

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

+ **O.M.P. No.299/2003**

Date of decision : March 18, 2010

MAHANAGAR TELEPHONE NIGAM LTD. ... Petitioner.

Through: Mr. Vivek Malik, Advocate
VERSUS

HARYANA TELECOM LTDRespondent

Through: Mr. Narendra M.Sharma and Ms. Mithu
Jain, Advocates.

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

1. Whether the Reporters of local papers may be allowed to see the judgment?
2. To be referred to the Reporter or not? Yes
3. Whether the judgment should be reported in the Digest? Yes

% **JUDGMENT(ORAL)**

VALMIKI J. MEHTA, J

1. By this objection petition under Section 34 of the Arbitration and Conciliation Act, 1996, the petitioner challenges the Award of the Arbitration Tribunal dated 12.3.2003. The Award arrives at a finding holding the respondent guilty of delay in supply of the goods, yet, denies the benefit of the

clause of liquidated damages to the present petitioner on the ground that the petitioner was in law bound to prove loss, however, it failed to prove that any loss was caused to it. The Award therefore directs the petitioner to refund the amount of Rs.1,03,20,763/- appropriated by it towards liquidated damages. The basic stress in the Award is that the petitioner failed to prove that any loss has been caused to it, and therefore, it was consequentially held that the relevant sub-Clause 16.2, providing for liquidated damages was in the nature of penalty/in terrorem and that therefore the petitioner was not entitled to appropriate the amount towards liquidated damages.

2. The facts of the case are that the petitioner had floated a tender for supply of underground Jelly Filled Telephone Cables. The offer of the respondent herein was accepted and four purchase orders were placed upon the respondent as under:-

a.	20-80(527)/94-MM/HTL/94-95/56 dated 16.8.1994
b.	20-80(527)/94-MM/HTL/94-95/89 dated 21.9.1994
c.	20-80(527)/94-MM/HTL/94-95/91 dated 29.9.1994
d.	20-80(527)/94-MM/HTL/94-95/108 dated 18.10.1994

Against the above purchase orders, the respondent made supplies and raised bills. However, while making payments against the aforesaid bills, the petitioner deducted a total sum of Rs.1,03,20,763/- on account of liquidated damages pursuant to the first part of Clause 16.2 of the contract on account of delayed supplies. The relevant Clause 16 reads as under:-

“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 fail 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 the supply material 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.”

3. An amendment was entered into between the parties on 13.3.1995 and as per which amendment, an extension for supplies was granted **with** Liquidated Damages.

4. Two contentions were raised by the present petitioner in the arbitration proceedings to justify its claim of liquidated damages. Firstly, it was contended that by virtue of the first part of Clause 16.2, the petitioner was entitled, in view of the admitted delays in the supplies, to appropriate amount as liquidated damages. The second contention was that by virtue of the letter dated 6.5.1995, the respondent had clearly agreed to pay damages by saying “We are ready to accept the price and L/D as acceptable to MTNL”.

5. Though the Award runs into 77 paras, but in sum and substance the Arbitration Tribunal has held that Clause 16.2 is in the nature of a penalty clause and therefore, violative of Section 74 of the Contract Act, 1872. The Arbitration Tribunal held that the petitioner was bound to and yet did not adduce any proof of loss or damage sustained by it as a consequence of the delayed delivery of the material and therefore, it was held that compensation cannot be awarded to the petitioner although there was delayed supply.

6. The Arbitration Tribunal has further held that mere delay in supplies is unlikely to cause damages. It has also been further held that in view of the latter part of Clause 16.2, unless and until the delay hampers installing and commissioning of the system, only then in such a case there would be caused to the petitioner actual loss/damages. On the basis that there is no hampering in commissioning of the system, the Arbitration Tribunal has denied the entitlement of the petitioner to appropriate the amount towards liquidated damages. The Arbitration Tribunal has thus proceeded on the latter part of Clause 16.2 and not the earlier part which was relied upon by the petitioner. Paras 18, 20 and 36 of the Award are at this stage relevant and are reproduced as under:-

“18. The object of section 74 of the Contract Act is to confer jurisdiction on the court to award reasonable compensation. In the present case MTNL has not adduced any proof of loss or damage sustained by it as a consequence of delayed delivery of the material. The object of award of damages is to make good the loss or damage as a result of the breach of contract. Since there is no proof of legal injury or proof of actual damage or loss we will not be justified in awarding compensation to MTNL even though the claimant did not supply the contracted

goods on the stipulated dates of delivery. The supplier supplied the goods during the period of extension granted by MTNL while reserving the right to claim liquidated damages.

