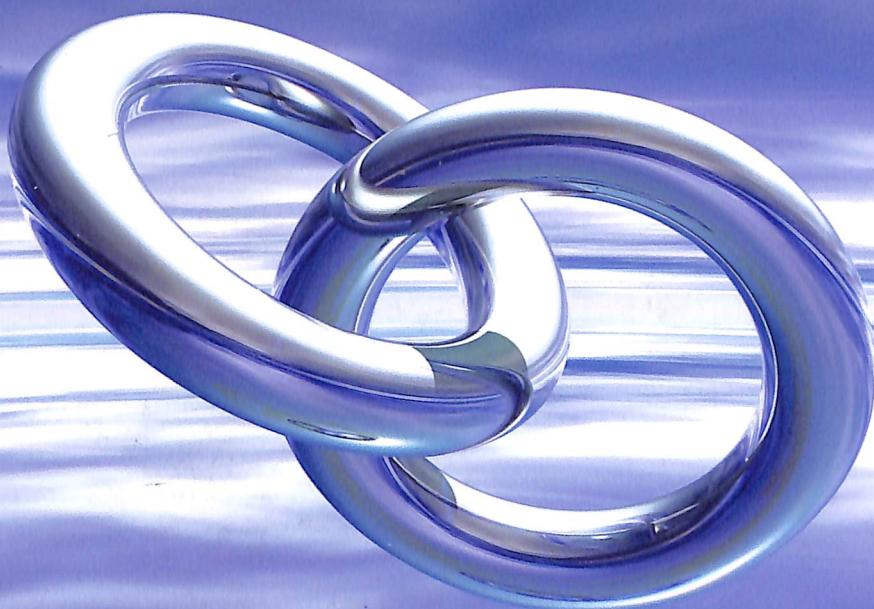


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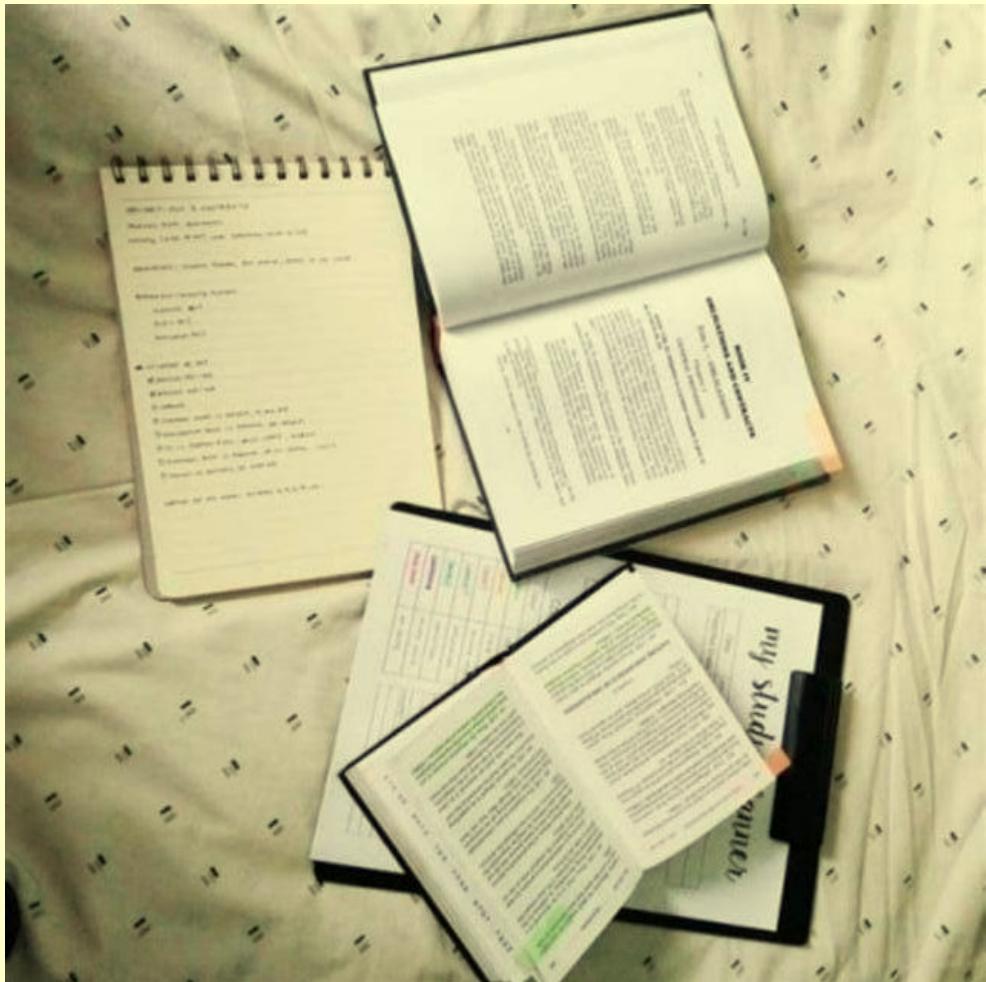
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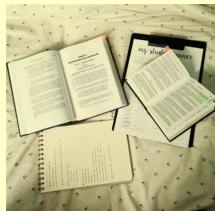
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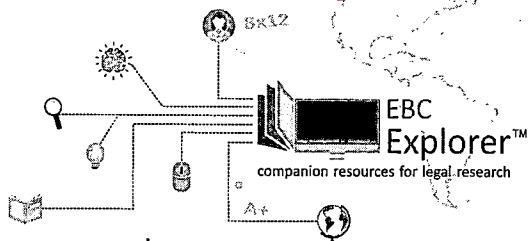
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# LAW OF CONTRACT

(A Study of the Contract Act, 1872)

*and*

*Specific Relief*

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## Preface

The Contract Act, 1872 provides the legal framework for formulation of trade, business and commercial relations and transactions in which contract is involved. It has completed its history of 144 years. The provisions of the Act and principles enshrined therein and the application of such principles by the courts to enormous and ever changing fact-situations constitute the body of the Law of Contract of the country.

The court decisions provide the basic source material of development of this subject and also for finding out the recent trends, some of the important rulings of the period between the present and preceding editions are to be seen in the following areas of the subject: A contract means bilateral relations, not just only unilateral. But exceptionally, one of the parties may be given the right to do things unilaterally, e.g., a banker was given the right to appoint an arbitrator all by himself under the loan arrangement. This special position may be allowed to protect the interest of lending bankers.

An agreement entered into by the e-mail process has binding effect, though not signed by parties. Some new decisions have been delivered on withdrawal of bids. No bidder can insist that his bid should be accepted because it is the lowest. All that he can say is that there should be no bias, and there should be fairness, in the decision-making process. The mere deposit of 20 per cent of the bid amount does not make the bidder owner of the property. He has to wait for approval of his bid. Letters of intent that the tender would be accepted does not have binding effect either way. A contractor can be blacklisted only because of grave misperformance of the contract, not because of his impropriety at the stage of bids or tenders.

No binding obligation emerges on the part of the Government where the contract is in conflict with constitutional provisions. Where the owner of land had enjoyed considerable benefits after his land was freed from acquisition and before it was transferred to the Government for school making purpose without price, he was not allowed to assail the transaction by saying that it was without consideration. Mortgage in favour of a minor is *void ab initio*. Alienation by *de facto* guardian of minor's land was reversible at the instance of the minor on attaining majority and the price paid was

## VIII Law of Contract

recoverable from the guardian and not the minor. Beneficial rights under the Employees' State Insurance Act cannot be contracted out. Controllers of Cricket cannot have an interest in the events organised by the Board. It is something awfully against public policy.

Restraint upon a former employee as a ladies hairdresser from practising the same profession for 12 months and within half a mile of the employer's place has been held to be reasonable. An arbitration agreement restraining parties from approaching court over the same issue has been held to be not opposed to public policy or being in restraint of trade. A Lok Adalat is not a court. Restrictions upon jurisdiction are not applicable to it. A contract for CCTV services at Railway stations which happen to display vulgar material was terminated. The forfeit of the whole of his deposit money might be ruinous to him whereas the Railway's loss was not of monetary nature.

A bank guarantee was not allowed to be encashed because the Authority had made good its losses otherwise. The controversial point whether the surety alone be allowed to be sued without touching the principal debtor though the latter is in possession of means which comfortably enable him to pay, continues to engage attention of the courts. The right to encash a bank guarantee was held to have been lost when the contract had expired without encashment of the bank guarantee. Pledgee's right for his dues prevails over all other rights and claims. If an LIC agent does not deposit the amount received by him from the insured, LIC has to bear the consequences.

Privity of contract is necessary for seeking specific performance. A contract requiring a retrospective date for execution was held to be not specifically enforceable. Specific enforcement cannot be claimed against a person who is devoid of title or any right to transfer: *Nemo dat quod non habet*. A person who becomes entitled to specific performance also becomes entitled to an injunction to prevent the other party from dealing with the property in any manner whatsoever.

All these and many more rulings have been absorbed into the text at their appropriate places.

Ghaziabad  
October 3, 2016

—DR AVTAR SINGH

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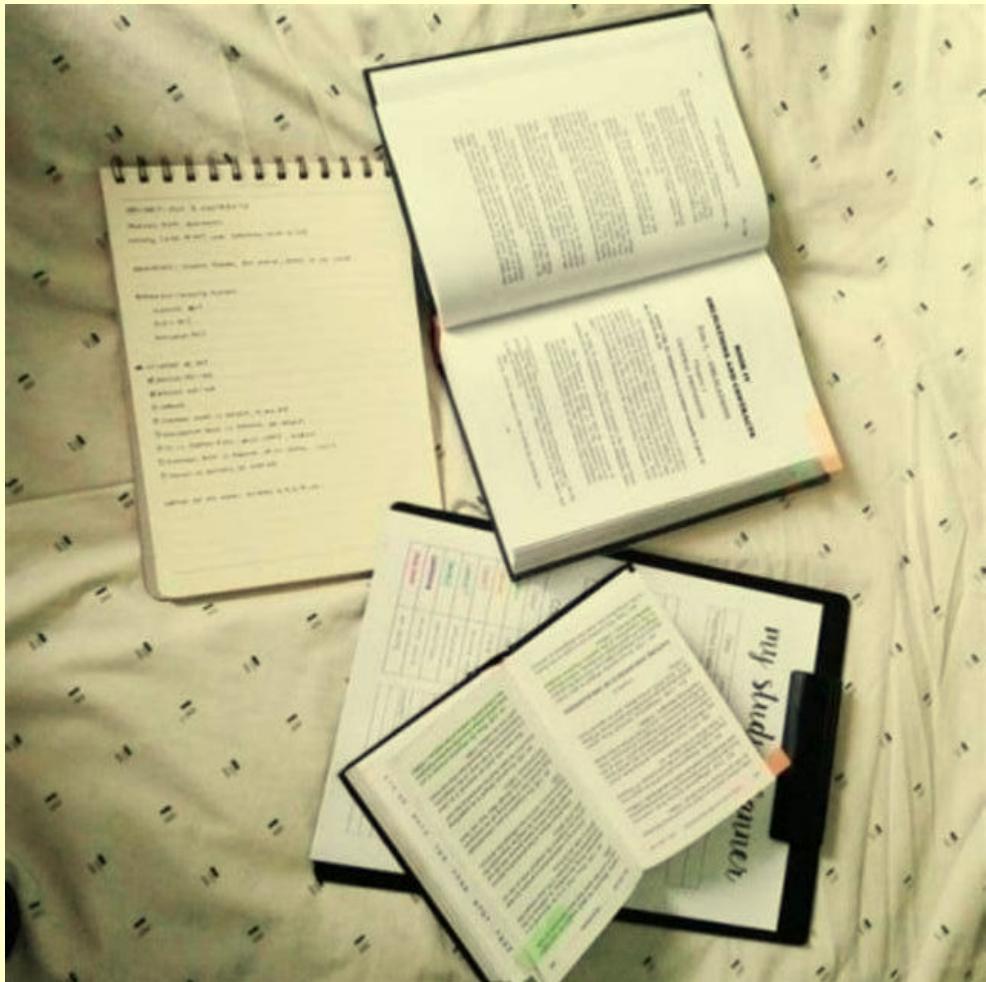
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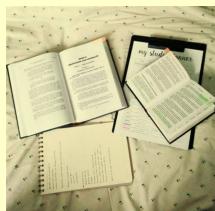
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PART I

**GENERAL PRINCIPLES**  
**(Ss. 1–75)**

# Agreement, Contract and Proposal

THE INDIAN CONTRACT ACT, 1872

[Act 9 of 1872]<sup>1</sup>

[25 April 1872]

**Preamble.**—Whereas it is expedient to define and amend certain parts of the law relating to contracts; it is hereby enacted as follows:—

## *Preliminary*

**S. 1. Short title.**—This Act may be called the Indian Contract Act, 1872.

**Extent and commencement.**—It extends to<sup>2</sup> (the whole of India)<sup>3</sup> (except the State of Jammu and Kashmir); and it shall come into force on the first day of September 1872.

1. For the Statement of Objects and Reasons for the Bill which was based on a report of Her Majesty's Commissioners appointed to prepare a body of substantive law for India, dated 6th July, 1856, *see*, Gaz. of India, 1867, Extra., p. 34; for the Report of the Select Committee, *see*, *ibid*, Extra., dated 28th March, 1872; for discussions in Council, *see*, *ibid*, 1867, Supplement, p. 1064; *ibid*, 1871, p. 313 and *ibid*, 1872, p. 527.

The chapters and sections of the Transfer of Property Act, 1882 (IV of 1882), which relate to contracts are, in places in which that Act is in force, to be taken as part of Act IX of 1872—*see* Act IV of 1812, S. 4.

This Act has been extended to Berar by the Berar Laws Act, 1941 (IV of 1941), to Dadra and Nagar Haveli by Regn. 6 of 1963, S. 2 and Sch. I, to Goa, Daman and Diu by Regn. 11 of 1963, S. 3 and Sch., to Laccadive, Minicoy and Amindivi Islands by Regn. 8, 1965, S. 3 and Sch., to Pondicherry by Act 26 of 1968, S. 3 and Sch. and has been declared to be in force in—

the Santhal Parganas—*see* the Santhal Parganas Settlement Regulation (III of 1872), S. 3, as amended by the Santhal Parganas Justice and Laws Regulation, 1899 (III of 1899), S. 3.

Panth Piploda—*see* the Panth Piploda Laws Regulation, 1929 (I of 1929), S. 2.

It has been declared by notification under S. 3(a) of the Scheduled Districts Act, 1874 (XIV of 1874), to be in force in—

the Tarai of the Province of Agra—*see* Gaz. of India, 1876, Part 1, p. 505;

the Districts of Hazaribagh, Lohardaga and Manbhumi and Pargana Dhalbhum and the Kolhan in the District of Singbhum—*see* Gaz. of India, 1881, Part 1, p. 504.

The District of Lohardaga included at this time the present District of Palamau which was separated in 1894. The District of Lohardaga is now called the Ranchi District—*see* Calcutta Gaz., 1899, Part 1, p. 44.

It has been amended in C.P. by C.P. Act 1 of 1915 and in C.P. and Berar by C.P. Berar Act 15 of 1938.

