

## **The Union Of India vs K.H. Rao on 16 January, 1976**

**Equivalent citations: AIR1976SC626, (1977)1SCC583, 1976(8)UJ203(SC), AIR 1976 SUPREME COURT 626, 1976 TAX. L. R. 1458**

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**Bench: R.S. Sarkaria, S. Murtaza Fazal Ali**

### **JUDGMENT**

R.S. Sarkaria, J.

1. This is a defendant's appeal directed against a judgment and decree of the Mysore High Court.
2. On September 16, 1949, the plaintiff, K.H. Rao, entered into an agreement (Ex. D-2) with the defendant (Union of India) through its Military Head Quarter, Madras Area, contracting to supply onions for the period, October 1, 1949 to March 31, 1950, at the supply depots of the defendant in Bangalore, Cochin, Coimbatore and Wellington, at the rates mentioned in the Schedule to the agreement. The supply was to be made in such quantities as may be required from time to time by the defendant, not exceeding 1 bs. 45 000 a month for the Bangalore Depot, 1 bs. 300 for the Coimbatore Depot, 1 bs. 5000 for the Wellington Depot and 1 bs. 5000 for the Cochin Depot. Under the agreement, there was a security deposit of Rs. 4,300/- made by the defendant. This deposit was liable to forfeiture only in the event of any breach or non-performance of the contract by the plaintiff. Clause (7) of the agreement provided that if there was failure on the part of the plaintiff to perform the contract, the defendant was at liberty to make purchases of the onions elsewhere at the risk of the plaintiff. Clause (8) empowered "the officer sanctioning the contract" to rescind the contract by written notice to the plaintiff in the six contingencies referred to in that clause, one of which was that such rescission could be made by that officer if the plaintiff declined, neglected or delayed, in complying with any demand or requisition or if he in any other manner failed to perform or observe the conditions of the contract.
3. We are concerned here with the supplies to Bangalore Depot. The plaintiff supplied the onions, as undertaken by him, to that Depot for October and for the first seven days of November, 1949. From and on November 17, 1949, the plaintiff completely stopped the supply of onions notwithstanding the demands issued by the defendant from time to time for the same. After some correspondence, the plaintiff was informed by a letter (Ex. P-7) that from the 29th December 1949, the contract stood rescinded. This communication of rescission (Ex. D.40) was signed by one J.H. Wadia, then a Lt. Colonel, CRIASC.

4. The plaintiff made unsuccessful demand for the payment of the amounts admittedly due to him for the onions he had supplied and also for the return of the security deposit which he had made under the contract in question and also similar sums, due to him under earlier contract with the defendant.

5. On March 5, 1953, the defendant informed the plaintiff's bankers that a sum of Rs. 18,228/14/5 was debited against the plaintiff towards damages payable by him for the breach of the contract.

6. There after, on April 4, 1953, the plaintiff filed a suit for the recovery of Rs. 45,359/- consisting of these items:

(a) Amount claimed as due under earlier Rs. As. P. contracts. 9.453-4-0 (b) Amount claimed towards the value of the goods supplied under the suit contract. 10.928-5-0 (c) Security deposit under the suit contract. 4,300-0-0 (d) Security deposit under the earlier contracts. 3,045-0-0 (e) Claims towards reimbursements of the value of onions supplied to defendant otherwise than under the contract. 4,950-0-0 (f) Profits which plaintiff had been prevented from making under the suit contract. 3,000-0-0 (g) Interest on these sums 9,632-7-0 (h) Notice charges 50-0-0 ----- Rs. 45,359-0 -----

7. The plaintiff pleaded that more than Rs. 75,000/- was due to him from the defendant on December 15, 1949 under the earlier contract and that there was abnormal delay on the part of the defendant in the payment of the bills, which paralysed the financial resources of the plaintiff; that his supplies to the Bangalore depot were made in compliance with excessive demands and some of them, were illegally diverted by the defendant to the Jalahalli Depot, though the supply to that depot was the obligation of another contractor; that the CRIASG Madras was not competent to rescind the contract or forfeit the deposits and therefore, the rescission was illegal and that the defendant illegally refused to accept substitutes for onions as per the terms of the contract. The set off Rs. 18 228-11-5 made by the defendants for the alleged recovery of damages was also challenged as unwarranted, illegal and unauthorised and that the breach of contract was on the part of the defendants.