20. The claimant, it is true, had agreed to pay damages for the loss which MTNL may suffer as a consequence of delay in the delivery of the goods. But the claimant did not agree that it be punished with a penalty. If MTNL had proved actual loss or damages as a result of delay in delivery of the goods we would have certainly awarded reasonable compensation. Unfortunately, there is not an iota of evidence to prove loss or damage sustained by MTNL as a result of the delay in supplies.

36. Mere delay in supplies is unlikely to cause damage. This is the theory on which the clause is based. But if delay hampers commissioning of the system there is actual damage to MTNL. Our case is a case of mere delay. There was admittedly no hampering in the commissioning of any system. For mere delay without more it is at once unreasonable and unconscionable to award large sums of money as damages. It is so enormous that it is burdensome and obnoxious, though agreed to by the supplier. Here equity has played a role for centuries in giving relief against oppressive clauses. This kind of penalty has only a punitive purpose. This is not an award of liquidated damages for actual loss. Punitive damages which are intended to punish a party are generally not recoverable for breach of contract. The truth is there is no reasonable relationship between the harm and the award.”

(underlining is mine)

7. Before I proceed further in this case, it is necessary to refer to paragraphs 64 and 67 of the judgment of the Supreme Court in the case of **ONGC Vs. Saw Pipes, 2003 (5) SCC 705** which read as under:-

“64. It is apparent from the aforesaid reasoning recorded by the Arbitral Tribunal that it failed to consider Sections 73 and 74 of the Indian Contract Act and the ratio laid down in *Fateh Chand case*¹⁸ wherein it is specifically held that jurisdiction of the court to award compensation in case of breach of contract is unqualified except as to the maximum stipulated; and compensation has to be reasonable. Under Section 73, when a contract has been broken, the party who suffers by such breach is entitled to receive compensation for any loss caused to him which the parties knew when they made the contract to be likely to result from the breach of it. This section is to be read with Section 74, which deals with penalty stipulated in the contract, *inter alia* (relevant for the present case) provides that 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 breach

is entitled, whether or not actual 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. Section 74 emphasizes that in case of breach of contract, the party complaining of the breach is entitled to receive reasonable compensation whether or not actual loss is proved to have been caused by such breach. Therefore, the emphasis is on reasonable 741 compensation. If the compensation named in the contract is by way of penalty, consideration would be different and the party is only entitled to reasonable compensation for the loss suffered. But if the compensation named in the contract for such breach is genuine pre-estimate of loss which the parties knew when they made the contract to be likely to result from the breach of it, there is no question of proving such loss or such party is not required to lead evidence to prove actual loss suffered by him. Burden is on the other party to lead evidence for proving that no loss is likely to occur by such breach. Take for illustration: if the parties have agreed to purchase cotton bales and the same were only to be kept as a stock-in-trade. Such bales are not delivered on the due date and thereafter the bales are delivered beyond the stipulated time, hence there is breach of the contract. The question which would arise for consideration is — whether by such breach the party has suffered any loss. If the price of cotton bales fluctuated during that time, loss or gain could easily be proved. But if cotton bales are to be purchased for manufacturing yarn, consideration would be different.”

67. Take for illustration construction of a road or a bridge. If there is delay in completing the construction of road or bridge within the stipulated 742 time, then it would be difficult to prove how much loss is suffered by the society/State. Similarly, in the present case, delay took place in deployment of rigs and on that basis actual production of gas from platform B-121 had to be changed. It is undoubtedly true that the witness has stated that redeployment plan was made keeping in mind several constraints including shortage of casing pipes. The Arbitral Tribunal, therefore, took into consideration the aforesaid statement volunteered by the witness that shortage of casing pipes was only one of the several reasons and not the only reason which led to change in deployment of plan or redeployment of rigs Trident II platform B-121. In our view, in such a contract, it would be difficult to prove exact loss or damage which the parties suffer because of the breach thereof. In such a situation, if the parties have pre-estimated such loss after clear understanding, it would be totally unjustified to arrive at the conclusion that the party who has committed breach of the contract is not liable to pay compensation. It would be against the specific provisions of Sections 73 and 74 of the Indian Contract Act. There was nothing on record that compensation contemplated by the parties was in any way unreasonable. It has been specifically mentioned that it was an agreed genuine pre-estimate of damages duly agreed by the parties. It was also mentioned that the liquidated damages are not by way of penalty. It was also provided in the contract that such damages are to be recovered by the purchaser from the bills for payment of the cost of material submitted by the contractor. No evidence is led by the claimant to establish that the stipulated condition was by way of penalty or the compensation contemplated was, in any way, unreasonable. There was no reason for the Tribunal not to rely upon the clear and unambiguous terms of agreement stipulating pre-estimate damages because of delay in supply of goods. Further, while extending the

time for delivery of the goods, the respondent was informed that it would be required to pay stipulated damages”.

