered by the plaintiff in consequence of the default by the defendant, save as to the loss suffered by him by being kept out of possession of the property. There is no evidence that the property had depreciated in value since the date of the contract provided; nor was there evidence that any other special damage had resulted. The contact provided for forfeiture of Rs 25,000 consisting of Rs, 1039 paid as earnest money and Rs 24,000 paid as part of the purchase price. The defendant has conceded that the plaintiff was entitled to forfeit the amount of Rs 1000 which was paid as earnest money. We cannot however agree with the High Court that 13 percent of the price may be regarded as reasonable compensation in relation to the value of the contract as a whole, as that in our opinion is assessed on an arbitrary assumption. The plaintiff failed to prove the loss suffered by him in consequence of the breach of the contract committed by the defendant and we are unable to find any principle on which compensation equal to ten percent of the agreed price could be awarded to the plaintiff. The plaintiff has been allowed Rs 1000 which was the earnest money as part of the damages. Besides he had use of the remaining sum of Rs 24,000, and we can rightly presume that he must have been deriving advantage from that amount throughout this period. In the absence therefore of any proof of damage arising from the breach of the contract, we are of opinion that the amount of Rs 1000 (earnest money) which has been forfeited, and the advantage that the plaintiff must have derived from the possession of the remaining sum of Rs 24,000 during all this period would be sufficient compensation to him. It may be added that the plaintiff has separately claimed mesne profits for being kept out possession for which he has got a decree and therefore the fact that the plaintiff was out of possession cannot be taken, into account in determining damages for this purpose. The decree passed by the High Court awarding Rs.11,250 as damages to the plaintiff must therefore be set aside."

(underlining added)

5. The ratio in ***Fateh Chand's*** case ***(supra)*** has been reiterated recently by the Supreme Court in the judgment in the case of ***Kailash Nath Associates Vs. Delhi Development Authority, (2015) 4 SCC 136*** and the relevant paras of this judgment are paras 30 to 35, 40 and 43 to 43.1 to 43.7, and which paras read as under:-

> "**30.** We now come to the reasoning which involves Section 74 of the Contract Act. The Division Bench held:
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> > *"38.* The learned Single Judge has held that the property was ultimately auctioned in the year 1994 at a price which fetched DDA a handsome return of Rupees 11.78 crores and there being no damages suffered by DDA, it could not forfeit the earnest money.
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> > *39.* The said view runs in the teeth of the decision of the Supreme Court in *Shree Hanuman Cotton Mills Vs. Tata Aircraft Ltd.: AIR 1970 SC 1986* which holds that as against an amount tendered by way of security, amount tendered as earnest money could be forfeited as per terms of the contract.
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> > *40.* We may additionally observe that original time to pay the balance bid consideration, as per Ex. P-1 was May 18, 1982 and as extended by Ex. P-8 was October 28, 1982. That DDA could auction the plot in the year 1994 in the sum of Rupees 11.78 crores was immaterial and not relevant evidence for the reason damages with respect to the price of property have to be computed with reference to the date of the breach of the contract".
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> **31**. Section 74 as it originally stood read thus:
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> > "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, 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."

32. By an amendment made in 1899, the Section was amended to read:

> *"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.
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> *Explanation.*--A stipulation for increased interest from the date of default may be a stipulation by way of penalty.
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> *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 any condition of any such instrument, to pay the whole sum mentioned therein.
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> *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."

33. Section 74 occurs in Chapter 6 of the Indian Contract Act, 1872 which reads "Of the consequences of breach of contract". It is in fact sandwiched between Sections 73 and 75 which deal with compensation for loss or damage caused by breach of contract and compensation for damage which a party may sustain through non-fulfillment of a contract after such party rightfully rescinds such contract. **It is important to note that like Sections 73 and 75, compensation is payable for breach**

of contract Under Section 74 only where damage or loss is caused by such breach.