2. Subs. by A.O. 1950 for “all the Provinces of India”.

3. Subs. by S. 3 and Schedule of Act 3 of 1951 for “except Part ‘B’ States”.

<sup>4</sup>[\* \* \*] Nothing herein contained shall affect the provisions of any Statute, Act or Regulation not hereby expressly repealed, nor any usage or custom of trade, nor any incident of any contract, not inconsistent with the provisions of this Act.

**S. 2. Interpretation clause.**—In this Act the following words and expressions are used in the following senses, unless a contrary intention appears from the context:—

- (a) When one person signifies to another his willingness to do or to abstain from doing anything, with a view to obtaining the assent of that other to such act or abstinence, he is said to make a proposal;
- (b) When the person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted. A proposal, when accepted, becomes a promise;
- (c) The person making the proposal is called the "promisor", and the person accepting the proposal is called the "promisee";
- (d) When, at the desire of the promisor, the promisee or any other person has done or abstained from doing or does or abstains from doing, or promises to do or to abstain from doing, something, such act or abstinence or promise is called a consideration for the promise; [Notes under Chap. 3 on consideration]
- (e) Every promise and every set of promises, forming the consideration for each other, is an agreement; [Notes under consideration]
- (f) Promises which form the consideration or part of the consideration for each other, are called reciprocal promises; [Notes under consideration]
- (g) An agreement not enforceable by law is said to be void; [Notes under Section 23 void agreements]
- (h) An agreement enforceable by law is a contract;
- (i) An agreement which is enforceable by law at the option of one or more of the parties thereto, but not at the option of the other or others, is a voidable contract; [see Notes under Sections 19 to 19-A]
- (j) A contract which ceases to be enforceable by law becomes void when it ceases to be enforceable. [For notes see under Section 56]

### DEFINITION OF CONTRACT

The term "contract" is defined in Section 2(h) of the Indian Contract Act, 1872, as follows: "An agreement enforceable by law is a contract."<sup>5</sup>

Thus for the formation of a contract there must be—(1) an agreement, and (2) the agreement should be enforceable by law.

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- 4. The words "the enactments mentioned in the Schedule hereto are *repealed* to the extent specified in the third column thereof; but" were *repealed* by S. 3 and Sch. II of the Repealing and Amending Act, 1914 (X of 1914).
  - 5. *Bharti Airtel Ltd v Union of India*, (2015) 12 SCC 1, a licence to provide telecom service is a contract between the licensee and Government of India, the licensor.

## Agreement

“Agreement” is defined in Section 2(e) as “every promise and every set of promises forming the consideration for each other”. And a promise is defined as an accepted proposal. Section 2(b) says: “A proposal, when accepted, becomes a promise.” This is another way of saying that an agreement is an accepted proposal. The process of definitions comes down to this: A contract is an agreement; an agreement is a promise and a promise is an accepted proposal. Thus every agreement, in its ultimate analysis, is the result of a proposal from one side and its acceptance by the other.<sup>6</sup>

### *When agreement becomes contract*

An agreement is regarded as a contract when it is enforceable by law.<sup>7</sup> In other words, an agreement that the law will enforce is a contract. The conditions of enforceability are stated in Section 10. According to this section, an agreement is a contract when it is made for some consideration, between parties who are competent, with their free consent and for a lawful object.

**S. 10. What agreements are contracts.**—All agreements are contracts if they are made by the free consent of parties competent to contract, for a lawful consideration and with a lawful object, and are not hereby expressly declared to be void.

Nothing herein contained shall affect any law in force in <sup>8</sup>[India] and not hereby expressly repealed, by which any contract is required to be made in writing or in the presence of witnesses, or any law relating to the registration of documents.

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6. An arrangement for sale of goods which imposed no obligations on the part of the purchaser and was not even signed by him was held to be no agreement. It must have been a mere understanding. There being no mutuality, the purchaser could not ask for the remedy of specific enforcement under S. 15, Specific Relief Act, 1963; *S.M. Gopal Chetty v Raman*, AIR 1998 Mad 169. Every agreement has not to be in writing. It must be bilateral, *Tarsem Singh v Sukhminder Singh*, (1998) 3 SCC 471; AIR 1998 SC 1400. Writing is necessary only when prescribed by law, *T.N. Tea Plantation Corpn Ltd v Srinivasa Timbers*, AIR 1999 Mad 111. *Conrad Dias v Joseph Dias*, (1996) 2 Mah LJ 208: (1995) 3 Bom CR 218, oral agreement between father and son for tenancy. *Asudamal Laxmandas Sindhi v Kisanrao Wamanrao Dharmale*, (2004) 2 Bom CR 361, an agreement for sale of land does not require to be an attested document. It was an agricultural land and the purchaser was not a farmer. His suit for specific enforcement was allowed because it was his problem to get necessary approvals.
  7. S. 2(h). *Mohta Alloy & Steel Works v Mohta Finance & Leasing Co Ltd*, 1987 AIHC 1327 (Del), a lease agreement between two bodies corporate was signed by one only, representing both sides because he was a director in both the legal entities. Held valid. *K. Basavarajappa v Tax Recovery Commr*, (1996) 11 SCC 632, an agreement to sell does not create any right or interests in the property under sale. *R. Rangaraj v Legal Representatives*, 2000 AIHC 2206, agreement signed by the very party who had to sell the land, valid for specific enforcement. *Randhir Singh Chandolk v Vipin Bansal*, (2006) 135 DLT 56, under an oral arrangement of sale of property, the receipt for money was signed by the seller, the court said that the law did not prohibit a written offer of sale signed by the seller being accepted orally by the buyer.
  8. Subs. by S. 3 and Schedule of Act 3 of 1951 for the words “Part A States, and Part C States” which have been substituted by the A.O. 1950 for “the Provinces”.

Every contract is an agreement, but every agreement is not a contract. An agreement becomes a contract when the following conditions are satisfied:

- (1) There is some consideration for it. [Ss. 2(d) and 25]
- (2) The parties are competent to contract.<sup>9</sup> [Ss. 11 and 12]
- (3) Their consent is free. [Ss. 13–22]
- (4) Their object is lawful.<sup>10</sup> [Ss. 23–30]

*Bilateral relation, not unilateral*

There was a concluded agreement under the Rural Franchisee Scheme between consumers and Electricity Board fixing specific rates with regard to incentive payable to consumers. It was held that a unilateral revision or modification in the scheme by the Board was not permissible during currency of the agreement. Such amendments were not enforceable.<sup>11</sup>

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9. C.K. Asati v Union of India, AIR 2005 MP 96, experience of partners can be considered as experience of their firm. Without considering this, refusal of tender to the firm was not proper. Patel Engg Ltd v National Highways Authority of India, AIR 2005 Del 298, requirement of experience in award of contract, correct perspective is to see, actual experience of the participant and entity and not label of the firm. A statutory body could not give effect to experience certificate issued by it.
  10. Once an enforceable agreement comes into being it remains enforceable even if the goods which were to be delivered under it were brought late and they were also accepted by the other party. See, Jain Mills and Electrical Stores v State of Orissa, AIR 1991 Ori 117. A Collector can be authorised only by statute to recover any dues as arrears of land revenue. Such authority cannot be given under an agreement. Power so given by Zila Parishad was held to be against law, Mahesh Chandra v Zila Panchayat Mainpuri, AIR 1997 All 248. A *statutory contract* means a contract of the contents of which some portion is filled under a statute. For example, S. 43-A(2) of the Electricity Supply Act, 1948 fills into a power purchase agreement the terms relating to determination of tariff. Indian Thermal Power Ltd v State of M.P., (2000) 3 SCC 379: AIR 2000 SC 1005. The fact that a contract is for construction of a public utility and is awarded by a statutory body does not necessarily make it a statutory contract. Kerala SEB v Kurien E. Kalathil, (2000) 6 SCC 293: AIR 2000 SC 2573. B. Rajamani v Azhar Sultana, AIR 2005 AP 260: (2005) 2 An LD 862, agreements to sell immovable property was reduced to writing but not signed by the purchaser, did not mean there was no concluded contract. The contract came into existence when both parties agreed. It became enforceable. Varsha Fabrics (P) Ltd v State of Orissa, (2006) 102 Cut LT 137, the share Purchase Agreement had not been signed by the parties, the court said that signing of the same was a mere formality, since the terms and conditions had already been negotiated and agreed upon between the parties. Bhagwati Enterprises v Rajasthan SRTC, AIR 2006 Raj 233, tenders issued for appointment of sole licensee for transportation business, applicant's tender accepted and work order issued. The applicant accordingly furnished requisite bank guarantee, concluded contract arose even though no formal contract signed. Syndicate Bank v R. Veeranna, (2003) 2 SCC 15: (2003) 5 Kant LJ 1, provision in contract that interest could be revised upwards on loans up to a certain percentage, the Supreme Court held that no prior notice for exercising this power was necessary. Bharat Forge Ltd v Onil Gulati, AIR 2005 Del 369, the suit was based on invoices and bills containing the terms of supply and other requisite terms the invoices were acted upon, accepted and paid partly. The claim for the rest of the amount was maintainable even in the absence of any writing. Oriental Insurance Co Ltd v Peacock Plywood (P) Ltd, AIR 2005 Cal 97, acceptance by bank to provide loan on the basis of documents of hypothecation etc. executed by the customer was held to be binding on the bank. But as no lender can be compelled to disburse loan, an action lies only for breach of contract.
  11. Sunil Chandra Mishra v State of Bihar, AIR 2016 Pat 47.

Under a hypothecation agreement, a unilateral right was given to the bank to refer any dispute to arbitration. No consent of the borrower was stipulated. The court said that in the absence of *consensus-ad-idem*, such clause could not be regarded as an arbitration clause.<sup>12</sup> In the same decision the court adopted the view that such a unilateral option is not unfair, unreasonable or against public policy. Financial institutions carrying on the business of collecting, investing, lending funds are well within their rights to carve out ways and means of settlement of commercial transactions with their borrowers.<sup>13</sup>

Where the highest bidder did not avail the opportunity given to him to retain property by making payment along with 10 per cent interest, it was held that there was no bona fide intention on the part of the bidder. The Authority could resume possession.<sup>14</sup>

### Contract as civil obligation

The law of contract confines itself to the enforcement of voluntarily created civil obligations. It does not cover the whole range of civil obligations. There are many obligations of civil nature, like those imposed by law or created by the acceptance of a trust, whose violation may be actionable under the law of torts or of trusts, or under a statute, but they are outside the field of contract. The law of contract is also not able to take care of the whole range of agreements. Many agreements remain outside its purview because they do not fulfil the requirements of a contract. In addition, there are some agreements which literally satisfy the requirements of a contract, such as proposal, acceptance, consideration, etc., but which do not catch its spirit and they are not enforced because it does not sound to be reasonable to do so. They are excluded under the legal device that the parties must not have intended legal consequences.

### PROPOSAL OR OFFER

A proposal and its acceptance is the universally acknowledged process for the making of an agreement. The proposal is the starting point. Section 2(a) defines “proposal” as follows:

When one person signifies to another his willingness to do or to abstain from doing anything, with a view to obtaining the assent of that other to such act or abstinence, he is said to make a proposal.

The person who makes the proposal is called the promisor or “offeror”, the person to whom it is made is called the proposee or “offeree” and when he accepts it, he is called a “promisee”. In the terminology of Section 2(c) “the person making the proposal is called the “promisor”, and the person

12. *U.N. Automobiles (P) Ltd v Bank of Baroda*, AIR 2016 Raj 41.

13. *Ibid.*

14. *HUDA v Kedar Nath*, (2015) 1 SCC 186: (2015) 1 SCC (Civ) 482.

accepting the proposal is called the “promisee”. In view of the above definition, a proposal is in the first place an expression of the offeror’s willingness to do or to abstain from doing something. Secondly, it should be made with a view to obtaining the assent of the offeree to the proposed act or abstinence.

### Communication of proposal

The first part of the definition of “proposal” lays emphasis upon the requirement that the willingness to make a proposal should be “signified”. To signify means to indicate or declare. In the traditional language of the law of contract, it means that the proposal should be communicated to the other party. The process of making a proposal is completed by the act of communicating it to the other party. Section 3 recognises the modes of communication:

**S. 3. Communication, acceptance and revocation of proposals.**—The communication of proposals, the acceptance of proposals, and the revocation of proposals and acceptances, respectively, are deemed to be made by any act or omission of the party proposing, accepting or revoking, by which he intends to communicate such proposal, acceptance or revocation, or which has the effect of communicating it.

Thus, a proposal may be communicated in any way which has the effect of laying before the offeree the willingness to do or abstain.<sup>15</sup> It may, for example, be done by words of mouth<sup>16</sup>, or by writing, or even by conduct.

### Implied proposals

A man frequently expresses his desire to do something or to get something done by his actions. “Words are not the only medium of expression. Conduct may often convey as clearly as words a promise, or an assent to a proposed promise.”<sup>17</sup> An offer and acceptance need not always be formal,

15. It is now settled law that a contract can come into existence between the parties by exchange of letters. *Ram Krishan Singhal v Executive Engineer*, ILR (1991) 1 Del 275. Followed in *SBI v Aditya Finance & Leasing Co (P) Ltd*, AIR 1999 Del 18 at p. 21, here a lease contract was inferred from correspondence and the minutes of the meeting between the parties. *Sumitra Kaulra v DDA*, 1996 AIHC 4373 (Del), an allotment of flats, on whatever basis, like by lot or otherwise, becomes effective from the date of communication to the allottee. If there is anything wrong in the process of allotment that can be questioned under writ jurisdiction.

16. *P. Syamala v R. Gopinathan*, (2004) 1 CTC 117, oral agreement for sale of property under which the seller received cheques for the price and encashed them. The agreement was held to be valid and not defeated by the subsequent registered sale agreement with a subsequent buyer. *Abdul Salam Sheikh Rahim v Sk Mehbob Sheikh Amir*, (2006) 3 Bom CR 700, alleged oral agreement for sale of tenanted premises to the tenant, premises sold to another at a higher price, subsequent sale held valid because there was no concluded oral contract, there were only negotiations, even the earnest was not paid and was only undertaken to be paid. *T. Jayaram Naidu v Yasodha*, AIR 2008 NOC 972 (Mad), an oral agreement for sale is valid and enforceable, proving such agreement may be difficult, but when proved, valid.

17. *Restatement, CONTRACTS*, American Law Institute, S. 21.

nor does the law of contract or of sale of goods require that consent to a contract must be in writing.<sup>18</sup> Offer and acceptance can be spelt out from the conduct of the parties which covers not only their acts but also omissions.<sup>19</sup> An offer which is expressed by conduct is called an "implied offer" and the one which is expressed by words, written or spoken, is called an "express offer". An acceptance may likewise be made expressly or impliedly. Section 9 declares:

**S. 9. Promises, express and implied.**—In so far as the proposal or acceptance of any promise is made in words, the promise is said to be express. In so far as such proposal or acceptance is made otherwise than in words, the promise is said to be implied.

