IN THE HIGH COURT OF JUDICATURE AT MADRAS

(ORDINARY ORIGINAL CIVIL JURISDICTION)

MONDAY, THE 06th DAY OF DECEMBER 2021

THE HON'BLE MR. JUSTICE SENTHILKUMAR RAMAMOORTHY

O.P. No.185 of 2015
and
A.Nos.2120 to 2123 of 2015

In the matter of Arbitration and Conciliation Act 1996
and
In the matter of Arbitration Award dated 03.03.2014 between M/s. Concrete Products & Construction Company and Union of India, owning Southern Railway Rep.by Principal Chief Engineer

M/s. Concrete Products & Construction Company,
Rep.by its Joint Managing Partner,
No.398, Poonamallee High Road,
Kilpauk, Chennai 600 010 ...Petitioner/Applicant (in all applications)

-vs

1.Union of India,
Owning Southern Railway
Represented by the Principal Chief Engineer,
Headquarters Office,
Works Branch, Chennai 600 003

2.Mr.R.K.Dash,
Chief Materials Manager/SGT,
East Coast Railway,
Rail Sadan, Chandrasekharpur,
Bhubaneswar,
Odissa 751017 ...Defendants/Respondents (in all applications)

O.P. No.185 of 2015

Original Petition praying that this Hon'ble Court be pleased to set aside the Arbitration Award dated 03.03.2014 passed by the second Respondent in the dispute between the Petitioner and the first Respondent.

A.No.2120 of 2015:

Application praying that this Hon'ble Court be pleased to direct the 1st Respondent to release interest of Rs.2,03,76,936/- on Rs.4,34,04,566/- and interest of Rs.6,74,670/- on Rs.15,81. 989/- computed in accordance with the provisions of Sections 15, 16 and 17 of the Micro, Small and medium Enterprises Development Act 2006.

A.No.2121 of 2015:

Application praying that this Hon'ble Court be pleased to direct the return of security deposit of Rs.20,00,000/- made by the petitioner with interest thereon at 18% per annum from the date of remittance till payment.

A.No.2122 of 2015:

Application praying that this Hon'ble Court be pleased to direct the refund of Rs.24,03,208- recovered as Liquidated Damages from the petitioner.

A.No.2123 of 2015:

Application praying that this Hon'ble Court be pleased to direct to refund

of a sum of Rs.16,84,809/- towards excess land lease collected by the

Railway Administration from the Petitioner.

This Original Petition along with these applications coming on this day before this court for hearing in the presence of Mr.Abishek Jenasenan for Mr.A.Jenasenan, Advocates for the petitioner in O.P.No.185 of 2015 and for the applicant in A.Nos.2120 to 2123 of 2015 and Mr.C.V.Ramachandramurthy, Advocate for the respondent in O.P.No.185 of 2015 and A.Nos.2120 to 2123 of 2015 and upon reading the petition and the award dated 03.03.2014 filed herein and the order herein dated 28.08.2018, and it is made clear that nothing in this order should be construed as a finding that the Petitioner is entitled to interest as per the MSMED Act,

it is ordered as follows:-

That the Arbitration Award dated 03.03.2014 passed by the second respondent herein, be and is hereby set aside the Award as regards the refusal to grant interest as per the MSMED Act and regards the grant of liquidated damages and forfeiture of security deposit.

2. That the Petitioner herein shall be at liberty to institute *de novo* arbitral proceedings in such regard in accordance with the relevant contract.

3. That if such proceedings are instituted, the Petitioner herein shall be entitled to the benefit of Section 43(4) of the Arbitration and Conciliation Act, 1996.

4. That the A.Nos.2120 to 2123 of 2015 do stand closed.

WITNESS THE HON'BLE MR.JUSTICE MUNISHWAR NATH BHANDARI ACTING CHIEF JUSTICE, HIGH COURT AT MADRAS AFORESAID, THIS THE 06th DAY OF DECEMBER 2021.

Sd./-
ASSISTANT REGISTRAR (O.S-II)

//Certified to be true copy//
Dated at Madras this the day of 2022.

COURT OFFICER(O.S.)

