

\$-26

\*

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

*Date of decision: 09.10.2018*

+ OMP (COMM.) 429/2018

UNION OF INDIA THROUGH: ITS SECRETARY

..... Petitioner

Through: Mr.Dinesh Agnani, Sr. Adv. with  
Mr.L.B.Rai, Mr.Mohit Kumar Sharma,  
Ms.Disha Singh, Advs.

versus

INTERCITY CABLES PVT. LIMITED ..... Respondent

Through: Mr.Sachin Datta, Sr. Adv. with  
Ms.Kanika Sinha, Mr.Tanmaya Sinha,  
Advs.

**CORAM:**

**HON'BLE MR. JUSTICE NAVIN CHAWLA**

**NAVIN CHAWLA, J. (Oral)**

**IA 13972/2018**

Exemption allowed subject to all just exceptions.

**OMP (COMM) 429/2018 & IA 13971/2018**

1. This petition under Section 34 of the Arbitration and Conciliation Act, 1996(hereinafter referred to as the 'Act') has been filed by the petitioner challenging the Arbitral Award dated 25.07.2018 passed by the Sole Arbitrator adjudicating the disputes that have arisen between the parties in relation to the Advance Purchase Order dated 25.09.1995 and the

subsequent Purchase Order dated 23.02.1996 for supply of Optical Fibre Line Terminating Equipment (PDH) placed by the petitioner on the respondent.

2. The Arbitrator by the Impugned Award has found that the respondent had failed to make the supplies in terms of the Purchase Order. The Arbitrator further held that the excuse of the respondent that it was not able to make the supplies for lack of response from the petitioner to its proposal for entering into a collaboration with another company was unjustified. Therefore, the respondent was found to be in breach of the Agreement, that is, the Advance Purchase Order and the consequent Purchase Order placed by the petitioner on the respondent.

3. At the same time and in spite of this finding, the Sole Arbitrator had held that as the petitioner was unable to prove any loss suffered by it due to this breach of the Agreement, it was not entitled to retain the proceeds of the Performance Bank Guarantee encashed by it and has ordered a refund of the said proceeds alongwith interest @9% per annum with effect from the date of encashment of the Bank Guarantee till realization. The Arbitrator has also awarded costs assessed at Rs.3 lacs in favour of the respondent.

4. The learned senior counsel for the petitioner relying upon clause 15.2 of the General (Commercial) Conditions of Contract submits that incase of a delay by the supplier in the performance of its delivery obligations, the petitioner was

entitled to *inter alia* forfeit the performance security. As the Arbitrator has found the respondent to be in breach of its performance obligations, the Performance Bank Guarantee was rightly encashed and forfeited by the petitioner. In such circumstances, the petitioner was not required to prove any loss being suffered by it due to such breach of the contract by the respondent.

5. I am unable to agree with the said submission of the learned senior counsel for the petitioner. In the present case, a few terms of the contract would be relevant to answer the said submission. Clause 4 of the General (Commercial) Conditions of Contract reads as under:-

4. *PERFORMANCE SECURITY:*

4.1 *The supplier shall furnish performance security to the purchaser for an amount equal to 5% of the value of each purchase order upto Rs.4 Crores and 2% for every additional one crore of purchase order limited to maximum to one crore based on the quantity proposed to be procured against the purchase order.*

4.2 *The proceeds of the performance security shall be payable to the Purchaser as compensation for any loss resulting from the Supplier's failure to complete its obligations under the Contract.*

4.3 *The Performance Security Bond shall be in the form of a bank guarantee issued by a Scheduled Bank and in the form provided in the Bid Document, Section IX.*

4.4 *The performance security Bond will be discharged by the Purchaser after completion of the Supplier's performance obligations, including any Warranty obligations, under the Contract."*

*(Emphasis Supplied)*

6. A reading of clause 4.2 would clearly show that the proceeds of the performance security are to be adjusted against any loss resulting from the supplier's failure to complete its obligations under the contract. The same is also evident from the terms of the Performance Bank Guarantee itself, which is quoted hereinunder:

*“We State Bank of India do hereby undertake to pay the amounts due and payable under this guarantee without any demur, merely on a demand from the Government stating that the amount claimed is due by way of loss or damage caused to or would be caused to or suffered by the Government by reason of breach by the said contractor(s) of any of the terms or conditions contained in the said Agreement or by reason of the contractor(s) failure to perform the said Agreement. Any such demand made on the bank shall be conclusive as regards the amount due and payable by the Bank under this guarantee where the decision of the Government in these counts shall be final and binding on the Bank. However, our liability under this guarantee shall be restricted to an amount not exceeding Rs.34,58,000/- (Rupees Thirty Four Lakhs Fifty Eight thousand only).”*  
(Emphasis Supplied)

7. Clause 15.2 of the General (Commercial) Conditions of Contract is reproduced hereinunder:

*“15.2 Delay by the Supplier in the performance of its delivery obligations shall render the Supplier liable to any or all of the following sanctions: forfeiture of its performance security, imposition of liquidated damages and/or termination of the contract for default.”*

8. Though clause 15.2 speaks about forfeiture of the performance security, as held by the Supreme Court in ***Kailash Nath Associates vs. Delhi Development Authority & Anr.*** (2015) 4 SCC 136, such forfeiture has to be in terms of Section 74 of the Contract Act. In ***Kailash Nath*** (supra), the Supreme Court considering the earlier judgments of the Supreme Court on Sections 73 and 74 of the Contract Act has held as under:

*“40. From the above, it is clear that this Court held that Maula Bux case was not, on facts, a case that related to earnest money. Consequently, the observation in Maula Bux 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 five Judges in Fateh Chand case 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 case 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.*