A contract implied in fact requires meeting of minds. The courts have to refuse to read an implied term into a contract which is silent on the point or did not clearly indicate the nature of terms.<sup>20</sup>

A bid at an auction is an implied offer to buy. Similarly, stepping into an omnibus<sup>21</sup> and consuming eatables at a self-service restaurant, both create implied promises to pay for the benefits enjoyed. An illustration of a contract arising impliedly from conduct is *Upton-on-Severn RDC v Powell*.<sup>22</sup>

A fire broke out in the defendant's farm. He believed that he was entitled to the free services of Upton Fire Brigade and, therefore, summoned it. The Brigade put out the fire. It then turned out that the defendant's farm was not within free service zone of the Upton, which therefore, claimed compensation for the services. The court said: "The truth of the matter is that the defendant wanted the services of Upton; he asked for the services of Upton and Upton, in response to that request, provided the services. Hence the services were rendered on an implied promise to pay for them."

Similarly, where the charterer of a ship chartered for loading steel billets, instead loaded general merchandise, for which the rate of freight was higher, he was held to have done so under an implied promise to pay the higher rate;<sup>23</sup> where the time for which a ship was chartered expired, but the ship-owner did not call back the ship and it remained in use with the other party, the Supreme Court said that a silent agreement arose under which current

18. *P. Poppan v Karia Gounder*, (2002) 2 CHN 40, enforceability of oral contracts and examining whether time was of essence.

19. *Coffee Board v CCT*, (1988) 3 SCC 263: AIR 1988 SC 1487.

20. *Maharashtra Rajya Sahakari Kappos Utpadak Panan Mahasangha Ltd v Manga Bhaga Choudhary*, (2009) 3 Mad LJ 721.

21. *Wilkie v London Passenger Transport Board*, (1947) 1 All ER 258 (CA).

22. (1942) 1 All ER 220 (CA).

23. *Steven v Bromley & Son*, (1919) 2 KB 722 (CA). See also *Dinshaw and Dinshaw v Indoswe Engineers (P) Ltd*, AIR 1995 Bom 180: (1995) 3 Bom CR 548, the contractor having used B class pipes instead of C class, was allowed to recover the price for the material actually used. *Lubrizol (India) Ltd v Lubrizol Corpn, US*, (1998) 2 Bom CR 210, the expression "landed costs" was held impliedly to include customs and other duties.

charter rates became applicable;<sup>24</sup> where the customer of a bank did not object to the charge of a compound rate of interest in accordance with the usual course of business, he was held to have impliedly contracted to pay the compound interest;<sup>25</sup> and where the rules of a yacht club regatta provided that competitors would be liable for damage done by fouling, they were held bound to each other by the rules and where one of them fouled and sank a yacht, he was held liable.<sup>26</sup> This last mentioned case shows that in order to ascertain whether an agreement has arisen, regard must be had to the totality of the circumstances in which the parties contracted and not merely to the formalities of offer and acceptance. Sometimes a sequence of events may exhibit an agreement, though offer and acceptance are indiscernable.

This should be contrasted with a case in which a member of a Jockey Club sought to recover damages from his club for causing him loss of earnings by refusing him a racing licence on medical grounds. He based his contention on the contractual duty of the club of carrying out its licensing functions with care. The claim was struck out. The Jockey Club was a domestic tribunal and no contractual duty could be implied in respect of its functioning. The only obligation in such cases is to act fairly.<sup>27</sup>

Section 9 was applied by the Supreme Court in a case<sup>28</sup> where on the orders of a go between man certain goods were supplied by the plaintiff on his own account to the defendants. The defendants clearly and unerringly accepted the goods and paid a part of the price. Accordingly a liability to pay the balance arose. "The defendants by their clear conduct of accepting the goods and never repudiating any of the numerous letters and telegrams of the plaintiff demanding the money from them, clearly showed that a direct contract which in law is called an implied contract by conduct was brought about between them." In another matter before the Supreme Court the facts were:<sup>29</sup> A contract was signed between an Indian and a Yugoslavian party. One of the terms provided for arbitration by the International Chamber of Commerce in Paris. Immediately thereafter the Indian party cabled and also wrote its objection about the arbitration clause. The other party made no reply to it, but permitted the work to go on. A dispute having arisen, it was held that the arbitration clause had become deleted from the contract by an implied agreement. A suit could lie in a court of law. In another case of the same kind,<sup>30</sup> a harbour authority offered to an operator berthing facilities for his operations. Correspondence between the two followed with

24. *Bharat Petroleum Corp Ltd v Great Eastern Shipping Co Ltd*, (2008) 1 SCC 503: AIR 2008 SC 357.

25. *Haridas Ranchordas v Mercantile Bank of India Ltd*, (1919-20) 47 IA 17.

26. *Clarke v Earl of Dunraven (The Satanita)*, 1897 AC 59 (HL).

27. *Wright v Jockey Club*, The Times, 16-6-1995.

28. *Haji Mohd Ishaq v Mohd Iqbal and Mohd Ali & Co*, (1978) 2 SCC 493, 500: AIR 1978 SC 798.

29. *Ramji Dayawala & Sons (P) Ltd v Invest Import*, (1981) 1 SCC 80: AIR 1981 SC 2085.

30. *Thovensen Car Ferries v Weymouth Borough Council*, (1972) Lloyd's Rep 614.

a view to operate a service from there to another port. Subsequently, the port authorities attempted to withdraw their facilities. The operator was allowed to recover damages for breach of contract. The correspondence had already given rise to an implied agreement that the pro-offered facilities had been accepted. Where the parties conducted their business transactions on the basis of a clause in their agreement, it was held that that clause became embedded into their contract and they would not be heard to say that the clause was intended to be only a general term.<sup>31</sup>

Failure on the part of a hirer under a hire-purchase agreement to keep up the payment of instalments would enable the financier to resume possession of the material delivered under the contract, even if the contract contains no term to that effect. Such right is the result of a legal implication.<sup>32</sup> A valuer was engaged by a bank for evaluating properties offered by the borrower for the purpose of an equitable mortgage. There was nothing to indicate that the bank made any promise to pay him his professional fee. The practice, on the other hand, was that such fee was paid by borrowers. The bank was held not liable under any implied promise, nor for compensation under the *quantum meruit* principle.<sup>33</sup>

No implied contract to pay higher price was deemed to have arisen where the Government, being bound under a contract to supply material at fixed prices, supplied it at enhanced rate and someone on behalf of the contractor happened to accept the material.<sup>34</sup> In a contract for supply of specified quantity every month by the Government to a dealer, the court said that, because the date of supply was not prescribed, no term could be implied that supply should be made in the first week of the month. Supply made in the last week of the month was held to be not a breach of contract.<sup>35</sup>

An auction purchaser failed to deposit the balance amount. The auction seller could prove his loss by showing that he had to sell the machine at a lower price. But he neither pleaded nor proved any loss. He was not allowed to forfeit the earnest money.<sup>36</sup>

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31. *A.B.C. Laminart (P) Ltd v A.P. Agencies*, (1989) 2 SCC 163; AIR 1989 SC 1239. In *Tatung Electronic (S) Pte Ltd v Binatone International Ltd*, (1991) 3 CLJ 2339 (Singapore), the legal requirement of 45 per cent local content in televisions to be imported into UK was held to have become an implied term of the contract.
  32. *K.A. Mathai v Kora Bibbikutty*, (1996) 7 SCC 212. An unconditional acknowledgement of liability with nothing said to the contrary amounts to an implied promise to pay, *R. Kumar and Co v Chemicals Unlimited*, AIR 2001 Bom 116. Accordingly, a summary suit for recovery of the admitted amounts was allowed under Or. 37, R. 2, CPC.
  33. *SBI v T. Bardhan*, AIR 2011 Gau 68.
  34. *State of A.P. v Pioneer Construction Co*, AIR 1978 AP 281.
  35. *State of Kerala v K.D. Thomas*, 1996 AIHC 1339 (Ker); *ONGC Ltd v Essar Steel Ltd*, (2002) 2 Bom CR 379, a contract formulated through a tender, the formal contract could not be signed because certain clarifications were needed, but work order was issued and the work was completed. Arbitration proceeding commenced in terms of the contract. Award submitted thereunder was not allowed to be challenged on the ground that there was no formal contract.
  36. *Airport Authority of India v RR Singhal*, AIR 2012 Del 51.

### *Communication when complete*

**S. 4. Communication when complete.**—The communication of a proposal is complete when it comes to the knowledge of the person to whom it is made.

Obviously, therefore, an offer cannot be accepted unless and until it has been brought to the knowledge of the person to whom it is made. This principle enabled the Allahabad High Court in *Latman Shukla v Gauri Datt*<sup>37</sup> to deal with a matter involving a very crucial question on this point.



CASE PILOT

Defendant's nephew absconded from home. He sent his servant in search of the boy. When the servant had left, the defendant by hand bills offered to pay Rs 501 to anybody discovering the boy. The servant came to know of this offer only when he had already traced the missing child. He, however, brought an action to recover the reward. But his action failed.

Explaining the principle, BANERJI J said: "In my opinion a suit like the present can only be founded on a contract. In order to constitute a contract, there must be an acceptance of an offer and there can be no acceptance unless there is knowledge of the offer."

When this case was decided, the English Law on the point was uncertain. But the principle, that there can be no acceptance without knowledge of offer had already been adopted in the United States. For example, as early as 1868, a judge remarked: How can there be consent or assent to that of which the other party has never heard?<sup>38</sup> The principle has been carried a little further in an Australian case<sup>39</sup> where it was held that even if the acceptor had once known of the offer but had completely forgotten about it at the time of acceptance, he would be in no better position than a person who had not heard of the offer at all. One of the judges gave the following interesting illustration:

An offer of £100 to any person who would swim a hundred yards in the harbour on the first day of the year would not in my opinion be satisfied by a person who was accidentally or maliciously thrown overboard on that date and swam the distance simply to save his life, without any thought of the offer.

The facts of the case were:

The Australian Government had offered a reward of £1000 to anyone giving information about certain murderers. The offer further added that if the information was given by an accomplice, not being himself the murderer, he would also be entitled to a free pardon. The plaintiff, being an accomplice, saw the offer and having been so excited by the hope of

37. (1913) 11 All LJ 489 at p. 492.

38. See, *Fitch v Snedkar*, (1868) 38 NY 248 at p. 249.

39. *R. v Clarke*, (1927) 40 CLR 227.

pardon, he gave the information to save himself, completely forgetting the reward. He could not recover the reward.

Where a woman gave information about the murderers of her husband, not so much for reward, but to assuage her feelings, she was allowed to recover.<sup>40</sup> Where an offer has been accepted with knowledge of the reward, the fact that the informer was influenced by motives other than the reward will be immaterial.

### INTENTION TO CONTRACT

There is no provision in the Indian Contract Act requiring that an offer or its acceptance should be made with the intention of creating a legal relationship. But in English Law it is a settled principle that “to create a contract there must be a common intention of the parties to enter into legal obligations”.<sup>41</sup> It was pointed out in an early case that “contracts must not be the sports of an idle hour, mere matters of pleasantry and badinage, never intended by the parties to have any serious effect whatsoever”.<sup>42</sup> “It is not every loose conversation that is to be turned into a contract, although the parties may seem to agree.”<sup>43</sup> The case of *Balfour v Balfour*<sup>44</sup> has become well known as an illustration of this principle:

The defendant and his wife were enjoying leave in England. When the defendant was due to return to Ceylon, where he was employed, his wife was advised, by reason of her health, to remain in England. The defendant agreed to send her an amount of £30 a month for the probable expenses of maintenance. He did send the amount for some time, but afterwards differences arose which resulted in their separation and the allowance fell into arrears. The wife's action to recover the arrears was dismissed.

Lord ATKIN explained the principle thus: “There are agreements between parties which do not result in contract within the meaning of that term in our law. The ordinary example is where two parties agree to take a walk together, or where there is an offer and acceptance of hospitality. Nobody would suggest in ordinary circumstances that these arrangements result in what we know as contracts, and one of the most usual forms of agreement which does not constitute a contract appears to be the arrangements which are made between husband and wife. These arrangements do not result in contracts at all, even though there may be what would constitute consideration for the agreement. They are not contracts because parties did not intend that they shall be attended by legal consequences.”



CASE PILOT

40. See, King's Bench decision in *Williams v Carwardine*, (1833) 2 LJKB 101.

41. ATKIN J at p. 293 in *Rose & Frank Co v J.R. Crompton & Bros Ltd*, (1923) 2 KB 261 (CA).

42. *Dalrymple v Darlymple*, (1811) 161 ER 665, per Lord STOWELL.

43. Costigan, CASES ON CONTRACTS (3rd Edn.) 32.

44. (1919) 2 KB 571 at pp. 578–79.

### Family and social matters

The intention of the parties is naturally to be ascertained from the terms of the agreement and the surrounding circumstances. It is for the court in each case to find out whether the parties must have intended to enter into legal obligations. "In the case of arrangements regulating social relations it follows almost as a matter of course that the parties do not intend legal consequences to follow. In the case of agreements regulating business relations it equally follows almost as a matter of course that the parties intend legal consequences to follow."<sup>45</sup>

This does not, however, mean that in family or social matters there cannot be a legally binding contract.<sup>46</sup> All that the law requires is that the parties must intend legal consequences. *McGregor v McGregor*<sup>47</sup> is an early illustration of a binding engagement between a husband and wife. Here a husband and wife withdrew their complaints under an agreement by which the husband promised to pay her an allowance and she was to refrain from pledging his credit, the agreement was held to be a binding contract. An agreement between relatives to share a house has been held to be binding.<sup>48</sup>

The "principle applies to dealings between other relations, such as father and son and daughter and mother". These words occur in the judgment of DANCKWERTS LJ in *Jones v Padavatton*:<sup>49</sup>

A divorced woman was living in Washington with her son where she was employed as an assistant accountant in the Indian Embassy on attractive terms. Her mother was in Trinidad and wished her daughter to be near her. She was particularly attached to the grandson. The mother persuaded her daughter, much against her will, to leave service, to take legal education in England and finally to come back to Trinidad as a practising lawyer. The mother undertook to foot the expenses. Subsequently, the mother bought a house in England, part of which was allowed to the daughter and rest tenanted out. For five long years the daughter could not complete her education. She also remarried in the meantime. Differences arose between them and the mother stopped payments and also commenced proceedings to evict the daughter.

DANCKWERTS LJ allowed the mother's appeal. His Lordship said: "There is no doubt that this case is a most difficult one, but ... is one of those family arrangements which depend on the good faith of the promises which are made and are not intended to be rigid, binding agreements." SALMON LJ also allowed the mother's appeal, but on a different ground. He felt that

45. Per BANKES LJ at p. 282 in *Rose & Frank Co v J.R. Crompton & Bros Ltd*, (1923) 2 KB 261 (CA).

46. For example, the Supreme Court observed in *Chandrakant Manilal Shah v CIT*, (1992) 1 SCC 76: AIR 1992 SC 66 that a contract of any kind including that of partnership between the undivided members of a Hindu family is quite possible.

47. (1888) LR 21 QBD 424 (CA). See also *Pearce v Merriman*, (1904) 1 KB 80.

48. *Parker v Clark*, (1960) 1 WLR 286.

49. (1969) 1 WLR 328 (CA) at p. 620.

acting on her mother's promise, the daughter had left an attractive service and gone to another country for education and the mother could not in these circumstances get out of the promise at her sweet will and leave the daughter in that condition. The engagement, therefore, did result in a contract, but the agreement could last only for a period reasonably sufficient for the daughter to complete her education and the period of five years was more than sufficient for the purpose. She could not have expected her mother to support her, her son and husband in perpetuity.