8. The defendants resisted the suit on the ground that the suit was time-barred : that the plaintiff had failed to perform his part of the contract which was, in consequence, validly rescinded; that the security was validly forfeited and that the defendants were entitled to a sum of Rs. 18, 228-14 5 as damages for the breach of the contract.

9. The trial court (District Judge) held that the plaintiff had committed breach of the contract, and consequently, the defendants had rightfully rescinded the contract and debited Rs. 18228-14-5 against the plaintiff; that the diversion of the supply to Jalahalli depot by the defendant was not impermissible or contrary to the contract; that the suit was not time-barred except in regard to the part of the claim which relates to damages. In the result, the District Judge passed a decree for Rs. 2270 8 0 only in favour of the plaintiff and dismissed the rest of his claim.

10. Aggrieved, the plaintiff carried an appeal to the High Court which held that so far as the Bangalore Depot was concerned, the demand was excessive and outside the contract as the supply made at Bangalore Depot was diverted illegally to the Jalahalli Unit (R.I.A.I) which was outside the Bangalore jurisdiction; that since the rescission of the contract was made by the General Officer Commanding (Area Commander) who had sanctioned the contract, it was void and the security deposit could not be forfeited; that an amount of Rs. 9,607-11-4 was due to the plaintiff towards the price of the onions under the suit contract and another sum of Rs. 9,453-4-0 was payable to the plaintiff under the earlier contracts. That as no demands were made after the 29th Dec, 1949 on the plaintiff, he was not liable to pay the difference between the market rate and the contract rate. Modifying the decree of the trial court, awarded to the plaintiff, decree for Rs. 31,609-5-4, consisting of these items was passed.

(a)(i) Amounts due under the earlier Rs. As. P. contracts ... 9,543-4-0 (ii) Interest on the above amounts at 6% p. a. from 1st Dec. 1949 till the date of the suit. ... 1,915-0-0  
(b)(i) Security Deposit under earlier contracts. ... 3,045-0-0 (ii) Interest on the Deposit at 6% p. a. ... 609-0-0 (c)(i) Amount due for onions supplied under the suit contract. ... 9,607-11-4 (ii) Interest on this sum at 6% p. a. ... 1,878-0-0 (d)(i) Security deposit under the suit contract. 4,300-0-0 (ii) Interest on the deposit at 6% p. a. 711-0-0 ----- Rs. 31,609-5-4 ----- Hence this appeal.

11. It is undisputed that the plaintiff did not supply any onions under the contract after November 17, 1949, despite demands by the defendant. Evidently, therefore, the plaintiff had committed a breach of the contract and thereupon, Clauses 7 and 8 of the agreement became operative. Under Clause 7, the defendant was at liberty to make purchases of onions elsewhere at the risk of the plaintiff and recover on demand any excess cost so incurred over the contract price from the plaintiff. The breach of the contract, also gave a right to the Officer sanctioning the contract, to rescind the contract after written notice.

12. The only question that falls to be determined is whether the rescission of the contract with effect from December 29, 1949 was made by a competent officer. The High Court has held that since the communication of rescission was signed by a Lt Col. GRIASC, and not by the Area Commander, it had not been made by the "officer sanctioning the contract" within the contemplation of Clause 8 of the agreement. The finding of the High Court has been seriously challenged before us by the appellant. It is stressed that the agreement was also executed by a Lt. Col. of GRIASC who in reality was the "Officer sanctioning the contract", and the mere fact that the officer had before executing the agreement verbally obtained the approval of the then Brigadier who was acting as Area Commander, does not mean that the Area Commander, and not the Lt. Col. CRIASG, was the "Officer sanctioning the contract". On this point, the Counsel has adopted the reasoning of the trial Court.