*41. It must, however, be pointed out that in cases where a public auction is held, forfeiture of earnest money may take place even before an agreement is reached, as DDA is to accept the bid only after the earnest money is paid. In the present case, under the terms and conditions of auction, the highest bid (along with which earnest money has to be paid) may well have been rejected. In such cases, Section 74 may not*

*be attracted on its plain language because it applies only “when a contract has been broken”.*

*42. In the present case, forfeiture of earnest money took place long after an agreement had been reached. It is obvious that the amount sought to be forfeited on the facts of the present case is sought to be forfeited without any loss being shown. In fact it has been shown that far from suffering any loss, DDA has received a much higher amount on re-auction of the same plot of land.*

*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:*

*xxxxxx*

*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.”*

9. The learned Sole Arbitrator has also considered the above clauses of the Agreement and the Bank Guarantee and

has held as under:

*“Is Clause 4 of the General (Commercial) Conditions of Contract, as reproduced above, not a pre-determined and mutually agreed estimate of compensation? I think it is. It does determine 5% of the contract value as performance security and the parties did mutually agree that the proceeds of the performance security shall be payable to the purchases “as compensation for any loss resulting from the Supplier’s failure to complete its obligations under the contract”.*

**XXXX**

*“As would be borne out from above the intention of the parties is to be essentially gathered from the words used in the contract. If that be so, and it being so, it is significant to note that Clause 4(2) in our case is significantly different from Clauses 11 and 12 in Saw Pipes case. In Clause 4 (2) the proceeds of the performance security were payable to the Respondent as compensation only for any loss resulting from the Supplier's failure to complete its obligations under the contract". In Saw Pipe's case there was no such condition. Rather, in that case the liquidated damages of 1% of the contract price was agreed as "genuine pre-estimate of damages duly agreed by the parties" leaving no requirement of proving loss. In the matter before me the intention of the parties is clear and unambiguous and it is that compensation had to be necessarily "for any loss resulting from Supplier's failure to complete its obligations under the contract". True, the Claimant failed and that too without any justification to complete its obligations. But then, that in itself is not sufficient. The Respondent has to show that what has been recovered was on account of loss suffered by the Respondent and that too on account of Claimant's failure to honour its contractual obligation in terms of Clause 4. I say so because that is clear from the*

*language used in Clause 4 which is clearly distinguishable from the contractual Clauses 11 and 12 before the Supreme Court in Saw Pipe's case.*

*In the case of Maula Bux v. Union of India (1970) 1 SCR 928, it was clearly pointed out that "where loss in terms of money can be determined, the party claiming compensation must prove the loss suffered by him". In the matter before me, and I am saying it at the risk of repetition, Clause 4 (2) clearly stipulates that compensation could be recovered only "for any loss resulting from the Supplier's failure to complete its obligations under the contract" and thus clearly laying down that the parties were in agreement that "loss" could be determined. In any case, it is not the case of the Respondent nor was it even obliquely suggested that the "loss" resulting from the Claimant's failure to perform its part of the contract was not capable of being determined and if that be so, and it being so, the Respondent was required to prove actual loss. The Respondent has failed to prove the same."*

**XXXXX**

*"However, in both the letters there was no reference to the Respondent having suffered any loss or there being any likelihood of any loss in future. Thus neither on October 3, 1996 when it was decided to cancel the contract and to get the performance bank guarantee encashed nor at an earlier stage was it the case of the Respondent that it had suffered loss or was likely to suffer loss in the future. Ofcourse the Respondent, and as already noted above, has come up with counter claims but they were not even in existence when the performance guarantee was encashed and are admittedly barred by limitation. They also cannot be looked into as reference to me to act as an Arbitrator is confined only to the "disputes raised in the petition". The fact, thus, remains that at the time when the*



*contract was cancelled and performance bank guarantee was encashed it was not the case of the Respondent that it was getting the bank guarantee encashed as "compensation for any loss resulting from the Supplier's failure to complete its obligations under the contract". This being the position, I do feel that though there was lapse on the part of the Claimant in as much as it did not perform its part of the contract the performance bank guarantee which was only "compensation" for "any loss that the Respondent suffered", could not been encashed solely on account of Claimant's failure to complete its obligations under the contract. There was no such loss. In any case, the Performance Guarantee was not encashed on that ground. And this being the position the invocation of the Bank Guarantee was not in terms of the Bank guarantee nor in terms of Clause 4.2 as referred to above. Reference in this connection may be made to M/s Ansal Properties & Industries Ltd. versus Union of India and Others 1994 (29) DRJ page-66 and so also to Puri International (P) Ltd. versus National Building Construction Company Ltd. 1997 (41) DRJ page-592. Not only this. I feel that encashment of performance guarantee or the whole amount was also bad for the reason that ultimately the Purchase Order turned out to be not for a sum of Rs. 1128.66 lacs but only for a sum of Rs. 75964126 reducing the requirement of performance guarantee from Rs. 34,58,000/- to Rs.27,20,000/-. I say so also for the reason that the A.P.O. was not the Purchase Order."*

10. Interpretation of the contract by the Arbitrator and a finding based on appreciation of evidence led by the parties before the Sole Arbitrator, cannot be interfered with by this Court in exercise of its powers under Section 34 of the Act unless the same is found to be perverse or one which no

reasonable person could have reached. In this case, as discussed above, the finding of the Arbitrator cannot be faulted.

11. In view of the above, I find no merit in the present petition and the same is accordingly dismissed, with no order as to costs.

**NAVIN CHAWLA, J**

**OCTOBER 09, 2018**  
**RN**