The mere opening of a joint banking account between a man and his wife or the man promising to buy her a car in an effort to improve their strained matrimonial relationship has been held to be a purely domestic arrangement not resulting in any legal relationship.<sup>50</sup>

### Objectivity, not subjectivity, test of contractual intention

The test of contractual intention is objective, not subjective. What matters is not what the parties had in mind, but what a reasonable person would think, in the circumstances, their intention to be. Thus, where three ladies, two of them being mother and daughter and the third a paying guest, together made entries into a crossword puzzle in the name of the mother, the expenses being met by one or other, without any rules. The entry was successful and the mother refused to share the prize. But the court held that she was bound to do so, for any reasonable man looking at their conduct would at once conclude that they must have intended to share the prize.<sup>51</sup> Following these principles, the Supreme Court observed on the facts of a case:

Here, one partner has lent a large sum of money to the other to be utilised as capital in the partnership venture. The transaction is in the context of a commercial venture. The presumption is that legal obligations are intended. The onus is on the parties asserting the absence of legal obligations and the test is not subjective, but is an objective one. Where, as here, the tax implications of large financial obligations are sought to be put an end to, the burden is heavy on the assessee to establish that what would otherwise be the incidents of the transaction were excluded from contemplation by the parties.<sup>52</sup>

The court cited the following passage from an English case:<sup>53</sup>

In deciding whether or not there was any contract in relation to a certain transaction, or whether or not sufficient notice of a certain term was given, the law applies an objective and not a subjective test .... In the absence of such evidence, how can the court assume, that the master did not intend to enter into a contract.

50. *Spellman v Spellman*, (1961) 1 WLR 921 (CA).

51. *Simpkins v Pays*, (1955) 1 WLR 975.

52. *CWT v Abdul Hussain Mulla Muhammad Ali*, (1988) 3 SCC 562, per VENKATACHALIAH J.

53. *Bahamas Oil Refining Co v Kristiansands Tankrederie A/S*, (1978) 1 Lloyd's Rep 211. The court also cited *Edwards v Skyways Ltd*, (1964) 1 WLR 349 at p. 359 (QB).

The results of cases on this subject are bound to be variable, for the matter wholly depends upon the fact whether the conduct of the parties in the surrounding circumstances affords evidence of objective intention. For example, in *Merritt v Merritt*,<sup>54</sup> an agreement to transfer to the wife the beneficial ownership of the matrimonial home made at the time of separation was held to be binding. But in *Gould v Gould*,<sup>55</sup> an agreement similarly made was held to be not binding as the husband undertook to pay only as long as he had the means to pay. Uncertainty of these words showed that no legal relations were contemplated.<sup>56</sup>

### Business matters

In an agreement to provide loan facilities to a company's subsidiary, the company gave to the lender assurances of providing security by giving them two "letters of comfort", they being commercial papers, were held sufficient to create the responsibility of providing security. Taking into account the nature of the promise, the court held: "A letter of comfort from a parent company to a lender stating that it was the policy of the parent company to ensure that its subsidiary was 'at all times in a position to meet its liabilities' in respect of a loan made by the lender to the subsidiary did not have contractual effect if it was merely a statement of present fact regarding the parent company's intentions and was not a contractual promise as to the parent company's future conduct. On the facts, the relevant para of the letters of comfort was in terms a statement of present fact and not a promise as to future conduct and in the context in which the letters were written was not intended to be anything other than a representation of fact giving rise to no more than a moral responsibility on the part of the defendants to meet M's debt."<sup>57</sup> An investment in a partnership firm was taken by the Supreme Court to be of commercial nature putting the onus on the party asserting that he did not intend to be a legal partner to prove that fact.<sup>58</sup>

Even in business matters, parties intend to rely on each other's "good faith and honour," and not on the courts. For example, in *Rose & Frank Co v J.R. Crompton & Bros Ltd.*<sup>59</sup>

An exhaustive agreement was drawn between one American and two English firms for their dealings in paper tissues. The agreement contained the following clause: "This arrangement is not entered into as a formal legal agreement and shall not be subject to a legal jurisdiction in the law courts either in the US or in England." The agreement was terminated by

54. (1970) 1 WLR 211 (CA); noted, (1970) 86 LQR 436 at p. 437.

55. (1970) 1 QB 275; (1969) 3 WLR 490 (CA). Criticised (1970) JBL 113.

56. This result has been criticised. See, Ingram, *Intention to Create Legal Relations*, (1970) JBL 181; P.L. Bradbury, *Contractual Intent*, 120 New LJ 828.

57. *Kleinwart Benson Ltd v Malaysia Mining Corp*n, (1988) 1 WLR 799 (CA), going by the presumption of legal consequences in all commercial matters.

58. *CWT v Abdul Hussain Mulla Muhammad Ali*, (1988) 3 SCC 562 at p. 568.

59. (1923) 2 KB 261 (CA).

one of the parties contrary to its terms. The American firm brought an action for the breach. It was held that the document did not constitute a binding contract as there was no intention to affect legal relations.

“Intention to contract” said Lord ATKIN LJ, “may be negatived impliedly by the nature of the promise .... If the intention may be negatived impliedly, it may be negatived expressly .... I have never seen such a clause before, but I see nothing necessarily absurd in businessmen seeking to regulate their business relations by mutual promises which fall short of legal obligations, and rest on obligations of either honour or self-interest or perhaps both.”<sup>60</sup>

In another case, coupons were invited from persons generally showing certain entries and the correct entries were to be rewarded. There was a clause on the back of every coupon that the transaction would not give rise to any legal relationship, or be legally enforceable, but binding in honour only. No action was allowed either about the receipt of a coupon or the correctness of its particulars.<sup>61</sup>

A winner at a football pool sued for his winning, but was not allowed to recover because the pool was subject to a condition that it was not legally enforceable.<sup>62</sup> The practice, whereby workmen go to their place of business in a motor car or on the motor cycle of a fellow workman upon the terms of making contribution to the cost of transport, has been held not to result in a contract.<sup>63</sup> Stating the reasons UPJOHN LJ said: “The hazards of everyday life, such as temporary indisposition, the incidence of holidays, the possibility of a change of shift or different hours of overtime, or incompatibility arising, make it most unlikely that either contemplated that the one was legally bound to carry and the other to be carried to work.” In a subsequent case, it was pointed out that such an agreement should be held binding at least to the extent so as to enable the vehicle owner to recover the promised contribution from the other party.<sup>64</sup> Lord CROSS OF CHELSEA did not think it necessary that there should be positive evidence of intention to contract. He gave an illustration:

If I get into a taxi and ask the driver to drive me to the Victoria Station it is extremely unlikely that either of us directs his mind to the question whether we are entering into a contract. We enter into a contract not because we form any intention to enter into one but because if our minds were directed to the point we should as reasonable people both agree that we were in fact entering into one.

60. At p. 293. See also *Appleton v H. Littlewood Ltd*, (1939) 1 All ER 464 (CA); *Jones v Vernon's Pools Ltd*, (1938) 2 All ER 626, in both of which a clause providing that no legal relations should arise, was held to exclude all litigation. For a criticism of this English rule see, Tuck, (1943) 21 Canadian Bar Rev 123.

61. *Jones v Vernon's Pools Ltd*, (1938) 2 All ER 626.

62. *Appleton v H. Littlewood Ltd*, (1939) 1 All ER 464 (CA).

63. *Coward v Motor Insurers' Bureau*, (1962) 2 WLR 663 (CA).

64. *Albert v Motor Insurers' Bureau*, (1971) 3 WLR 291 (HL).

### Supreme Court's view of requirement of "intention"

The Supreme Court has expressed its reservation about the need of this separate requirement of "intention to contract" under the Contract Act. Going by the criticism which is already there in the West, the court found that it was a necessity of those systems where consideration was not a requisite of enforceability. Thus it is still an open question whether the requirement of "intention to contract" is applicable under the Indian Contract Act in the way in which it has been developed in England.<sup>65</sup>

But earlier to this, a limited recognition of the applicability of this principle in India could be inferred from the decision of the Supreme Court in *Banwari Lal v Sukhdarshan Dayal*.<sup>66</sup> In an auction sale of plots of land, a loudspeaker was spelling out the terms, etc., of the sale, one of the statements being that a plot of certain dimensions would be reserved for a Dharamshala (public inn). Subsequently, that plot was also sold for private purposes. The purchasers sought to restrain this. CHANDRACHUD J (afterwards CJ) said: Microphones... have not yet acquired notoriety as carriers of binding representations. Promises held out over loudspeakers are often claptraps of politics. In the instant case, the announcement was, if at all, a puffing up of property put up for sale.

In a subsequent case<sup>67</sup> on the subject, the Supreme Court noted the general proposition that in addition to the existence of an agreement and the presence of consideration there is also the third contractual element in the form of intention of the parties to create legal relations, and also noted that this proposition, though accepted in English Law, has not passed unchallenged. The court then cited the following passage from Cheshire and Fifoot's LAW OF CONTRACT:<sup>68</sup> "...the criticism of it made by Prof. Williston demands attention, not only as emanating from a distinguished American jurist, but as illuminating the whole subject. In his opinion, the separate element of intention is foreign to the common law, imported from the Continent by academic influences in the 19th century and useful only in systems which lack the test of consideration to enable them to determine the boundaries of contract."

### Letters of intent

A letter of intent merely indicates a party's intention to enter into a contract on the lines suggested in the letter. It may become a prelude to a contract. However, where a letter stated that it would be followed by a detailed purchase order which carried an arbitration clause, it was held that the letter

65. *CWT v Abdul Hussain Mulla Muhammad Ali*, (1988) 3 SCC 562 at p. 569.

66. (1973) 1 SCC 294.

67. *CWT v Abdul Hussain Mulla Muhammad Ali*, (1988) 3 SCC 562 at p. 569.

68. (10th Edn) 97.

was not a supply order and the arbitration clause contained in it did not by itself fructify into an arbitration agreement.<sup>69</sup>

### GENERAL OFFERS

It was suggested in the old case of *Weeks v Tybald*<sup>70</sup> that an offer must be made to a definite person. That case arose out of the defendant's affirmation to the public that he would give £100 to him that should marry his daughter with his consent. The plaintiff alleged that he did so and sued the defendant. Rejecting the action, the court said: "It is not averred nor declared to whom the words were spoken." The difficulty suggested was that if an offer of this kind addressed to several persons could be accepted, the offeror would find himself bound in innumerable contracts. This was, however, soon overruled. The modern position is that an offer may be made to the world at large. But the contract is not made with all the world. Contract is made only with that person who comes forward and performs the conditions of the proposal. The principle is thus stated in Anson: "An offer need not be made to an ascertained person, but no contract can arise until it has been accepted by an ascertained person."<sup>71</sup> An offer of this kind has already been seen in *Lalman Shukla v Gauri Datt*<sup>72</sup> which was addressed to the public generally. Another authority is *Carlill v Carbolic Smoke Ball Co (Smoke Ball case)*.<sup>73</sup>

A company offered by advertisement to pay £100 to anyone "who contracts the increasing epidemic influenza, colds or any disease caused by taking cold, after having used the ball according to printed directions". It was added that "£1000 is deposited with the Alliance Bank showing our sincerity in the matter". The plaintiff used the smoke balls according to the directions but she nevertheless subsequently suffered from influenza. She was held entitled to recover the promised reward.



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It was contended by the defendants that there was no intention to enter into legal relations as it was simply a puffing advertisement; that the offer was not made to any one person in particular and that the plaintiff had not communicated her intention to accept. The first argument was easily disposed of by BOWEN LJ by saying: "Was it intended that the £100 should, if the conditions were fulfilled, be paid? The advertisement says that £1000 is lodged at the bank for the purpose. Therefore, it cannot be said that the statement that £100 would be paid was intended to be a mere puff." His Lordship also exposed the fallacy of the argument that an offer could not be made to the world at large, when he said: "Why should not an offer be

69. *Dresser Rand S.A. v Bindal Agro Chemical Ltd*, (2006) 1 SCC 751: AIR 2006 SC 871, relying upon its own earlier decision in *Rajasthan Coop Dairy Federation Ltd v Maha Laxmi Mingrata Marketing Service (P) Ltd*, (1996) 10 SCC 405: AIR 1997 SC 66.

70. 1605 Noy 11: 74 ER 982.

71. Anson's LAW OF CONTRACT (23rd Edn by A.G. Guest, 1971) 40.

72. (1913) 11 All LJ 489.

73. (1893) 1 QB 256 (CA).

made to all the world which is to ripen into a contract with anybody who comes forward and performs the condition? It is an offer to become liable to anyone who, before it is retracted, performs the conditions, and although the offer is made to the world, the contract is made with that limited portion of the public who come forward and perform the condition on the faith of the advertisement.”

### Proposals acceptable by conduct

His Lordship also pointed out that in cases like this communication of acceptance is not necessary. “As notification of acceptance is required for the benefit of the person who makes the offer, he may dispense with notice to himself if he thinks it desirable to do so...and if he expressly or impliedly intimates in his offer that it will be sufficient to act on the proposal without communicating acceptance of it to himself, performance of the condition is a sufficient acceptance without notification. In the advertisement cases it seems to follow as an inference to be drawn from the transaction itself that a person is not to notify his acceptance of the offer before he performs the condition.... I advertise to the world that my dog is lost and that anybody who brings the dog to a particular place will be paid some money, are all the police and other people whose business is to find lost dogs to sit down and write me a note saying that they have accepted my proposal?”<sup>74</sup>

Section 8 of the Contract Act incorporates this principle:

**S. 8. Acceptance by performing conditions, or receiving consideration.**—Performance of the conditions of a proposal, or the acceptance of any consideration for a reciprocal promise which may be offered with a proposal, is an acceptance of the proposal.

The principle of the section was followed by YEARS CJ of the Allahabad High Court in *Har Bhajan Lal v Har Charan Lal*<sup>75</sup> and applied to a situation where the terms of a general offer were substantially, though not literally complied with.

A young boy ran away from his father's home. The father eventually issued a pamphlet, offering a reward in these terms: “Anybody who finds trace of the boy and brings him home, will get Rs 500.” The plaintiff was at the Dharamshala of a railway station, there he saw a boy, overheard part of the conversation, realized that the boy was the missing boy and promptly took him to the Railway Police Station and sent a telegram to the boy's father that he had found his son. It was held that the handbill was an offer open to the whole world and capable of acceptance by any person who fulfilled the condition, and that the plaintiff substantially performed the condition and was entitled to the amount offered.

74. At pp. 269–70 of *Carlill v Carbolic Smoke Ball Co*, (1893) 1 QB 256 (CA).

75. AIR 1925 All 539.

A Privy Council decision<sup>76</sup> is still another illustration of an offer which is accepted by acting upon its terms. Upon the marriage of the appellant, her aunt, Papamma, a wealthy Hindu widow with whom she had resided since childhood, promised that if the appellant and her husband would reside with her, she would purchase immovable property for the appellant. The appellant and her husband accordingly resided with the aunt. She did purchase some property but in her own name. This dissatisfied the appellant who with her husband ceased to reside with the aunt. The aunt wrote to the appellant that the property had been purchased for the appellant and would be transferred to her upon the writer's death. The appellant and her husband thereafter resided with the aunt until her death. This was held to be a sufficient acceptance of the promise contained in the aunt's letter:

The Board is of the opinion accordingly that there was here a completed contract. Papamma accomplished her desire, and she obtained the consideration which she had so much at heart. Acceptance of her terms and compliance with her stipulation were made.