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KY

29.12.2021

O.P. No.185 of 2015

ORDER

DATED : 06.12.2021

THE HON'BLE MR. JUSTICE
SENTHILKUMAR RAMAMOORTHY

FOR APPROVAL: 4.1.2022

APPROVED ON: 05.01.2022

IN THE HIGH COURT OF JUDICATURE AT MADRAS

D A T E D : 06.12.2021

C O R A M **:**

The Hon'ble Mr. Justice **SENTHILKUMAR RAMAMOORTHY**

O.P.No.185 of 2015
and
Application Nos.2120 to 2123 of 2015

M/s.Concrete Products & Construction Company
Rep. by its Joint Managing Partner
No.398, Poonamallee High Road,
Kilpauk, Chennai – 600 010. ... Petitioner

Vs

1.Union of India
Owning Southern Railway,
Rep. by the Principal Chief Engineer,
Headquarters Office,
Works Branch, Chennai – 600 003.

2.Mr.R.K.Dash
Chief Materials Manager/SGT,
East Coast Railway,
Rail Sadan, Chandrasekharpur,
Bhubaneswar,
Odissa – 751017. ... Respondents

PRAYER : This Petition has been filed under Section 34 of the Arbitration and Conciliation Act 1996 praying to set aside the Arbitration Award dated 03.03.2014 passed by the second Respondent in the dispute between the Petitioner and the first Respondent.

For Petitioner : Mr.Abishek Jenasenan
for Mr.A.Jenasenan

For Respondents : Mr.C.V.Ramachandramurthy

ORDER

The claimant before the Arbitral Tribunal is the Petitioner herein. An Arbitral Award dated 03.03.2014 (the Award) is assailed.

2. An agreement was entered into between the Respondents and the Petitioner for supply of 2,94,400 numbers of pre-stressed mono block concrete sleepers (PSC Sleepers) at a price of Rs.1194/- per unit exclusive of taxes and with price variation. The original delivery period was two years and 37 days, i.e. from 19.11.2009 to 25.12.2011 with a permissible variation of + or – six months as regards time and + or – 30% as regards quantity. According to the Petitioner, as regards the Ambattur Concrete Sleepers Plant (the ABU Plant), the original monthly target was fixed at 10,000 numbers. Such monthly target was reduced from time to time. For instance, the Petitioner asserts that the monthly target was reduced to 3000 numbers by communication dated 26.07.2011 from the Respondents and to nil by communication dated 10.11.2011. Consequently, it is contended that it was not possible to meet the over all delivery schedule. In such

circumstances, a request was made to the Respondents to consent to the assignment of the contract to a sister concern of the Petitioner. Such request was declined. The Respondents, however, by communication of 03.02.2012, agreed to reduce the total quantity by 30%. Eventually, by communication dated 02.11.2012, the Respondents terminated the contract with effect from 20.10.2012 and proceeded to initiate action for the forfeiture of the security deposit and for the imposition of liquidated damages at 5% on the value of unsupplied and undelivered sleepers. The Petitioner herein initiated arbitral proceedings in the above facts and circumstances.

3. The Petitioner claimed a sum of Rs.4,49,90,340/- along with interest thereon amounting to Rs.55,61,514/- up to 31.01.2013 by relying upon Sections 15 to 17 of the Micro, Small and Medium Enterprises Development Act, 2006(the MSMED Act). In addition, the following relief was prayed for: a declaration that the termination of the contract is void; for refund of the security deposit of Rs.20,00,000/- with interest thereon at 18% per annum; a perpetual injunction restraining the Respondents from recovering liquidated damages of Rs.71,42,445/- ; and refund of a sum of Rs.16,84,809/- towards excess land licence fee collected by the Respondents from the Petitioner.

4. The Respondents herein filed a counter along with a counter

claim. By way of such counter claim, forfeiture of the security deposit of Rs.20,00,000/-; recovery of liquidated damages of Rs.68,16,977/-; and arbitration costs were prayed for. By the Award, the Arbitral Tribunal directed the Respondents to make the payment of Rs.4,49,90,340/- within a period of 30 days. In the event of default, simple interest at 7% per annum was directed to be paid. As regards termination, the Arbitral Tribunal concluded that termination may be done only for the unsupplied quantity. The forfeiture of the security deposit was upheld. As regards the claim for liquidated damages, the Arbitral Tribunal concluded that liquidated damages could be levied for delayed supply of supplied quantities, but not for unsupplied quantities.

5. The Petitioner assails the Award only insofar as it pertains to the refusal to award interest as per the MSMED Act, the award of liquidated damages as regards delayed supply of supplied quantities and the forfeiture of the security deposit.