34. In *Fateh Chand Vs. Balkishan Dass (supra)*, this Court held:

> "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....."
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> * * *
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> Section 74 of the Indian Contract Act deals with the measure of damages in two classes of cases (i) where the contract names a sum to be paid in case of breach and (ii) where the contract contains any other stipulation by way of penalty. We are in the present case not concerned to decide whether a covenant of forfeiture of deposit for due performance of a contract falls within the first class. The measure of damages in the case of breach of a stipulation by way of penalty is by Section 74 reasonable compensation not exceeding the penalty stipulated for. In assessing damages the Court has, subject to the limit of the penalty stipulated, jurisdiction to award such compensation as it deems reasonable having regard to all the circumstances of the case. Jurisdiction of the Court to award compensation in case of breach of contract is unqualified except as to the maximum stipulated; but compensation has to be reasonable, and that imposes upon the Court duty to award compensation according to settled principles. The section undoubtedly says that the aggrieved

party is entitled to receive compensation from the party who has broken the contract, whether or not actual damage or loss is proved to have been caused by the breach. Thereby it merely dispenses with proof of "actual loss or damages"; it does not justify the award of compensation when in consequence of the breach no legal injury at all has resulted, because compensation for breach of contract can be awarded to make good loss or damage which naturally arose in the usual course of things, or which the parties knew when they made the contract, to be likely to result from the breach.

* * *

Section 74 declares the law as to liability upon breach of contract where compensation is by agreement of the parties pre-determined, or where there is a stipulation by way of penalty. But the application of the enactment is not restricted to cases where the aggrieved party claims relief as a Plaintiff. The section does not confer a special benefit upon any party; it merely declares the law that notwithstanding any term in the contract predetermining damages or providing for forfeiture of any property by way of penalty, the court will award to the party aggrieved only reasonable compensation not exceeding the amount named or penalty stipulated. The jurisdiction of the court is not determined by the accidental circumstance of the party in default being a Plaintiff or a Defendant in a suit. Use of the expression "to receive from the party who has broken the contract" does not predicate that the jurisdiction of the court to adjust amounts which have been paid by the party in default cannot be exercised in dealing with the claim of the party complaining of breach of contract. The court has to adjudge in every case reasonable compensation to which the Plaintiff is entitled from the Defendant on breach of the contract. Such compensation has to be ascertained having regard to the conditions existing on the date of the breach."

35. Similarly, in *Maula Bux v. Union of India (UOI): 1969 (2) SCC 554*, it was held:

"Forfeiture of earnest money under a contract for sale of property-movable or immovable-if the amount is reasonable, does not fall within Section 74. That has been decided in several cases: *Chiranjit Singh Vs. Har Swarup: 21 AIR 1926 PC 1; Roshan Lal Vs. Delhi Cloth and General Mills Co. Ltd.: 22 ILR (1911) 33 All 166; Mohd. Habibullah Vs. Mohd. Shafi: 23 ILR (1919) 41 All 324; Bishan Chand Vs. Radha Kishan Das: 24 ILR (1897) 19 All 489.* These cases are easily explained, for forfeiture of a reasonable amount paid as earnest money does not amount to imposing a penalty. But if forfeiture is of the nature of penalty, Section 74 applies. Where under the terms of the contract the party in breach has undertaken to pay a sum of money or to forfeit a sum of money which he has already paid to the party complaining of a breach of contract, the undertaking is of the nature of a penalty.

Counsel for the Union, however, urged that in the present case Rs. 10,000/- in respect of the potato contract and Rs. 8,500 in respect of the poultry contract were genuine pre-estimates of damages which the Union was likely to suffer as a result of breach of contract, and the Plaintiff was not entitled to any relief against forfeiture. Reliance in support of this contention was placed upon the expression (used in Section 74 of the Contract Act), "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". It is true that in every case of breach of contract the person aggrieved by the breach is not required to prove actual loss or damage suffered by him before he can claim a decree, and the Court is competent to award reasonable compensation in case of breach even if no actual damage is proved to have been suffered in consequence of the breach of contract. But the expression "whether or not actual damage or loss is proved to have been caused thereby" is intended to cover different classes of contracts which come before the Courts. In case of breach of some contracts it may be impossible for the Court to assess compensation arising from breach, while in other cases compensation can be calculated in accordance with established rules. Where the Court is unable to assess