It has been observed in a decision of the Patna High Court<sup>77</sup> that "where the acceptance is to consist of an act, as for example, despatching goods ordered by post, the rule is that no further communication of acceptance is necessary". Where the allotment of a quarter was to become a complete transaction on the making of the final payment, not to have done so brought about lapse of the allotment. Such allottee was not allowed to question the allotment of the quarter to another person.<sup>78</sup> In a claim against Railways for short delivery of goods, two cheques were dispatched to the claimant with this clarification that encashment of the cheques would be full and final satisfaction of the claim. The claimant encashed the cheques and subsequently protested and claimed the full claim amount. His claim application was dismissed.<sup>79</sup>

### General offer of continuing nature

Where a general offer is of continuing nature, as it was, for example, in the *Smoke Ball* case, it will be open for acceptance to any number of persons until it is retracted. But where an offer requires some information as to a missing thing, it is closed as soon as the first information comes in.

### OFFER AND INVITATION TO TREAT

An offer should be distinguished from an invitation to receive offers. When a man advertises that he has got a stock of books to sell, or houses to let, there is no offer to be bound by any contract. "Such advertisements are

76. *Malraju Lakshmi Venhavyamma v Venkata Narasimha Appa Rao*, (1915–16) 43 IA 138 at p. 146.

77. *State of Bihar v Bengal Chemical & Pharmaceutical Works Ltd*, AIR 1954 Pat 14.

78. *Ramesh Ramchandra Neware v Shanker Mahadeo Chefalkar*, (2004) 1 Bom CR 470.

79. *Bhagwati Prasad Pawan Kumar v Union of India*, (2006) 5 SCC 311: AIR 2006 SC 2331.

offers to negotiate—offers to receive offers—offers to chaffer.”<sup>80</sup> An offer is the final expression of willingness by the offeror to be bound by his offer, should the other party choose to accept it. This may be inferred from the definition of “proposal” in Section 2(a), which emphasises that there should be the expression of willingness to do or abstain with a view to obtaining the assent of the other. The offeror must have expressed his willingness to contract in terms of his offer with such finality that the only thing to be waited for is the assent of the other party. Where a party, without expressing his final willingness, proposes certain terms on which he is willing to negotiate, he does not make an offer, but only invites the other party to make an offer on those terms. This is perhaps the basic distinction between an “offer” and an “invitation” to receive offers. The Privy Council in *Harvey v Facey*<sup>81</sup> has explained the distinction.



The plaintiffs telegraphed to the defendants, writing: “Will you sell us Bumper Hall Pen? Telegraph lowest cash price”. The defendants replied, also by a telegram: “Lowest price for Bumper Hall Pen, £900”.

The plaintiffs immediately sent their last telegram stating: “We agree to buy Bumper Hall Pen for £900 asked by you.”

The defendants, however, refused to sell the plot of land at that price. The plaintiffs contended that by quoting their minimum price in response to the enquiry the defendants had made an offer to sell at that price. But the Judicial Committee turned down the suggestion. Their Lordships pointed out that in their first telegram, the plaintiffs had asked two questions, first, as to the willingness to sell and, second, as to the lowest price. The defendants answered only the second, and gave only the lowest price. They reserved their answer as to the willingness to sell. Thus, they had made no offer. The last telegram of the plaintiffs was an offer to buy, but that was never accepted by the defendants. “Their Lordships are of opinion that the mere statement of the lowest price at which the vendor would sell contains no implied contract to sell at that price to the person making the inquiry.”

The principle of this case was followed by the Supreme Court in *Col. D.I. McPherson v M.N. Appanna*.<sup>82</sup>

The plaintiff offered to purchase a lodge owned by the defendants for Rs 6000. He wrote the defendant’s agent asking whether his offer had been accepted and saying that he was prepared to accept any higher price if found reasonable. The agent replied: “Won’t accept less than rupees ten thousand”. The plaintiff accepted this and brought a suit for specific performance. It was held that the defendant did not make any offer or counter-offer in his cable but was merely inviting offers. There was no

80. *Carlill v Carbolic Smoke Ball Co*, (1893) 1 QB 256 (CA).

81. 1893 AC 552.

82. AIR 1951 SC 184: 1951 SCR 161. Followed in *Badri Prasad v State of M.P.*, (1971) 3 SCC 23: AIR 1970 SC 706. See also *Matanhells Bros v Shri Mahabir Industries (P) Ltd*, AIR 1970 Pat 91.

assent to the plaintiff's offer to buy at Rs 10,000 and, therefore, no concluded contract.

As distinguished from it where the proposee, in response to a proposal to purchase his land, asked for a higher price and also some advance with acceptance; the Court held that the proposer's acceptance, along with an advance payment amounted to a contract, although the proposee later revoked his offer.<sup>83</sup>

A Development Authority made an announcement for making an allotment of plots on first come first served basis on payment of full consideration. An application in response to this made with full consideration was held to be an offer and, therefore, there could be no concluded contract till the offer was accepted.<sup>84</sup>

### Catalogues and display of goods

A shopkeeper's catalogue of prices is not an offer; it is only an invitation to the intending customers to offer to buy at the indicated prices. "The transmission of a price list," observed Lord HERSCHELL, "does not amount to an offer to supply an unlimited quantity of the wine described at the price named, so that as soon as an order is given there is a binding contract to supply that quantity. If it were so, the merchant might find himself involved in any number of contractual obligations to supply wine of a particular description which he would be quite unable to carry out, his stock of wine of that description being necessarily limited."<sup>85</sup> For the same reason the display of goods in a shop with price chits attached is not an offer even if there is a "self-service" system in the shop. This was so held in *Pharmaceutical Society of Great Britain v Boots Cash Chemists Southern Ltd.*<sup>86</sup> Lord GODDARD CJ said: "It would be wrong to say that the shopkeeper is making an offer to sell every article in the shop to any person who might come in and that person can insist on buying any article by saying 'I accept your offer' .... In most bookshops customers are invited to go in and pick up books and look at them even if they do not actually buy them. There is no contract by the shopkeeper to sell until the customer has taken the book to the shopkeeper or his assistant and said: 'I want to buy this book' and the shopkeeper says 'yes'. That would not prevent the shopkeeper, seeing the book picked up, saying, 'I am sorry I cannot let you have that book; it is the only copy I have got and I have already promised it to another customer.' Therefore, I am of opinion, the mere fact that a customer picks up a bottle of medicine from the shelves in this case does not amount to an acceptance of an offer to sell. It is an offer by the customer to buy, and there is no sale effected until the buyer's offer to buy is accepted by the acceptance of the price."

83. *Byomkesh Banerjee v Nani Gopal Banik*, AIR 1987 Cal 92.

84. *Adikanda Biswal v Bhubaneshwar Development Authority*, AIR 2006 Ori 36.

85. *Grainger & Son v Gough*, 1896 AC 325, 334 (HL).

86. (1952) 2 QB 795 at p. 802, affirmed, *Pharmaceutical Society of Great Britain v Boot Cash Chemists (Southern) Ltd*, (1953) 1 QB 401: (1953) 2 WLR 427 (CA).



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A banker's catalogue of charges is also not an offer.<sup>87</sup> A railway timetable is in the same category.<sup>88</sup> Where a shopkeeper was convicted of offering for sale a flick-knife contrary to the Restriction of Offensive Weapons Act, 1959 [S. 1(1)] (UK) which he had displayed in his shop window, it was held that it was in no sense an offer for sale the acceptance of which could constitute a contract.<sup>89</sup>

### Announcement to hold auction

An auctioneer's announcement that specified goods will be sold by auction on a certain day is not an offer to hold the auction and he will not be liable to persons travelling up to the place if he changes his mind and does not hold the auction.<sup>90</sup> Indication of reserve price is neither a proposal to sell at that price nor it is a valuation of the property.<sup>91</sup> Even when an auction is held, the bid is not an acceptance so as to entitle the highest bidder to get the goods. The highest bid is nothing more than an offer to buy and it requires to be accepted by the auctioneer.<sup>92</sup> It does not matter for this purpose that the auction was held by the Government. Even a Government auction may be cancelled before any bid is finally accepted. After cancelling the auction (in this case the right to fell trees in a forest), the right was handed over to a Government corporation and it was considered to be no argument that a corporation cannot afford to pay an amount equal to private bidders. The Supreme Court also gave this latitude to the Government, as is enjoyed by a private auctioneer, that it may even ignore the highest bid and accept a lower bid. The highest bidder may be found to be an undesirable person for many reasons, for example, from the mere enormity of the bid.<sup>93</sup> However, one contractor should not be preferred over another without any rhyme or reason, this would be more so in the matter of Government contracts. Where out of the participating bidders or tenderers, any one is called to revise his

87. *State Aided Bank of Travancore Ltd v Dhirt Ram*, (1941–42) 69 IA 1: AIR 1942 PC 6.

88. In one English case, namely, *Denton v Great Northern Rly*, (1865) 5 E&B 860, the Railway company was held liable in damages for fraud in cancelling a train.

89. *Fisher v Bell*, (1961) 1 QB 394 (DC).

90. *Harris v Nickerson*, (1873) LR 8 QB 286. See also *Union of India v Gangadharan Mohandas*, (1997) 2 Cal LJ 221, cancellation of auction after due consideration, no bidder can claim anything under the doctrine of legitimate expectations.

91. *Anil Kumar Srivastava v State of U.P.*, (2004) 8 SCC 671: AIR 2004 SC 4299.

92. *Spencer v Harding*, (1870) 5 CP 561: 39 LJCP 332: 23 LJ 237.

93. *State of U.P. v Vijay Bahadur Singh*, (1982) 2 SCC 365: AIR 1982 SC 1234. A government contract is like any other contract between private parties and only those remedies are available for its breach as in other cases. Remedy by way of writ is not available for enforcing government contract, *State of U.P. v Bridge and Roof Co (India) Ltd*, (1996) 6 SCC 22: AIR 1996 SC 3515. An invitation for tenders required certain documents to be submitted. It was held that such documents could be submitted even afterwards. Tender should not be disqualified for that reason alone. *Mukul Kumar v Northern Rly*, AIR 1995 All 72. Strict compliance with ancillary or subsidiary conditions of tender not necessary. Such requirements can be complied with afterwards, *Jyoti Krishna Engineers v State Bank of Hyderabad*, AIR 1993 AP 327.

figure, an equal opportunity should be given to the highest bidder or the lowest tenderer,<sup>94</sup> provided there is otherwise nothing against him.

Fixation of reserve price in an invitation for submission of tenders has been held to be not an offer.<sup>95</sup>

### Definiteness of proposal

A classified advertisement to the effect: "cocks and hens 25s. each" has been held to be not an offer to sell.<sup>96</sup> Similarly, a letter which stated that the writer was prepared to offer for sale his estate for a certain price and allow reasonably sufficient time for verification of data and detail for the completion of the sale, was held to be not a definite offer.<sup>97</sup>

### Free distribution of articles

Where in pursuance of a scheme adopted by ESSO, the petrol station proprietors announced that they would give "the World Cup Coins", one for every buyer of four gallons of petrol, it was held that the distribution of the coins was not a contract of sale so as to attract the provisions of Purchase Tax Act, but was only a gift.<sup>98</sup>

94. *Desai & Co v Hindustan Petroleum Co*, 1984 Guj LH 864. The highest bidder cannot compel authorities to enter into contract with him. The authorities may decide not to go further with the matter, *Gajendra Singh v Nagarpalika Nigam*, AIR 1996 MP 10; *Sarita Karnwal v Meerut Mandal Vikas Nigam Ltd*, AIR 2012 Utr 30, rice mill running in loss put to sale, highest bidder negotiated with the government and made a higher bid. In the meantime, another company made a still higher bid, not accepted, 20 years lost since then government not compelled to accept. Valuation must have altered materially.

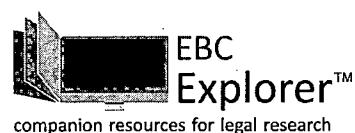
95. *Anil Kumar Srivastava v State of U.P.*, (2004) 8 SCC 671: AIR 2004 SC 4299.

96. *Partridge v Crittenden*, (1968) 1 WLR 1204.

97. *Clifton v Palumbo*, (1944) 2 All ER 497 (CA). See also *Bigg v Boyd Gibbins Ltd*, (1971) 1 WLR 913 (CA).

98. *Esso Petroleum Co Ltd v Commrs of Customs & Excise*, (1976) 1 WLR 1 (HL).

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The following cases from this chapter are available through EBC Explorer™:

- *Balfour v Balfour*, (1919) 2 KB 571
- *Carlill v Carbolic Smoke Ball Co*, (1893) 1 QB 256 (CA)
- *Harvey v Facey*, 1893 AC 552
- *Lalman Shukla v Gauri Datt*, (1913) 11 All LJ 489
- *Pharmaceutical Society of Great Britain v Boots Cash Chemists Southern Ltd*, (1952) 2 QB 795



# Acceptance

## DEFINITION

Section 2(b) defines acceptance as follows:

When the person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted. A proposal, when accepted, becomes a promise.

Thus “acceptance” is the assent given to a proposal, and it has the effect of converting the proposal into promise.<sup>1</sup>

## COMMUNICATION OF ACCEPTANCE

### Acceptance by external manifestation or overt act

The definition clearly requires that the assent should be signified. It may be signified or expressed by an act or omission by which the party accepting intends to communicate his assent or which has the effect of communicating it. [S. 3] A very common instance of an act amounting to acceptance is the fall of the hammer in the case of an auction sale. The principle is that there should be some external manifestation (*overt act*) of acceptance. A mere mental determination to accept unaccompanied by any external indication will not be sufficient. In the words of SHAH J (afterwards CJ):<sup>2</sup> “An agreement does not result from a mere state of mind: intent to accept an offer or even a mental resolve to accept an offer does not give rise to a contract. There must be... some external manifestation of that intent by speech, writing or other act.”

Such manifestation may be in the form of express words, written or spoken or may be signified through conduct. An illustration of acceptance by conduct is the decision of the House of Lords in *Brogden v Metropolitan Railway Co.*<sup>3</sup>



CASE PILOT

1. *Maharashtra Housing & Area Development Authority v Maharashtra State Human Rights Commission*, AIR 2010 Bom 104, an application for allotment of a flat does not by itself give a legal right for a flat to the applicant. Legal right arises only on issue of the letter of allotment. There can be no human right also earlier to that.
2. In *Bhagwandas Goverdandas Kedia v Girdharilal Parshottamdas & Co*, AIR 1966 SC 543; (1966) 1 SCR 656.
3. (1877) LR 2 AC 666 (HL).

B had been supplying coal to a railway company without any formal agreement. B suggested that a formal agreement should be drawn up. The agents of both the parties met and drew up a draft agreement. It had some blanks when it was sent to B for his approval. He filled up the blanks including the name of an arbitrator and then returned it to the company. The agent of the company put the draft in his drawer and it remained there without final approval having been signified. B kept up his supply of coals but on the new terms and also received payment on the new terms. A dispute having arisen B refused to be bound by the agreement.