6. The refusal to grant interest at the rates specified in the MSMED Act is assailed on the ground that the MSMED Act confers rights on any enterprise which is registered under the said enactment to claim interest at the rates specified therein if payments are not made within 45

days as specified therein. By drawing reference to Section 16 of the

MSMED Act, the Petitioner contends that the said provision opens with a non-obstante clause and overrides contractual stipulations to the contrary. By adverting to internal pages 10 and 11 of the Award, the Petitioner contends that the sole reason assigned by the Arbitral Tribunal for rejecting the claim for interest is that the relevant contract does not draw reference to Sections 15 to 17 of the MSMED Act. According to the Petitioner, the said conclusion is patently illegal. In addition, the Petitioner contends that such conclusion is contrary to public policy inasmuch as the MSMED Act was enacted to confer special benefits on MSMEs.

7. As regards the award of liquidated damages, the Petitioner contends that the counter claim of the Respondents was for recovery of liquidated damages at 5% of the unsupplied quantity. Such claim was made for a sum of Rs.68,16,977/-. The Arbitral Tribunal, at internal page 87, rejected the claim for liquidated damages with regard to unsupplied quantities by concluding that it would amount to a double penalty in view of the termination of the contract. However, the Petitioner contends that the Arbitral Tribunal committed a grave error in awarding liquidated damages for the alleged belated supply of 25,945 numbers of PSC Sleepers. With regard to the forfeiture of the security deposit, the Petitioner reiterates that the Respondents did not plead or establish loss. The Petitioner also

contends that the principles pertaining to liquidated damages would apply equally to the forfeiture of the security deposit. Therefore, the Petitioner contends that the Award as regards forfeiture of security deposit is unsustainable.

8. On this issue, the Petitioner relies upon the judgment of the Hon'ble Supreme Court in *Kailash Nath Associates v. DDA (2015) 4 SCC 136* ***(Kailash Nath)*** to the effect that even with regard to a claim for liquidated damages, it is necessary to establish the factum of loss and prove loss unless such loss is established to be impossible or difficult to prove. In the case at hand, the Petitioner contends that the Respondents did not plead that the loss was impossible or even difficult to prove. Indeed, it is submitted that even the factum of loss was not pleaded by the Respondents.

9. These contentions are refuted by the Respondents. By referring to the written submissions, the Respondents contend that the bills raised by the Petitioner could not be processed and paid on account of the non-execution of a rider agreement to extend the terms of the agreement. The next contention of the Respondents is that payment of interest is not permissible in terms of IRS condition 2401. By relying upon IRS condition 2401, it is contended that the Respondents are entitled to and exercised a

lien over such amounts on account of the breach of contract by the

Petitioner and the amounts payable on such account to the Respondents.

10. With regard to the reliance on the MSMED Act, the Respondents referred to earlier orders of this Court. By relying upon the order in *Union of India v. M/s.Nellai Concrete Products, O.P.No.1022 of 2017*, it is contended that the MSMED Act and the provisions relating to interest as specified therein would apply only to a reference made before the Facilitation Council constituted under the said Act. In addition, the order of a learned Judge in O.P.Nos.143 and 525 of 2016, which was affirmed in appeal by the Division Bench, is also relied upon.

11. By way of a short rejoinder, the Petitioner contends that the delay in supply is irrelevant at this juncture. As regards the non-execution of a rider agreement, the Petitioner points out that the Arbitral Tribunal considered the said contention and rejected the same on the ground that payment cannot be denied for non-execution of a rider agreement. As regards the judgments cited by the Respondents, the Petitioner contends that the judgment in O.P.Nos.143 and 525 of 2016 pertained to a security deposit and to the 75% pre-deposit requirement under the MSMED Act. Therefore, the said judgment has no bearing on the question of payment of interest for supply of goods or services.

12. In view of the Petitioner confining the challenge to three

aspects of the Award, only the said aspects need to be discussed herein. With regard to the payment of interest on unpaid invoices, the factual position, as on date, is that the Respondents have paid the Petitioner a sum of Rs.4,10,01,358/- on 31.07.2014 and a further sum of Rs.13,64,979/- on 04.08.2014. While making such payments, the Respondents levied and recovered a sum of Rs.24,03,208/- towards liquidated damages in terms of the Award. Thus, any interest claim would be from the date the relevant invoices became due until the above dates of payment thereof. This issue should be examined by bearing in mind the above factual context. The Arbitral Tribunal considered the question of payment of interest and rejected the claim on two grounds. First, at internal page 10 of the Award, the Arbitral Tribunal extracted IRS 2401. IRS 2401 is as under:

> "IRS 2401 states that "Whenever any claim or claims for payment of a sum of money arises out of or under the contract against the Contractor, the purchaser shall be entitled to withhold and also have a lien to retain such sum or sums in whole or in part from the security, if any, deposited by the Contractor and for the purpose aforesaid, the purchaser shall be entitled to withhold the said cash security deposit or the security, if any, furnished as the case may be and also have a lien over the same pending finalisation or adjudication of any such claim. In the event of the security being

insufficient to cover the claimed amount or amounts or if no security has been taken from the Contractor, the purchaser shall be entitled to withhold and have lien to retain to the extent of the such claimed amount or amounts referred to supra, from any sum of sums found payable or which at any time thereafter may become payable to the Contractor under the same contract or any other contract with the Purchaser or the Government pending finalisation or adjudication of any such claim.

It is an agreed term of the contract that the sum of money or moneys so withheld or retained under the lien referred to above, by the Purchaser will be kept withheld or retained as such by the Purchaser till the claim arising out of or under the contract is determined by the Arbitrator(if the contract is governed by the arbitration clause) or by the competent court as prescribed under clause 2703 hereinafter provided, as the case may be, and that **contractor will have no claim for interest or damages whatsoever on any account in respect of such withholding or retention under the lien referred to supra and duly notified as such to the Contractor**." (emphasis added).

13. On perusal of IRS 2401, it is evident that a lien may be exercised provided the exercise of lien is duly notified to the contractor. From the documentary evidence placed before the Arbitral Tribunal, it

appears that no such notification was made by the Respondents to the Petitioner. This aspect was not discussed by the Arbitral Tribunal. Secondly, the Arbitral Tribunal noticed that the relevant contract does not refer to the MSMED Act, and, on such basis, a conclusion was drawn that the MSMED Act is not applicable to the contract. Given the fact that the MSMED Act is a statute, it is not necessary for such statute to be incorporated by reference into the contract between the parties. While there could be other reasons for not applying the MSMED Act to the present dispute, the Arbitral Award does not discuss anything other than the non-citing of the provisions of the MSMED Act in the relevant contract. Therefore, the conclusion on this aspect is not sustainable and is liable to be interfered with. A claim for interest is grounded in facts inasmuch as the said claim would run from the date the relevant amount became payable and extend up to the date when payment was made. Therefore, if a claim for interest is to be made by the Petitioner herein, such claim would have to be made in *de novo* proceedings for such purpose.

14. Turning to the question of the grant of liquidated damages, a claim for damages involves four elements: a breach of contract; the occurrence of loss; the causal link between the breach and such loss; and

proof of the quantum of loss. In the context of liquidated damages, a minor qualification is made with regard to proof of quantum of loss. Starting with the judgment in *Maula Bux v. Union of India, (1969) 2 SCC 554* and, thereafter, in the more recent judgment in ***Kailash Nath***, the Hon'ble Supreme Court concluded that the person claiming liquidated damages should discharge the burden of either proving actual loss or establishing that such loss is impossible or difficult to prove given the nature of the contract. After considering the line of judgments on this issue, in *3i Infotech Limited v. Tamil Nadu e-Government Agency and another* 2020 (4) CTC 673, I had formulated the applicable principles in this regard in paragraph 23, which reads as under:

> " 23.The following principles emerge upon consideration of the judgments on liquidated damages and penalty and from the foregoing analysis:
>
> (i) Section 74 of the Contract Act provides for two categories of stipulated payments for breach: (a) a sum named in the contract as the amount to be paid in case of breach, which could be called stipulated compensation; and (b) stipulations by way of penalty.
>
> (ii) The principal difference between English law and Indian law, in this regard, is that a stipulation by way of penalty is unenforceable under English law whereas it is enforceable under Indian law.
>
> (iii) In both categories of stipulated payments under section 74, the sum stipulated operates as the maximum amount

or ceiling. In this respect also, the two categories are similar.

(iv) The term or label used, namely, liquidated damages, penalty or even price reduction, in the relevant clause, is not conclusive or determinative. However, it cannot be disregarded and the person contending that the label or term used is not the correct term would be required to discharge the burden of establishing the said assertion.

(v) The primary test for identifying and distinguishing between liquidated damages and penalty clauses is whether, when tested as of contract formation, the stipulated sum bears a reasonable correlation to anticipated loss; if so, it would be construed as a liquidated damages clause and, if not, as a penalty clause. A stipulated sum that bears such reasonable correlation to anticipated loss is considered as a genuine pre-estimate of loss.