> the compensation, the sum named by the parties if it be regarded as a genuine pre-estimate may be taken into consideration as the measure of reasonable compensation, but not if the sum named is in the nature of a penalty. Where loss in terms of money can be determined, the party claiming compensation must prove the loss suffered by him.
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> In the present case, it was possible for the Government of India to lead evidence to prove the rates at which potatoes, poultry, eggs and fish were purchased by them when the Plaintiff failed to deliver "regularly and fully" the quantities stipulated under the terms of the contracts and after the contracts were terminated. They could have proved the rates at which they had to be purchased and also the other incidental charges incurred by them in procuring the goods contracted for. But no such attempt was made."

40. From the above, it is clear that this Court held that *Maula Bux's* case *(supra)* was not, on facts, a case that related to earnest money. Consequently, the observation in *Maula Bux (supra)* that forfeiture of earnest money under a contract if reasonable does not fall within Section 74, and would fall within Section 74 only if earnest money is considered a penalty is not on a matter that directly arose for decision in that case. The law laid down by a Bench of 5 Judges in *Fateh Chand's* case *(supra)* is that all stipulations naming amounts to be paid in case of breach would be covered by Section 74. This is because Section 74 cuts across the rules of the English Common Law by enacting a uniform principle that would apply to all amounts to be paid in case of breach, whether they are in the nature of penalty or otherwise. It must not be forgotten that as has been stated above, forfeiture of earnest money on the facts in *Fateh Chand's* case *(supra)* was conceded. In the circumstances, it would therefore be correct to say that as earnest money is an amount to be paid in case of breach of contract and named in the contract as such, it would necessarily be covered by Section 74.

43. 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:

43.1. 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.

43.2. 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.

43.3. 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.

43.4. **The Section applies whether a person is a Plaintiff or a Defendant in a suit**.

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

43.6. 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.

43.7. Section 74 will apply to cases of forfeiture of 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."

(emphasis is mine)

6. In the present case, the written statement filed by the defendants/sellers does not contain any pleading that the defendants/sellers have suffered a loss on account of breach of contract by the plaintiffs/proposed buyers, and therefore, the advance amount paid of Rs.20,71,000/- cannot be sought to be forfeited on account of any loss caused because there is no pleading of loss. Once there is no pleading with respect to the loss, there does not arise any issue of any evidence being led on this aspect because there is no pleading that any loss has been caused to the defendants on account of breach of contract by the plaintiffs.

7. In view of the above, a substantial amount of Rs. 20,71,000/- cannot be forfeited by the defendants/sellers simply on the ground that there is such clause entitling forfeiture in the contract. There cannot be forfeiture once there is no pleading of any loss being caused to the defendants on account of breach of contract by the plaintiffs. In my opinion, the defendants at best be entitled to forfeit only a nominal amount of the advance amount paid and therefore I allow the defendants forfeiting the 10% of the amount paid of Rs.20,71,000/-. Therefore, the defendants are liable to pay to the plaintiffs a sum of Rs.18,63,900/- and a decree for this amount is passed in favour of the plaintiff. Since the defendants have enjoyed the

money of the plaintiffs, plaintiffs will also be entitled to interest at 6% per annum simple *pendente lite* and future till payment of this amount of Rs.18,63,900/-. I may note that the defendant no.1 had died during the pendency of the suit and counsel for the plaintiffs admits that since the legal heirs of defendant no.1 were not brought on record, the suit will stand abated as against the legal heirs of defendant no.1 and thus the decree will only be passed and executed against defendant nos. 2 and 3. Decree sheet be prepared accordingly.

AUGUST 18, 2015 **VALMIKI J. MEHTA, J.**
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