8. The aforesaid paragraphs show that in certain cases / contracts, it is not possible to prove the exact damage and loss which is caused to the aggrieved party. Consequently, if there is a provision for liquidated damages, such liquidated damages can be claimed by the aggrieved party from the person who has committed breach of the contract. The figure of liquidated damages however is only an upper limit of damages and the Arbitrators can award a lower reasonable sum instead of the stipulated amount of liquidated damages. It is however, very clear that it is not necessary that there should be proof of actual loss and even if, it is not proved that there is an actual loss, the **nature of the contract** can show that loss has been caused. In fact, onus of proof shifts on the guilty party to show that actual loss has not been caused. It is only when the person who is guilty of breach of contract establishes that no loss has been caused, only in such circumstances, aggrieved party is dis-entitled to appropriate any amount towards liquidated damages under a contractual clause.

In the present case the cables contracted for were for general supplies and not meant only for a specific exchange and a specific installation and commissioning. Petitioner MTNL is a commercial organisation and it would have earned revenue from its customers, both old and new, who would have been served by the laying of the contracted cables. In such cases since actual

loss of revenue from customers cannot exactly be proved on account of delay in supply of cables, that is why liquidated damages are provided for in the contract. The nature of the contract in this case was such that loss is very much a consequence of delay. Such loss thus need not be proved.

9. Mr. Narendra Sharma, learned counsel for the respondent very strenuously argued in favour of sustaining the Award on the following four grounds:-

(i) Firstly, it was necessary for the petitioner to prove the loss and since loss has not been proved to have been caused to the petitioner, the petitioner is not entitled to appropriate any amount towards liquidated damages.

(ii) The second argument was that the sub-Clause is in the nature of penalty and since the Clause is in the nature of penalty, the Clause is violative of Section 74 of the Contract Act and therefore the same dis-entitles the petitioner to claim liquidated damages therein.

(iii) The third argument as raised by the counsel for the respondent was that on referring to the contract, it is seen that the Clause in question does not use the expression “genuine pre-estimate of damages” and therefore it should be held that the Clause in question is not towards genuine pre-estimate of damages but is in fact in the nature of penalty and a clause in interrorem.

(iv) Lastly and fourthly, it was contended that the clause in question when read, is to be read in such a fashion that both the parts of the sub-Clause 16.2 are inter-related and that no damages for delayed supplies can be independently granted until and unless there is in fact delay also in installation and commissioning of the system.

The counsel for the respondent has relied upon the decisions of *Saw Pipes* (supra) and two decisions of two learned Single Judges of this Court in *Haryana Telecom Ltd. Vs. Union of India* 2006(3) R.A.J. 225 (Del) and *Indian Oil Corporation Vs. Lloyds Steel Industries Ltd.* 2007 (4) Arb. LR 84 (Delhi).

10. I am unable to agree with any of the contentions as raised by the counsel for the respondent. The first two contentions as raised by the counsel for the respondent are inter-related. As already stated by me by referring to the decision in *Saw Pipe's* case, in certain contracts it is not necessary to prove the loss. The nature of the contract in the present case was such that proof of loss was not necessary. In the facts of the present case, so far as the first part of sub-Clause 16.2 is concerned, the same is independent of the latter part of sub-Clause 16.2. The earlier part of sub-Clause 16.2 provides for levy of liquidated damages which is relatable to the delayed supplies. The petitioner has acted under this earlier part of sub-Clause 16.2 and not under the latter part of sub-Clause 16.2. A reference to Clause 16.2 shows that the latter part of the Clause