13. On the other hand, Counsel for the respondent has reiterated the reasoning of the High Court.

14. It appears to us that the contention of the appellant must prevail.

15. Ex. D 3 is a letter, dated September 16, 1949, addressed to the plaintiff-respondent informing the latter that the Governor-General had accepted his tender dated, August 3, 1949 for the supply of onions to various Depots including Bangalore Depot. The tender has apparently been accepted by an officer of the rank of Lt. Col. whose endorsement under this letter reads as follows:

Acceptance sanctioned by Lt. Col. Adj. Victor, AA and Q.MS.

Below this endorsement there appears to be the signature of some officer (For Brig. Offg. Comd. Madras Area), This signature has been appended under the caption : "Designation of the Sanctioning Authority.

16. Ex. P-7 dated December 31, 1949, is a letter addressed by the Lt. Col-CR1ASC, to the plaintiff informing him about the rescission of the contract w. e.f. December 29, 1949 and the forfeiture of his security deposit of Rs. 4300/- and also the proposal to purchase onions elsewhere at the risk of the plaintiff. Ex. D-40 is another letter, dated December 29, 1949 from Lt. Col. AA & QMG Madras Area informing him that "the sanction of the; Area Command is accorded to the rescission of the contract.

17. Reading the letters Ex. D-40 and P-7 together, it will be clear that the Lt. Col. who communicated the rescission of the contract to the plaintiff was exercising the powers of "Area Commander in the matter. Lt. Col. Suri who had signed the letter Ex. D-40, was examined as DW-4. He produced Ex. D 38, a copy of the order passed by the General Officer Commanding Madras Area, delegating all his financial powers to the witness. The original of Ex. D-38 bears the signature of Maj General, A.A. Rudra, the then Area Command. It also bears specimen signatures of the witness, Lt. Col. Suri testified that the papers were put up before him with a recommendation for rescission of the contract in question in December. 1949 on account of constant failures on the part of the plaintiff to supply onions despite repeated warnings of the Commanders of the Supply Depots concerned. According to usual procedure, the witness took the papers to the G.O.C. for consultation. After discussion with him, the witness issued the orders of rescission of the contract. The witness added whenever the G O. C was not available for consultation, the witness used to pass orders in such matters in the exercise of his own discretion as per powers delegated to him. The witness also produced the copy of the office note, D-39, bearing the initials of Lt. Col. J. H. Wadia, the then C.A.S.G. Madras Area. The original office note however was not produced. It may be observed that no objection in regard to its mode of proof was taken when this document was let in evidence.

18. Ex. D-38 produced by the witness, provides:

Under the provisions of FR(I) Pt. I Rule 34(b) I hereby authorise the undermentioned officer to sign communications and documents of a financial character on my behalf upto the fullest extent under the rule in respect of 'A' and 'Q' matters, Lt. Col. Dr. Suri AA & QMS HQ, Madras Area.

19. The authenticity. p. Ex. D-38 cannot be doubted. It clearly establishesthat Lt. Col. Suri (then AA & Q.MG Madras' Area) was authorised to, exercise the powers of the Area Commander to the

fullest extent, having financial implication, which would include the power to rescind a contract, also.

20. The order, Ex. D-38, is dated December 17, 1949, while the rescission was made three weeks thereafter.

21. Even if it is assumed that the Area Commander was the "officer sanctioning the contract" then also, it is clear from the evidence of DW-4, Lt. Col. Suri, read with Ex D-40, that the order of rescission, in fact, had been passed by the Area Commander.

22. Our attention was drawn to the document, Ex. P-45, dated May 20, 1951, whereby the prescribed contract form was amended and in Clause 8, after the words "officer sanctioning the contract", the words or AA and QMG/ AQMG Area Drig i/c Adm Commd AQMG/QI Army HQ," was added. This amendment was of a clarificatory character, only. In any case, this has no bearing on the point under consideration because in the instant case it has been: proved than in fact, the contract had been sanctioned and later rescinded by the same officer.