The conduct of the company's agent in keeping the agreement in his drawer was an evidence of the fact that he had mentally accepted it. But he had not expressed his mental determination and retention of the agreement was not a sufficient acceptance. But the subsequent conduct of the parties in supplying and accepting coal on the basis of proposed agreement was a conduct that evidenced or manifested their intention. The final acceptance "was clearly given", said Lord CAIRNS LC "when the company commenced a course of dealing which is referable only to the contract and when that course of dealing was accepted and acted upon by B in the supply of coals".<sup>4</sup>

#### *Acceptance by conduct*

Another common example of acceptance by conduct is an action in terms of the offer. All cases of general offers, which are a kind of unilateral contract, demand some act in return for the promise to pay.<sup>5</sup> In express recognition of this principle Section 8 provides that "performance of the conditions of a proposal, of the acceptance of any consideration for a reciprocal promise which may be offered with a proposal, is an acceptance of the proposal". Such proposals demand acceptance by performance. Acceptance of money after prior information that higher rates of interest would be charged and retention of goods sent on approval amount to acceptance of the consideration offered along with a proposal.<sup>6</sup> A Canadian court has gone as far as to hold that, where an offer was made for the sale of a part of a land and lease of the other part subject to the condition that the offeree obtained planning permission and the offeree obtained permission within nine months, a valid contract arose, though no communication of acceptance had been made during the period of nine months.<sup>7</sup> "The offeror had indicated a particular

4. Where a proposal for supply of imported goods was already accepted by a telex message before the receipt of a standard form contract, it was held that the contract was already concluded and it was immaterial that the duly signed standard form was not returned, *Cotton Corp of India Ltd v Alagappa Cotton Mills*, AIR 2001 Bom 429: (2001) 3 Mah LJ 415.

5. *Carlill v Carbolic Smoke Ball Co*, (1893) 1 QB 256 (CA).

6. *Gaddar Mal v Tata Industrial Bank Ltd*, AIR 1927 All 407: ILR (1927) 29 All 674.

7. *Calgary Hardwood & Veneer Ltd v C.N.R. Co*, (1977) 4 WLR 18 (Alta SC); *Mukand Ltd v Hindustan Petroleum Corp*, (2005) 3 CLT 45 (Bom), bank guarantee forwarded for obtaining mobilisation advance, amounted to acceptance by conduct including arbitration, delay in issuing work orders, claim of escalation costs, reference to arbitration and award binding on parties.

mode of acceptance and, therefore, by doing the act, the offeree had accepted the offer and did not have to notify the offeror in advance of its intention to accept.”<sup>8</sup>

The position in India is the same. This appears from the decision of the Calcutta High Court in *Hindustan Coop Insurance Society v Shyam Sunder*.<sup>9</sup> After an oral understanding to insure and the completion of the medical examination, the company informed the proposer that if he submitted the proposal form and deposited the half-yearly premium, his proposal would be accepted. He accordingly submitted a cheque and the proposal. The company encashed the cheque but had not yet replied to him their acceptance of the proposal that the proposer died. The question was whether by encashing the cheque the company had accepted the proposal without there being the formal acceptance. HARRIS CJ referred to the English authorities and said:

Mere mental assent to an offer does not conclude a contract either under the Indian Contract Act or in English Law. The offeror may, however, indicate the mode of communicating acceptance either expressly or by implication both in India and English Law. In the case before us it is clear from the facts that the deceased indicated clearly the mode of acceptance of his proposal. The deceased indicated clearly that if the appellant accepted his proposal the cheque should be appropriated towards the first premium and that such appropriation would conclude the bargain. The cheque was received on that implied understanding.<sup>10</sup>

Where, on the other hand, the insurer had received the proposal form along with the first premium and it was still awaiting acceptance when the proposer died, no liability to pay arose. It was immaterial that the groundwork for acceptance was under preparation and the agent had assured that the proposal would be accepted.<sup>11</sup> Acceptance is complete only when

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8. Nicholas Rafferty, *Recent Developments in the Law of Contract*, (1978) 24 McGill LJ 239.
  9. AIR 1952 Cal 691. See further *Century Spg and Mfg Co Ltd v Ulhasnagar M.C.*, (1970) 1 SCC 582; AIR 1971 SC 1021: (1970) 3 SCR 854, a person acted on a representation held out by State.
  10. This should be contrasted with *LIC v Brazinha D'Souza*, AIR 1995 Bom 223, a proposal was received with premium amount which was kept in suspense for compliance of formalities. This did not amount to acceptance. No contract arose immediately. *LIC v Prasanna Devaraj*, AIR 1995 Ker 88, acceptance of cheque of premium, proposer died before consideration of the proposal by authorities, no contract. *LIC v Venkadaru Koteswaramma*, (2003) 1 Bankmann 152, signing of policy documents can be at a subsequent stage. In this case the proposal was accepted and medical was done. Acceptance arose, the proposer died within 5 days. *Elsa Tony Phillip v LIC*, AIR 2009 NOC 785 NCC: (2009) 1 ALJ 279, neither acceptance communicated, nor policy issued, mere encashment of the cheque did not amount to acceptance, insurer not liable to honour claim.
  11. *LIC v Vasireddy Komalavalli Kamba*, (1984) 2 SCC 719: AIR 1984 SC 1014. The company accepted the proposal and made the policy effective from 10.00 a.m. from 15-6-1998. An accident took place at 5.30 a.m. that very day. No liability under policy, *National Insurance Co Ltd v Geetha*, (2004) 1 CTC 401. Where the cheque issued for payment of first premium was dishonoured, the insurer was not liable to pay any claim laid by the insured himself and not by a third party, *National Insurance Co Ltd v Seema Malhotra*, (2001) 3 SCC 151: AIR 2001 SC 1197.

communicated to the offeror. Mere silence after receipt and retention of premium cannot be construed as acceptance.<sup>12</sup> The court followed the decision in *General Assurance Society Ltd v Chandmull Jain*<sup>13</sup> where it was observed that a contract is formed when the insurer accepts the premium and retains it. The decision further says that in the case of the assured, a positive act on his part by which he recognises or seeks to enforce the policy amounts to an affirmation of it.

It is clear that mere encashing the cheque sent along with the proposal cannot amount to be a concluded contract between the parties and it cannot be said that insurer has assumed risk because of the encashment of the cheque.<sup>14</sup>

Where the acceptance letter was issued alongwith the first premium receipt but it happened to be sent without knowing the fact of the proposer's death, the LIC was not allowed to disown its liability under the policy.<sup>15</sup>

Whether expressly or impliedly, the fact remains that acceptance has to be signified. In the words of BOWEN LJ:<sup>16</sup>

One cannot doubt that, as an ordinary rule of law, an acceptance of an offer made ought to be notified to the person who makes the offer in order that the two minds may come together. Unless this is done the two minds may be apart, and there is not that consensus which is necessary according to the English Law ... to make a contract.

### Communication to offeror himself

Further, acceptance must be communicated to the offeror himself. A communication to any other person is as ineffectual as if no communication has been made. To take, for example, *Felthouse v Bindley*:<sup>17</sup>

The plaintiff offered by means of a letter to purchase his nephew's horse. The letter said: "If I hear no more about the horse, I consider the horse mine at £33.15s." To this letter no reply was sent. But the nephew told the defendant, his auctioneer, not to sell the horse as it was already sold to his uncle. The auctioneer by mistake put up the horse for auction and sold it. The plaintiff sued the auctioneer on the ground that under the contract the horse had become his property and, therefore, defendant's unauthorised sale amounted to conversion. But the action failed.

The court said: "It is clear that the nephew in his own mind intended the uncle to have the horse, but he had not communicated his intention to the



CASE PILOT

12. *LIC v Annamma*, (1999) 3 KLT 142.

13. AIR 1966 SC 1644.

14. *Hiralaxmi v LIC*, (1999) 2 BC 118 (Bom DB).

15. *Omama Purushottaman Nair v LIC*, AIR 2005 Bom 152.

16. *Alexander Brogden v Metropolitan Rly Co*, (1877) LR 2 AC 666 (HL); *Sultan Sadik v Sanjay Raj Subba*, (2004) 2 SCC 377; AIR 2004 SC 1377, the contract of employment is also created by proposal and acceptance. Acceptance of the application for appointment must be communicated to the applicant who may then complete the contract by joining.

17. (1863) 7 LT 835.

uncle.” The case is also an authority for two further propositions. One of them is that the acceptance of an offer made should be communicated to the offeror himself or to the person he has authorised to receive the acceptance. A communication to a stranger, like the auctioneer in this case, will not do.

### *Offer cannot impose burden of refusal*

Secondly, an offeror cannot impose upon the offeree the burden of refusal. The offeror cannot say that if no answer is received within a certain time, the same shall be deemed to have been accepted. “It is not open to an offeror to stipulate against an unwilling offeree that the latter’s silence will be regarded as equivalent to acceptance. He cannot force him to take a positive course of action under penalty of being contractually bound if he does not.”<sup>18</sup>

### **Communication by acceptor himself**

The natural corollary of this principle is that the communication of acceptance should be from a person who has the authority to accept. Information received from an unauthorised person is ineffective. In *Powell v Lee*:<sup>19</sup>

The plaintiff was an applicant for the headmastership of a school. The managers passed a resolution appointing him, but the decision was not communicated to him. one of the members, however, in his individual capacity informed him. The managers cancelled their resolution and the plaintiff sued for breach of contract.

Rejecting the action the court observed: “There must be notice of acceptance from the contracting party in some way. Information by an unauthorised person is as insufficient as overhearing from behind the door.”

### **When communication not necessary**

In certain cases, however, communication of acceptance is not necessary. The offeror may prescribe a particular mode of acceptance, then all that the acceptor has to do is to follow that mode.<sup>20</sup> Then, there may be an offer which impliedly indicates that acting on its terms will be a sufficient acceptance. Announcement to pay reward for discovering a lost thing is an offer of this kind.<sup>21</sup> Again, the offeror may have acquiesced in a certain conduct on the part of the acceptor as equivalent to acceptance.<sup>22</sup> In such a

18. *Cotton Corp of India Ltd v Bombay Dyeing & Mfg Co Ltd*, (2006) 5 Bom CR 105, the term in the proposal that if it is not rejected up to a certain date, it would be deemed to have been accepted was held to be of no effect.

19. (1908) 24 TLR 606.

20. See, *State of Bihar v Bengal Chemical & Pharmaceutical Works Ltd*, AIR 1954 Pat 14.

21. See, for example, *Carlill v Carbolic Smoke Ball Co*, (1893) 1 QB 256 (CA); *Har Bhajan Lal v Har Charan Lal*, AIR 1925 All 539.

22. *Malraju Lakshmi Venkayyamma v Venkata Narasimha Appa Rao*, (1915-16) 43 IA 138.

case also no formal communication of acceptance is necessary.<sup>23</sup> Referring to the requirement of communication in *Carlill v Carbolic Smoke Ball Co*,<sup>24</sup> BOWEN LJ observed as follows:

But there is this clear gloss to be made upon that doctrine, that as notification of acceptance is required for the benefit of the person who makes the offer, he may dispense with notice to himself... and there can be no doubt that where the [offeror] expressly or impliedly intimates a particular mode of acceptance as sufficient to make the bargain binding it is only necessary for the other person to follow the indicated method of acceptance; and if the person making the offer expressly or impliedly intimates in his offer that it will be sufficient to act on the proposal without communicating acceptance of it to himself, performance of the condition is a sufficient acceptance without notification.

But there is this further gloss to be placed upon this principle that an offer can dispense with notification of acceptance that it applies only in cases of unilateral contracts as opposed to bilateral contracts. In a unilateral contract the offer demands an action, e.g., a reward for swimming across a river. The other party has only to perform the act and not to give a promise in return. Where the other party has to promise or undertake to do something, the requirement of the notification of his acceptance should not be allowed to be dispensed with. If, for example, in *Paul Felthouse v Bindley*<sup>25</sup> the nephew, without having replied to the uncle's letter, had asked his uncle to take away the horse and pay the price, the position of the uncle would have been curious, for, while the uncle could hardly have denied the promise, the nephew could always say at his convenience whether, by not communicating his acceptance, he had accepted the offer or not. It is for this reason that the law has in such cases always insisted upon an *overt act* (external manifestation) of acceptance than a mere mental determination. In a case of this kind before DENNING LJ,<sup>26</sup> a clause in the contract provided that the contract would be binding only when the other party put his signature upon it. His Lordship said:

Signing without notification is not enough. It would be deplorable if it were. The plaintiffs would be able to keep the form in their office unsigned, and then play fast and loose as they pleased. The defendant would not know whether or not there was a contract. ... Just as mental acceptance is not enough, nor is internal acceptance within the plaintiff's office.

In another case of the same kind,<sup>27</sup> a motor-cyclist was convicted for being with his motor cycle on a public road without third-party insurance.

23. For a further study of such contracts, see George P. Costigan, Jr., *Implied in Fact Contracts and Mutual Assent*, (1920) 33 Har L Rev 376.

24. (1893) 1 QB 256 (CA).

25. (1862) 142 ER 1037.

26. *Robophone Facilities Ltd v Blank*, (1966) 1 WLR 1428 (CA).

27. *Taylor v Allon*, (1966) 1 QB 304; (1965) 2 WLR 598.

His insurance had expired, but his company had sent him a temporary cover note. He had not accepted this and, therefore, at the relevant date there was no contract, though the temporary risk note was still in force. Lord PARKER, however, suggested that if he had taken out his motor cycle in reliance upon the temporary risk note that would have been sufficient acceptance by conduct without communication. Even this result would create the difficulty that while he could have saved his skin by showing the unaccepted temporary cover, he could always deny his liability to the company to pay the premium.

### Mode of communication

#### *Acceptance should be made in prescribed manner*

Acceptance has to be made in the manner prescribed or indicated by the offeror. An acceptance given in any other manner may not be effective, particularly where the offeror clearly insists that the acceptance shall be made in the prescribed manner. An American case illustrates this:<sup>28</sup>

A offered to buy flour from B requesting that acceptance should be sent by the wagon which brought the offer. B sent his acceptance by post, thinking that this would reach the offeror more speedily. But the letter arrived after the time of the wagon. A was held to be not bound by the acceptance.

What would have been the result if the mail had reached earlier than the wagon? According to Winfield<sup>29</sup> and Cheshire and Fifoot,<sup>30</sup> in that case the offeror would have been bound unless "he had an exclusive preference for reply by wagon". A minor departure from the prescribed mode of communication should not upset the fact of acceptance provided that the communication is made in an equally expeditious way, "for, in a case where the offeree was told to reply 'by return of post' it was said by the Court of Exchequer Chamber that a reply sent by some other method equally expeditious would constitute a valid acceptance".

Where the notice to exercise an option to purchase a building land was required to be sent by registered or recorded delivery post but it was sent by ordinary post and received within time, the court was of the opinion that the letter amounted to binding contract even though it was sent by ordinary post.<sup>31</sup>

This Anglo-American rule has, however, not been strictly followed in the Indian Contract Act. Section 7 deals with this matter.

**S. 7. Acceptance must be absolute.**—In order to convert a proposal into a promise, the acceptance must—

- (1) be absolute and unqualified,
- (2) be expressed in some usual and reasonable manner, unless the proposal prescribes the manner in which it is to be accepted. If the proposal

28. *Eliason v Henshaw*, (1819) 4 Wheaton 225.