comes into operation only for **enhancing the claim** for liquidated damages if the supply of Jelly Filled Telephone Cables is relatable to delay in installation and commissioning of a system. I may note that it is not the stand of the respondent in the arbitration proceedings that the Jelly Filled Cables which were to be supplied by the respondent were meant only and only for one single system of the petitioner and which system was not delayed in installing and commissioning and therefore no loss or damage has been caused to the petitioner. On the contrary, the Jelly Filled Cables which were to be supplied by the respondent to the petitioner, and for which there is an admitted delay, is towards a general supply are not related to any specific exchange or a specific system of installation and commissioning. I may only note that sometimes in printed contracts, there are general clauses which cover myriad situations which necessarily do not apply to the facts of a particular case. This was one type of case where a general language of the latter part of Clause 16.2 did not apply to the facts of the present case. During the course of arguments I specifically put a query to the learned counsel for the respondent to show me how under the subject contract, cables were being supplied only for a specific and a particular installation and commissioning. The counsel for the respondent however has not been able to point out anything from the record that the Jelly Filled Telephone Cables were supplied for commissioning and installation of only one particular system only. Clearly the contracted supplies were thus general supplies relatable to the earlier part of sub-Clause 16.2 and not to the latter part which

relate to a specific installation and commissioning. In my opinion it is also not necessary to state in the contractual clause that the liquidated damages are a genuine pre-estimate of damages as urged by the counsel for the respondent. Once there is a Clause of liquidated damages it is presumed to be a genuine pre-estimate of loss/damages, and in fact, onus of proof is on the guilty party to show why the clause of liquidated damages is in the nature of penalty having no/ little co-relation or is highly disproportionate to the actual loss suffered. This however has not been so pleaded and proved by the respondent in the arbitration proceedings.

11. The reference made by counsel to the decision in *Haryana Telecom Ltd.* (supra) is not applicable to the facts of the present case because in the said case there is a finding of fact that on account of the breach and failure to supply the contracted cables, the aggrieved party/Union of India, in fact, purchased the Jelly Filled Cables at a lower rate than the rate of the contract of which breach was committed and hence U.O.I. was not caused any loss by the breach of the contract. Therefore, since no loss was admittedly caused, in the said fact situation, it was held by the Arbitrator, and which findings were upheld by the court, that the Clause of liquidated damages cannot be enforced. In the judgment of *Indian Oil Corporation Ltd* (supra), again, there is a finding of fact that because of committing of breach of contract by the guilty party, in fact no loss was suffered by the aggrieved party.

12. The scope of hearing before this court while hearing objections under Section 34 of the Arbitration and Conciliation Act, 1996, is no doubt circumscribed, however, it is also settled law that if the Award is wholly illegal, in that, it violates the applicable law of the land or the findings therein are so perverse that it shocks the judicial conscience then the courts do in fact interfere with such Awards. Additionally, a perverse interpretation of a contractual clause also entitles a court, and in fact which is duty bound in such situations, to interfere with the Award. It has been held in ***ONGC Vs. Garware Shipping Corporation Ltd., 2007 (13) SCC 434*** by the Supreme Court in paragraph 30 that there is no such provision that Courts have to be slow in interfering with an Award even if the conclusions are perverse and the very basis of the Award is wrong. In ***Security Printing & Minting Corporation of India Ltd. and Anr. Vs. Gandhi Industrial Corporation, 2007 (13) SCC 236*** in paragraph 16 it has been held by the Supreme Court that even though the courts are slow in interfering with the Award it does not mean that if the Award is perverse the Courts are powerless to interfere in the matter. In ***Numaligarh Refinery Vs. Daelim Industrial Co. Ltd, 2007 (8) SCC 446*** in paragraph 17 of the judgment the Supreme Court has said that where it has been found that the Arbitrator has acted without jurisdiction and has put an interpretation on a clause of the agreement which is wholly contrary to law then in that case it cannot be said that there is no provision for the courts to set the things right, even though the

Courts do not ordinarily substitute the interpretation for that of the Arbitrator and that the finding of the Arbitrator is normally accepted.

13. In my view therefore, the Award in question is liable to be set aside because the same proceeds on a wrong interpretation of Section 74 of the Contract Act and which interpretation flies in the face of the ratio of the decision of *Saw Pipe's* case thus making the Award illegal. The interpretation as put forth by the Arbitration Tribunal on sub-Clause 16.2, is in fact clearly a perverse interpretation because it links the fact situation arising in the present case to the latter part of sub-Clause 16.2 and which does not arise in the facts of the present case where the earlier part of sub-Clause 16.2 applies. The Arbitration Tribunal was in fact duty bound to only consider and apply the earlier part of sub-Clause 16.1. The Award is therefore clearly perverse and is thus set aside.

14. With the aforesaid observations, the objection petition is allowed and the impugned Award dated 12.3.2003 is set aside. The petition is disposed of as allowed, leaving the parties to bear their own costs.

VALMIKI J.MEHTA, J

March 18, 2010
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