23. We therefore, think that the learned Judges of the High Court were in error in holding that the order of rescission of the contract was unauthorised and invalid. Accordingly, we reverse that finding, and hold that the contract had been duly rescinded under Clause 8(iv) of Ex. D-2,.on the failure of the plaintiff to supply the onions after the 17th November 1949, despite demand.

24. Counsel for the plaintiff-respondent tried to raise before us another plea founded on Section 38(2) of the Sale of Goods Act. The argument is that under the contract, the onions were to be supplied in monthly instalments and when the plaintiff failed to deliver the instalments from 17.11.1949 onwards, it did not amount to a repudiation of the entire contract making the plaintiff liable for damages, if any, incurred by the defendants after November 17, 1949 in making risk purchases from the market. This plea Cannot be entertained at this stage. It was not set up in the plaint. No issue was framed on this point, nor was it agitated before the courts below. As is clear from a plain reading of Section 38, itself, the question whether in case of a default of supply, the entire contract for instalment deliveries stands repudiated or not, is one of fact depending on the circumstances of the case. We therefore do not permit the plaintiff to raise this plea for the first time now in this Court.

25. The next question to be considered is, whether the diversion of any onions supplied at the Bangalore Depot by the plaintiff' to the, Jalahalli Depot amounted to a breach of any term of the contract the part of the defendants. In this connection, it is noteworthy that under the contract, the plaintiff was bound to supply at the Bangalore Depot onions up to the maximum of lbs. 45000 per month. How the onions were utilised or disposed of by the defendants after receipt of their delivery at the Bangalore Depot was a matter which was no concern of the plaintiff. The plaintiff had made the supplies for one month and 17 days only. It has not been shown that the onions supplied either in the month of October or in November were more than the stipulated amount of lbs. 45000. On the contrary, Ex. 46 series (pages 348 to 364.of the Paper Book) shows that the onions demanded from the plaintiff and supplied by him in October 1949 were lbs. 40900, and in November 1949

(upto 15th Nov.) were lbs. 20,300 only. That is to say, the total supplied by the plaintiff in these two months did not exceed lbs. 60,451.

26. Counsel for the plaintiff however arithmetically works out the supply for the first 7 days of November as lbs. 1500 per day to show that the demand made was excessive. We are afraid this method of calculation is repugnant to the contract, under which the maximum to be supplied was fixed on monthly basis. It is nobody's case that the defendants indented more than the stipulated quantity of lbs. 45000 for any month.

27. Nor has it been alleged or shown that the plaintiff was asked to supply the onions at Jalahalli Depot. If the defendants indented not more than lbs. 45000 per month, they were at liberty to divert the onions after their receipt at the Bangalore Depot to any other station. The property in the goods had passed to the defendants on delivery thereof. There is nothing in the agreement which prohibits such diversion by the defendants. So long as the onions demanded and supplied for any month at the Bangalore Depot did not exceed lbs. 45000, the plaintiff could not complain of any breach of the contract by the defendants, or have any grievance on the ground that a part of the onions so supplied to the Bangalore Depot had been diverted or taken by the defendants to Jalahalli.

28. The High Court was thus in error in holding that excessive demands for the supply of onions were made by the defendants and that the latter were not entitled under the contract to divert the onions supplied by the plaintiff at Bangalore Depot to Jalahalli Depot, we have therefore no hesitation in setting aside that finding.

29. It was contended before us on behalf of the Respondent that in any case, the defendants were not entitled to withhold payment of the sums due or the security deposit relatable to an earlier contract.

30. As against this, Mr. Prasad has referred us to Clause 5 of the agreement (tender D/5; which provides:

All moneys or compensations payable by me/us to Government under the terms) of the contract, may be deducted from or realised by the sale of sufficient part of my/our security deposit, or from interest arising therefrom or from any sums which may be due or may become due to me/us by Government under this or any other account.