29. Winfield, *Some Aspects of Offer and Acceptance*, (1939) 55 LQR 499, 515–16.

30. Cheshire and Fifoot, *LAW OF CONTRACT* (8th Edn, 1972) 40.

31. *Yates Building Co Ltd v R.J. Pedley & Sons (York) Ltd*, (1975) 237 EG 183.

prescribes a manner in which it is to be accepted, and the acceptance is not made in such manner, the proposer may, within a reasonable time after the acceptance is communicated to him, insist that his proposal shall be accepted in the prescribed manner, and not otherwise; but, if he fails to do so, he accepts the acceptance.

#### *Effect of departure from prescribed manner*

The section no doubt requires that acceptance should be made in the manner prescribed in the proposal. But a departure from that manner does not of itself invalidate the acceptance. A duty is cast on the offeror to reject such acceptance within reasonable time and if he fails to do so, the contract is clinched on him and he becomes bound by the acceptance. The section thus marks a visible departure from the English law and should, therefore, be read without reference to the English law on the subject.

English law is also now coming partly in line with Section 7. Article 7 of the Uniform Law on the Formation of Contracts for the International Sale of Goods, appended to the Uniform Laws on International Sales Act, 1967, contains the following provisions:

1. An acceptance containing additions, limitations, or other modifications shall be rejection of the offer and shall constitute a counter-offer.
2. However, a reply to an offer which purports to be an acceptance but which contains additional or different terms which do not materially alter the terms of the offer shall constitute an acceptance unless the offeror promptly objects to the discrepancy; if he does not object, the terms of the contract shall be the terms of the offer with the modifications contained in the acceptance.

It has been held by the Calcutta High Court<sup>32</sup> that where an offeror requires that the acceptance should be sent to a particular person, it "has to be read in a reasonable and in a sensible manner" and there was no violation of Section 7 when the offeree, instead of writing to the particular person, met him personally to communicate his acceptance. The defendant was bound by the acceptance.

There is however, one advantage to the acceptor in following the prescribed mode. By giving his acceptance in that mode, he has done all that the offeror required him to do and he is entitled to the contract, even if the acceptance does not reach the offeror.

#### *Where no manner prescribed: reasonable and usual manner*

Where no mode of acceptance is prescribed, acceptance must "be expressed in some usual and reasonable manner". Mail is, of course, a very reasonable manner in such cases. In England the rule is that where an offer

32. *Surendra Nath Roy v Kedar Nath Bose*, AIR 1936 Cal 87.

is received through post, acceptance may also be communicated by post. But in India, in view of the language of Section 7, post may be used as a mode of communication in all cases where it is reasonable, except when the offer requires a particular form of communication.

### When contract concluded (postal communication)

When the parties are at a distance and are contracting through post or by messengers, the question arises when is the contract concluded? Does the contract arise when the acceptance is posted or when it is received. The question first arose in England in *Adams v Lindsell*:<sup>33</sup>

On September 2, 1817, the defendants sent a letter offering to sell quantity of wool to the plaintiffs. The letter added "receiving your answer in course of post". The letter reached the plaintiffs on September 5. On that evening the plaintiffs wrote an answer agreeing to accept the wool. This was received by the defendants on September 9. The defendants waited for the acceptance up to September 8 and not having received it, sold the wool to other parties on that date. They were sued for breach of contract.

It was contended on their behalf that till the plaintiffs' answer was actually received there could be no binding contract and, therefore, they were free to sell the wool on 8th. But the court said:

If that were so, no contract could ever be completed by post. For if the defendants were not bound by their offer when accepted by the plaintiffs till the answer was received, then the plaintiffs ought not to be bound till after they had received the notification that the defendants had received their answer and assented to it. And so it might go on *ad infinitum* (endlessly).

The result of the decision is that a complete contract arises on the date when the letter of acceptance is posted in due course. This rule was affirmed by the Court of Appeal in *Household Fire & Accident Insurance Co v Grant*:<sup>34</sup>

The defendant in this case had applied for allotment of 100 shares in the plaintiff company. A letter of allotment addressed to the defendant at his residence was posted in due time, but it never reached the defendant. Nevertheless he was held bound by the acceptance.

THESIGER LJ stated the rule thus: "An acceptance which only remains in the breast of the acceptor without being actually and by legal implication communicated to the offeror, is no binding acceptance. ... But if the post be treated as the agent of both parties, then as soon as the letter of acceptance

33. (1818) 1 B&A 681: 106 ER 250 Court of King's Bench.

34. (1879) LR 4 Ex D 216 (CA). See also *Dunlop v Higgins*, (1848) 1 HLC 381, where an acceptance letter posted in due time was delayed by one day as the slippery state of roads from frost prevented the mail bag from reaching the station before departure of the train, nevertheless the defendants were held bound.

is delivered to the post office, the contract is made as complete and final and absolutely binding as if the acceptor had put his letter into the hands of a messenger sent by the offeror himself as his agent to deliver the offer and to receive the acceptance. ... The acceptor, in posting the letter has put it out of his control and done an extraneous act which clinches the matter, and shows beyond all doubt that each side is bound. How, then, can a casualty in the post office, whether resulting in delay, which in commercial transactions is often as bad as no delivery, or in non-delivery, unbind the parties or unmake the contract.”<sup>35</sup>

The Indian Contract Act, in Section 4 adopts a rather peculiar modification of the rule. According to the section, when a letter of acceptance is posted and is out of the power of the acceptor, the proposer becomes bound. But the acceptor will become bound only when the letter is received by the proposer. The section runs as follows:

**S. 4. Communication when complete.**—The communication of an acceptance is complete, as against the proposer, when it is put in a course of transmission to him, so as to be out of the power of the acceptor; as against the acceptor, when it comes to the knowledge of the proposer.

Thus the provision makes no difference in the position of the offeror. The offeror becomes bound when a properly addressed and adequately stamped letter of acceptance is posted. This aspect was emphasised by the Allahabad High Court in *Ram Das Chakrabarti v Cotton Ginning Co Ltd*.<sup>36</sup>

A letter of allotment of shares was claimed to have been posted by a company, but the applicant denied to have received it.

The High Court said: “It follows from this (Sections 4 and 5) that a notice of allotment, which is the acceptance of the offer to purchase shares, is communicated to the allottee when it is despatched, and from that moment there is a complete contract for him. Whether or not he receives the letter is absolutely immaterial.”<sup>37</sup> However, the company failed to furnish any evidence of the posting of the notice of allotment.

35. There was a strong dissenting judgment by BRAMWELL LJ. According to him if the communication of acceptance is complete at the time of posting, the same should be true of all communications sent through post. “Suppose,” he said, “a man has paid a tailor by cheque, and posts a letter containing a cheque to his tailor, which never reaches, is the tailor paid?... The question then is, is posting a letter which is never received a communication to the person addressed?” His Lordship answered by saying “that it is not a communication”. Many other problems illustrating the absurdity of the rule appear in the judgment of his Lordship. See, for example, the opinion of Lord BRAMWELL in *British & American Telegraph Co v Colson*, (1871) LR 6 Exch 108, where the defendant was held to be not bound by a letter of acceptance which was lost in the course of post. His Lordship said: “If a man proposed marriage and the woman was to consult her friends and let him know, would it be enough if she wrote and posted a letter which never reached him?” For other arguments against the rule, see Winfield, *Some Aspects of Offer and Acceptance*, (1939) 55 LQR 499, 510.

36. ILR (1887) 9 All 366. See also *J.K. Enterprises v State of M.P.*, AIR 1997 MP 68, communication of acceptance complete when letter posted to the address given by the offerer.

37. *Byomkesh Banerjee v Nani Gopal Banik*, AIR 1987 Cal 92, letter of acceptance duly posted

The contract is concluded at the place from where the proposal is accepted and communication of acceptance is despatched, i.e. the address at which the proposal was sent. The court at that place would have jurisdiction to entertain a cause of action under the contract.<sup>38</sup>

### *Difference between English and Indian laws*

The only difference that the section makes is in the position of the acceptor. In England when a letter of acceptance is posted, both the offeror and the acceptor become irrevocably bound. But in India, the acceptor does not become bound by merely posting his acceptance. He becomes bound only when his acceptance "comes to the knowledge of the proposer". The gap of time between the posting and the delivery of the acceptance can be utilised by the acceptor for revoking his acceptance by a speedier communication which will overtake the acceptance.<sup>39</sup>

The peculiarity of this rule is that after an acceptance is posted and before it comes to the knowledge of the offeror, only one party, that is, the offeror, is bound. The acceptor still has the right to recede from the contract by revoking his acceptance. A contract, on the other hand, means an agreement which binds both the parties to it.<sup>40</sup>

### *When parties in direct communication*

This rule, that the communication of an acceptance is complete as against the proposer when the letter is posted, is probably intended to apply only when the parties are at a distance and they communicate by post. In England also its operation has been confined only to cases where the post is used, and the illustration (b), appended to Section 4 also supposes communication by post. "Where, however, the parties are in each other's presence or, though separated in space", they are in direct communication, as, for example, by telephone, no contract will arise until the offeror receives the notification of acceptance. This appears from the speeches delivered in *Entores Ltd v Miles Far East Corporation*.<sup>41</sup> DENNING LJ observed as follows:

Let me first consider a case where two people make a contract by word of mouth in the presence of one another. Suppose, for instance, that I

by acceptor was held effective though the other party refused to receive it and it came back undelivered.

38. *ONGC v Modern Construction & Co*, (1997) 3 Guj LR 1855; *Progressive Constructions Ltd v Bharat Hydro Power Corp Ltd*, AIR 1996 Del 92; *Manohar v Saraswati Coop Housing Society Ltd*, (2005) 3 Mah LJ 297, allotment of a plot which had been completed by full payment, not allowed to be cancelled arbitrarily, without any show-cause notice.
39. S. 5, which provides that "an acceptance may be revoked at any time before the communication of its acceptance is complete as against the acceptor, but not afterwards".
40. This anomaly was pointed out by the Madras High Court in *Kamisetty Subbaih v Katha Venkataswami*, ILR (1903) 27 Mad 355, 359.
41. (1955) 2 QB 327; (1955) 3 WLR 48. *Trimex International FZE Ltd v Vedanta Aluminium Ltd*, (2010) 3 SCC 1; (2010) 1 SCC (Civ) 570, all communications made through e-mail, agreement thus arising was held to be valid, though there was no formal contract signed by the parties.



shout an offer to a man across a river or a courtyard but I do not hear his reply because it is drowned by an aircraft flying overhead. There is no contract at that moment. If he wishes to make a contract, he must wait till the aircraft is gone and then shout back his acceptance so that I can hear what he says. ... Now take a case where two people make a contract by telephone. Suppose, for instance, that I make an offer to a man by telephone and, in the middle of his reply, the line goes 'dead' so that I do not hear his words of acceptance. There is no contract at that moment.

The facts of the case were that an offer was made from London by telex to a party in Holland and it was duly accepted through the telex, the only question being as to whether the contract was made in Holland or in England. The Court of Appeal held that telex is a method of instantaneous communication and "the rule about instantaneous communications between the parties is different from the rule about the post. The contract is only complete when the acceptance is received by the offerer; and the contract is made at the place where the acceptance is received."<sup>42</sup>

Where, however, the proposal and acceptance are made by letters, the contract is made at the place where the letter of acceptance is posted. It has been observed by the Supreme Court that "authorities in India"<sup>43</sup> exhibit a fairly uniform trend that in case of negotiations by post the contract is complete when acceptance of the offer is put into a course of transmission to the offerer".<sup>44</sup> Thus where a premium due on a life insurance policy was sent by money order, it was held that the policy had revived from the date of the money order and not from the date of its receipt by the company. The assured having died in the meantime, his widow recovered the proceeds.<sup>45</sup>

Whatever merit this rule may have from the point of view of the assured or the offeree, it certainly makes the position of the offeror miserable. The current feeling, therefore, is that even in reference to postal communications the principle of consensus or "meeting of minds" should be adhered to and there should be no contract till the acceptance is received. Thus in *Holwell Securities Ltd v Hughes*<sup>46</sup> an option to purchase land was exercisable by notice, it was held that the mere posting of the notice which was never delivered was not a valid exercise of the option.

42. This was affirmed by the House of Lords in *Brinkbon Ltd v Stahag Stahl Und Stahlwarenhandelsgesellschaft M.B.H.*, (1983) 2 AC 34: (1982) 2 WLR 264 (HL), the contract was held to be made in Vienna where acceptance was received.

43. In *Sepulchre Bros v Sait Khushal Das Jagjivan Das Mehta*, AIR 1942 Mad 13, the Madras High Court held that although an acceptance by post is complete when the letter is posted, it is a continuing act until it reaches the person to whom it is communicated and thus can be taken to be made also at the place where it is received. But this opinion has not been followed.

See also *Baroda Oil Cakes Traders v Parshtottam Narayandas Bagulia*, AIR 1954 Bom 491.

44. SHAH J in *Bhagwandas Goverdhanadas Kedia v Girdharilal Parshtottamdas & Co*, AIR 1966 SC 543: (1966) 1 SCR 656.

45. *Hairoon Bibi v United India Life Insurance Co*, AIR 1947 Mad 122.

46. (1974) 1 WLR 155.



### Supreme Court approval of “Entores case”

The principle of the *Entores* case has been endorsed by the Supreme Court in *Bhagwandas Goverdhandas Kedia v Girdharilal Parshottamdas & Co.*<sup>47</sup> In this case, the plaintiffs made an offer from Ahmedabad to the defendants at Khamgaon to purchase certain goods and the defendants accepted the offer. The question was whether the conversation resulted in a contract at Khamgaon or at Ahmedabad. A majority of the judges (HIDAYATULLAH J [afterwards CJ]) (dissenting) preferred to follow the English rule as laid down in the *Entores case* and saw no reason for extending the post office rule to telephonic communications. SHAH J (afterwards CJ) felt that “Section 4 does not imply that the contract is made *qua* the proposer at one place and *qua* the acceptor at another place. The contract becomes complete... when the acceptance of offer is intimated to the offerer.” But, he continued to say, that the draftsman of the Indian Contract Act could not have envisaged use of telephone because it had not yet been invented and, therefore, the words of the section should be confined to communications by post.

HIDAYATULLAH J (afterwards CJ) was, on the other hand, convinced that though “the law was framed at a time when telephones, wireless, Telstar and Early Bird were not contemplated”, the language of Section 4 is flexible enough to cover telephonic communications. The courts should not completely ignore the language of the Act. When the words of acceptance are spoken into the telephone, they are put into the course of transmission to the offerer so as to be beyond the power of the acceptor. The acceptor cannot recall them. The communication being instantaneous the contract immediately arises.

Communication by fax is similar to communication by telex. Communication by fax is also instantaneous communication. If operates through telephone connection. The normal rule applies. Fax communication, like telephonic communication, becomes complete when the acceptance is received by the offeror.<sup>48</sup> The mere absence of a signed formal contract does not affect the unconditional acceptance of a proposal or implementation of the contract resulting from it. The unconditional acceptance of a contract through e-mail of an offer made through e-mail specifying the terms and conditions satisfied the requirements of Sections 4 and 7.<sup>49</sup>

### ABSOLUTE AND UNQUALIFIED

Section 7 provides:

In order to convert a proposal into a promise, the acceptance must be absolute and unqualified.