(vi) As regards enforcement, the two categories are treated differently. In case the court concludes that the stipulated payment is a genuine pre-estimate of anticipated loss in case of breach, the sum stipulated would be ordered to be paid if the court also concludes that it is difficult or impossible to prove loss in the facts and circumstances. Such pre-estimate is to be made at the time of contract formation although evidence thereof may be adduced when there is a dispute.

(vii) Even if the court concludes that the stipulated compensation is a genuine pre-estimate of loss, the party claiming such compensation is required to prove that loss was incurred as a consequence of breach and what is dispensed with is the obligation to prove the loss accurately by also proving quantum of loss as per the claim. To put it differently, even in such a situation, a claim cannot be sustained in an injuria sine damnum scenario.

(viii) If it is not difficult or impossible to prove loss, the person claiming liquidated damages is required to prove loss, including the quantum of loss, even if the sum stipulated is a genuine pre-estimate and, therefore, qualifies as a claim for liquidated damages. In contrast with the contract formation stage evidence with regard to genuine pre-estimate, needless to say, actual loss would be required to be proved with reference to the breach and the direct consequences flowing therefrom.

(ix) Given the fact that a party claiming liquidated damages cannot claim more than the stipulated sum, once such party establishes that the stipulated compensation is a genuine pre-estimate, a high standard of proof would not be insisted upon to prove difficulty or impossibility of proving loss. In other words, the court would bear in mind that parties negotiated and concluded the contract on the basis of risk allocation, whereby the party claiming liquidated damages forecloses the possibility of claiming an amount higher than the sum stipulated, by way of proving higher actual loss, so as to enjoy the benefit of the relative ease and certainty of establishing a claim for liquidated damages as opposed to a claim for unliquidated damages.

(x) On the contrary, if it is concluded that the stipulation is by way of penalty, the person claiming such penalty would be required to prove loss accurately, including the quantum of loss, and claim reasonable compensation on that basis."

15. The Respondents herein did not plead that they suffered loss in their counter statement cum counter claim before the Arbitral Tribunal, and no evidence of loss was adduced. Needless to say, the Respondents did not plead that the loss was impossible or difficult to prove in light of the

nature of the contract.

16. The conclusions of the Arbitral Tribunal should be examined in the above factual context. At internal page 12 of the Award, the Arbitral Tribunal recorded its conclusion that liquidated damages are leviable for 25,945 numbers of PSC Sleepers, which were supplied belatedly. Before arriving at such conclusion, in a table at paragraph 3 of the Award, the Arbitral Tribunal set out the dates of supply of specific quantities and held that liquidated damages are applicable for the quantity supplied belatedly. There is no consideration of the question whether the Respondents suffered loss as a result of belated supply and, most certainly, no discussion or conclusion with regard to the quantum of loss and the proof thereof in the Award. Thus, the award of liquidated damages is completely unsustainable in light of the law laid down in such regard. The Hon'ble Supreme Court held in *Fateh Chand v. Balkishan Das, AIR 1963 SC 1405,* that forfeiture of any amount deposited under the contract should satisfy the requirements of Section 74 of the Indian Contract Act, 1872. Except for recording that the supply was belated and drawing reference to paragraph 0504 of IRS condition and Clause 8.4 of the contract, the Award contains no discussion on loss in the context of forfeiture of security deposit too. These conclusions qualify as being patently illegal. Consequently, the Award merits interference under Section 34 of the Arbitration and Conciliation

Act, 1996.

17. The settled legal position is that an Arbitral Award can be severed and upheld in part while being set aside in part. However, such Award cannot be modified under Section 34.

18. For reasons set out above, O.P.No.185 of 2021 is allowed by setting aside the Award as regards the refusal to grant interest as per the MSMED Act and as regards the grant of liquidated damages and forfeiture of security deposit. However, it is made clear that nothing in this order should be construed as a finding that the Petitioner is entitled to interest as per the MSMED Act. As a corollary, it is open to the Petitioner to institute *de novo* arbitral proceedings in such regard in accordance with the relevant contract. If such proceedings are instituted, the Petitioner shall be entitled to the benefit of Section 43(4) of the Arbitration and Conciliation Act, 1996. Consequently, connected applications are closed.

Sd./-S.K.R.J
06.12.2021

//Certified to be true copy//
Dated at Madras this the day of 2021.

COURT OFFICER(O.S.)

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