31. The crucial words in the above clause are those that have been underlined. In the event of default of supply by the contractor and of valid rescission of the contract, the defendants were entitled under this Clause 5 read with Clauses 7 and 8 to set off and adjust the sum of Rs. 9,543/4/- due to the plaintiff under the earlier contract, against the damages incurred by the defendants.

32. But Clause 5 aforesaid does not authorise forfeiture of the security deposit of the plaintiff which he had made under the earlier contracts.

33. Now remains the question of the security deposit relating to the contract in question. Since the plaintiff had committed a breach of the contract, Clause 8 of the contract which gives a discretion to the defendants to forfeit the security deposit became operative. Viewed in the totality of the circumstances of this case, such forfeiture however would operate as a penalty. But the court cannot in view of the Exception to Section 74 of the Contract Act 1872, directly relieve the plaintiff of the hardship on that score. Nevertheless, there is another feature of this case which could not be overlooked by the court while assessing damages under Section 73 of the Contract Act. It is manifest from Ex. P 37, P-3 and P-39 that during the relevant period lbs. 28,360 of onions delivered by the plaintiff at the Bangalore Supply Depot were diverted to Jallahalli Unit. Although such diversion, as already observed, did not contravene any condition of the contract yet diversion of such a huge quantity to Jallahalli Depot was possibly beyond the ken of the plaintiff. In other words, such diversion resulted in an unexpected escalation of the damages. This factor could legitimately be taken into account in scaling down the damages. Confronted with this situation Mr. Prasad does not take a rigid stand with regard to the refund of the security deposit made by the plaintiff under the suit contract. We therefore scale down the damages to the extent of the security deposit and direct that the whole of this amount of Rs. 4300/- be refunded to the plaintiff.

34. According to the trial court, on account of the failure of the plaintiff to supply onions after the 17th November 1949, despite demand, the defendants had suffered a loss of Rs. 18228/115 being the difference between the contract price and the market price at which onions were purchased at the risk of the plaintiff by the defendants. The correctness of the accounts relating to the risk and purchase expense submitted by the defendants was not disputed in the trial court although in a light-hearted manner it was said that the purchases were made at higher rates than the prevailing market rates by the officers attached to the supply depot. No evidence however was led by the plaintiff to substantiate this assertion. We have therefore no hesitation in holding that the defendants did suffer a loss of Rs. 18,228/11/5 on account of the breach of the contract committed by the plaintiff.

35. The High Court held that these sums were due to the plaintiff from the defendants:

(a) Amount due under the earlier contract Rs. 9543-4-0	(b) Amount due for onions supplied under the suit contract Rs. 9607-11-4	-----	Total : Rs. 19,150-15-4
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36. This finding of the High Court has not been disputed before us. The difference between the damages incurred by the defendants and the sums due to the plaintiff for the supplies made under the earlier and the present contracts, comes to app. Rs. 922/- which is payable to the plaintiff with 6 per cent interest from January 1, 1950 till 6 6 1967, the date by which defendants were to deposit a portion of the decretal amount in accordance with the High Court's order dated 7.4.1967. No interest however can be allowed to the plaintiff on the security deposits.

37. In the light of above discussion, we partly allow the defendants appeal, and for the decree of the High Court, substitute a decree for the recovery of the under-mentioned amounts (less already paid to or withdrawn by the plaintiff):

1. Security deposit under the earlier con- tracts. Rs. 3,045-0-0 2. Security deposit under the suit contract. Rs. 4,300-0-0 3. Difference between the (i) damages incurred by the defendants and the amounts due to the plaintiff under the contracts, as indicated above Rs. 922-0-0 (ii) interest on this amount from Jan. 1, 1950 till 6.6.1967 i.e the date by which a portion of the decretal amount was ordered to be deposited by the High Court, Rs. 957-0-0 ----- Total : Rs. 9,224-0-0 -----

38. In addition, the plaintiff shall be entitled to get proportionate costs from the defendants of this Court only.