47. AIR 1966 SC 543: (1966) 1 SCR 656; *Pacific Refractories Ltd v Stein Heurtey India Projects (P) Ltd*, (2006) 3 Mah LJ 438: (2006) 4 Bom CR 311, letter posted from Calcutta accepting the offer, held, the contract must be deemed to have arisen there. A clause in the contract for exclusive Calcutta jurisdiction was held to be binding.

48. *Quadricron P Ltd v Bajrang Alloys Ltd*, (2008) 3 Mah LJ 407.

49. *Trimex International FZE Ltd v Vedanta Aluminium Ltd*, (2010) 1 SCC (Civ) 570.

### Counter proposals

“Any departure from the terms of the offer or any qualification vitiates the acceptance unless it is agreed to by the person from whom the offer comes. In other words, an acceptance with a variation is no acceptance; it is simply a counter-proposal, which must be accepted by the original promisor before a contract is made.”<sup>50</sup> The facts of the case in which this statement occurs were as follows:

Before accepting an offer the plaintiff introduced certain terms like ‘Free Bombay Harbour and interest’, which were not there in the original offer. This, the defendant refused to accept. Subsequently the plaintiff communicated his acceptance of the original offer, but the defendant did not assent to this. Plaintiff’s action for breach of contract was dismissed.

Sir JENKINS CJ said: “Unless there is an absolute and unqualified acceptance, the stage of negotiations has not yet passed, and no legal obligation is imposed.” The plaintiff’s first acceptance with new terms was in fact a counter offer which implied the rejection of the original offer. A counter offer puts an end to the original offer and it cannot be revived by subsequent acceptance. In another case:<sup>51</sup>

A offered by a letter to sell certain claims to B at a specified rate. B in turn offered to buy at a little less rate which A did not accept, but he did not withdraw his original offer. Then B accepted the rate as originally offered. This also A did not accept and B sued him for breach of contract. It was held that B by his counter-offer to buy at a reduced rate impliedly rejected A’s original offer and there was no contract.

The court relied upon *Hyde v Wrench*.<sup>52</sup> In this case an offer to sell a farm for £1000 was rejected by the plaintiff, who offered £950 for it. This was turned down by the offeror and then the plaintiff agreed to pay £1000. Holding that the defendant was not bound by any such acceptance, the court said: “The defendant offered to sell it for £1000, and if that had been at once unconditionally accepted, there would undoubtedly have been a perfect binding contract, instead of that, the plaintiff made an offer of his own, to purchase the property for £950 and thereby rejected the offer previously made by the defendant. It was not afterwards competent for him to revive the proposal of the defendant, by rendering an acceptance of it. Therefore, there exists no obligation of any sort between the parties.”<sup>53</sup>

50. Per Sir JENKINS CJ in *Haji Mohd Haji Jiva v E. Spinner*, ILR (1900) 24 Bom 510, 523; *Food Corporation of India v Ram Kesh Yadav*, (2007) 9 SCC 531; AIR 2007 SC 1421, a conditional offer has to be accepted or rejected with a counter-offer, the offeree cannot accept a part of it.

51. *Nihal Chand v Amar Nath*, AIR 1926 Lah 645.

52. (1840) 3 Beav 334.

53. See *Badrilal v Municipal Council of Indore*, (1973) 2 SCC 388; AIR 1973 SC 510.

Where the proposal carried an acceptance slip with certain conditions and said that the acceptance should be signed on the slip and not in any other manner and the offeree accepted by means of a separate letter without signing the slip, it was held that the acceptance was good because the offeror had to protest against such acceptance and he having not done so the conditions on the slip became waived.<sup>54</sup>

#### *Partial acceptance*

Acceptance should be of the whole of the offer. The offeree cannot accept a part of its terms which are favourable to him and reject the rest. Such an acceptance is another kind of counter-proposal and does not bind the offeror unless he agrees to the qualified acceptance. Thus, in a case:<sup>55</sup>

An application for certain shares in a company was made on the condition that the applicant would be appointed cashier in a new branch of the company. The company allotted him some shares without fulfilling the condition and claimed the share money.

It was held "that the petitioner's application for 100 shares was conditional and that he had no intention to become a member of the company when he applied for the shares until he was appointed a cashier in the branch office".<sup>56</sup>

#### *Inquiry into terms of proposal*

A mere inquiry into the terms of a proposal is not the same thing as a counter-proposal. In a negotiation for the sale of a quantity of iron, the proposal was "I would now sell for 40s. net cash, open till Monday". The offeree inquired by wire whether the offeror would accept 40s. for delivery over two months or less. The offeror, treating this as a rejection, sold off the goods. He was held liable for the breach. To seek an explanation of the terms is something different from introducing new terms.<sup>57</sup> An inquiry about the technical details of a proposal is not a counter-proposal. On acceptance of the proposal, the contract will be created on the basis of the terms and conditions of the original proposal including arbitration clause.<sup>58</sup>

54. *Compagnie de Commerce et Commission, SARL v Parkinson Stove Co Ltd*, (1953) 2 Lloyd's Rep 487.

55. *Ramanbhai M. Nilkanth v Ghashiram Ladliprasad*, ILR (1918) 42 Bom 595.

56. For another such case see *Mutual Bank of India Ltd v Sohan Singh*, AIR 1936 Lah 790. A person by accepting a part of the offer cannot say that a contract has been made and that the dispute should relate only to the unaccepted part of the offer. *General Assurance Society Ltd v LIC*, AIR 1964 SC 892; (1964) 2 SCR 125; (1964) 34 Comp Cas 10; *Technocom v Railway Board*, AIR 2009 Pat 15, acceptance of a part of tender by railways, not valid acceptance, a reservation or trinket acceptance, no acceptance in the eye of law, tenderer not liable for breach, earnest money has to be refunded.

57. *U.P. SEB v Goel Electric Stores*, AIR 1977 All 494.

58. *Fair Air Engineers (P) Ltd v N.K. Modi*, (1996) 6 SCC 385.

### Some instances

In a Karnataka case<sup>59</sup> a Government company drew out a scheme for procuring machinery on hire-purchase basis for small-scale firms. A firm requested the company to arrange for the supply of a machine of a particular maker. The company requested the maker to supply the machine to the firm along with agreement forms for signature. The firm received the machine but did not sign the forms. Even so it was held that a complete agreement had already arisen between the parties.

In another case,<sup>60</sup> an offeror asked the offeree to attend to everything else afterwards and send him 15 to 20 bags of areca nuts at once. The offeree wrote back that he would send the goods within 15 to 20 days. The offeror did not reply and ultimately about a month and a half later the offeree sent the goods. The court held that there was no absolute or unqualified acceptance within the meaning of Section 7(1). It was an order for immediate supply and the offeree by asking for 15 or 20 days' time had made a counter-proposal. This destroyed the original offer. Where a tender was accepted subject to a new stipulation that the contractor would have to provide supervisory staff as required by the Mines Act (35 of 1952), the acceptance was of no effect.<sup>61</sup>

Similarly, where a person asked to supply goods, accepted the offer, but subject to the payment of an advance, it was held that the demand for an advance was a new term and also an uncertain term because the amount was not specified and, therefore, prevented the contract from arising.<sup>62</sup> The court distinguished this case from another case where after receiving a counter-proposal, the offeror rejected it and repeated his original offer which was then accepted by the offeree, a contract was deemed to have arisen.<sup>63</sup> Where a landowner, on receiving a proposal, wrote back to the proposer to know whether he would offer a higher price and, if so, whether he would send some advance, and the latter accepted it by sending some advance, a contract arose leaving no chance for revocation.<sup>64</sup>

A person expressed a desire to purchase the Council house in which he was living. The Council sent him a letter which said "I refer to your request for details of the cost of buying your Council house. The Corporation may

59. *Shri Ram Metal Works v National Small Industries Corpn*, AIR 1977 Kant 24; *Union of India v Peeco Hydraulics (P) Ltd*, AIR 2002 Del 367, an offer containing an arbitration clause was accepted without protest and an attempt was also made to perform the contract. The acceptor was not allowed subsequently to object to the arbitration clause. *Bitin Bihari Singh v State of Bihar*, (2003) 3 BC 593, writ remedy not allowed for determining whether the quotation was 10 or 15 per cent below the Scheduled Rate. *Konark Uthasnagar Municipal Corpn v Commr, Uthasnagar MC*, (2003) 2 Bom CR 838, tender could not be accepted by a person who did not fulfil the eligibility criteria, criteria subsequently relaxed, the bidder became qualified, the court would not direct that any particular tender be accepted.

60. *Perala Krishnayyan Chettiar v Paimanathan Chettiar*, AIR 1917 Mad 63.

61. *Chhotey Lal Gupta v Union of India*, AIR 1987 All 329.

62. *Moolji Jaitha & Co v Seth Kirodimal*, AIR 1961 Ker 21.

63. *Pacific Minerals Ltd v Singhbbhum Mining Syndicate*, AIR 1938 Cal 343.

64. *Byomkesh Banerjee v Nani Gopal Banik*, AIR 1987 Cal 92.

be prepared to sell the house to you at the purchase price of £2180". He sent in an application and stated that he wished to buy the house. The issue before the House of Lords was whether the Council's letter amounted to an offer. It was held that this letter was not a contractual offer capable of being converted into a legally enforceable open contract by applicant's written acceptance of it.<sup>65</sup>

A written contract was executed between the parties for telecasting 65 episodes of a TV serial. Prior to this there was an oral approval by Doordarshan Authorities of the proposal to telecast 500 episodes. That approval was held to be only a part of the continuing negotiations. It could not have any effect because the parties subsequently bound themselves by a definite written contract.<sup>66</sup>

### Acceptance with condition subsequent

If an acceptance carries a condition subsequent, it may not have the effect of a counter-proposal. Thus, where an acceptance said: "terms accepted, remit cash down Rs 25,000 by February 5, otherwise acceptance subject to withdrawal", this was not a counter-proposal, but an acceptance with a warning that if the money was not sent the contract would be deemed to have been broken.<sup>67</sup> In another case, after invitation for and submission of tender, there were some negotiations between the parties. Acceptance was communicated to the tenderer by FAX stating that "a regular purchase order follows". The court said that this concluded the contract. The requirements of signatures of parties and collaborators and furnishing of bank guarantees for due performance were subsequent conditions. They were

65. *Gibson v Manchester City Council*, (1979) 1 WLR 294 (HL). See also *Rickmers Verwaltung GmbH v Indian Oil Corp Ltd*, (1999) 1 SCC 1: AIR 1999 SC 504, draft charter-party agreement executed between parties, but terms of letters of credit and performance guarantees could not be agreed upon. There was no concluded contract, arbitration clause could not acquire binding force. *Rajasthan SEB v Dayal Wood Works*, AIR 1998 AP 381: (1998) 2 ALD 599, security deposit made with tender. The tenderer's letter indicated terms and conditions of supply. Purchase orders issued by the Board contained additional terms and conditions which the tenderer did not accept. Held, no contract, security deposit refundable.
66. *Raj Chowdhury v Union of India*, AIR 2000 Cal 232. For interpretation of contracts and the importance in this context of prior negotiations, declarations of subjective intent, subsequent conduct of the parties in the surrounding circumstances, see McMeel Gerard, *Prior Negotiations and Subsequent Conduct, the Next Step towards Contractual Interpretation*, F.A. Trindade, "Reformation of the nervous shock rule", 2003 LQR 119, 272–97. The author discusses authorities on the orthodox limits on the materials which could be taken into account in contractual interpretation and the modern approach. He also examines cases on prior negotiations rule and subsequent conduct. *LIC v Machilipatnam Vankadaru Koteswaramma*, AIR 2003 AP 153, insurance, proposal submitted through an authorised agent of the corporation, administrative officer signed it in token of acceptance, examination by a panel doctor. All this amounted to acceptance before death. The court said that an inquiry by the LIC into the cause of death and subsequent repudiation of the policy showed existence of the policy.
67. *S.D. Katherine Stiffles v M.P. Carr Mackertich*, 164 IC 732. A letter of intent does not amount to a proposal or its acceptance. *Hermann Suerken Gmb & Co v Selco (Shipyard Pte) Ltd*, (1991) 3 CLJ 2289 Singapore HC.

not like a conditional acceptance or a counter-proposal. Communication of collaborators' approval was not necessary because the main tenderer was acting on their behalf.<sup>68</sup>

### Acceptance of counter proposal

Even "where the acceptance of a proposal is not absolute and unqualified the proposer may become bound, if, by his subsequent conduct, he indicates that he has accepted the qualifications set up".<sup>69</sup> Thus in *Hargopal v People's Bank of Northern India Ltd*:<sup>70</sup>

An application for shares was made conditional on an undertaking by the bank that the applicant would be appointed a permanent director of the local branch. The shares were allotted to him without fulfilling the condition. The applicant accepted the position as shareholder by accepting dividends, filing a suit to recover it and by pledging his shares.

It was, therefore, held, "that he could not contend that the allotment was void on the ground of non-fulfilment of the condition as he had by his conduct waived the condition".

When a counter-proposal is accepted, a contract arises in terms of the counter-proposal, and not in terms of the original proposal.

An offer to sell a machine contained a price variation clause whereby it was a condition of acceptance that goods would be charged at prices ruling at the date of delivery. The offeree placed an order for the machine in their form which did not contain any variation clause and which had a tear-off acknowledgement slip. The proposers signed and returned the slip. The machine was ready for delivery by September but the buyers could not accept it until November. The sellers invoked the price variation clause. The court did not permit it. The buyer's order was not an acceptance, but a counter-proposal, which the sellers accepted and that carried no price variation clause.<sup>71</sup>

Where tenders are invited subject to a deposit, it is open to the party inviting them to waive the requirement and an acceptance given to a tender without deposit would be binding on the tenderer.<sup>72</sup>

Where the tenderer modified the terms of his tender within the permissible period, but the modification was only partly accepted by the other side without the tenderer's consent, no contract arose. Earnest money could not be forfeited.<sup>73</sup>

68. *D. Wren International Ltd v Engineers India Ltd*, AIR 1996 Cal 424.

69. *Bhagwandas v Shri Dial*, 1913 Punj Rec. No. 92, p. 325.

70. AIR 1935 Lah 691. See also *Jawahar Lal Barman v Union of India*, AIR 1962 SC 378.

71. *Butler Machine Tool Co Ltd v Ex-Cell-O Corp (England) Ltd*, (1979) 1 WLR 401 (CA).

72. *Bismi Abdullah & Sons v FCI*, AIR 1987 Ker 56.

73. *D.S. Constructions Ltd v Rites Ltd*, 2006 AIHC 1835 (Del): (2006) 127 DLT 1.

### Provisional acceptance

An acceptance is sometimes made subject to final approval. A provisional acceptance of this kind does not ordinarily bind either party until the final approval is given. Meanwhile the offeror is at liberty to cancel his offer. The decision of the Punjab High Court in *Union of India v S. Narain Singh*<sup>74</sup> is an illustration in point. The court observed as follows:

Where the conditions of auction sale of liquor shop expressly provide that the acceptance of the bid shall be subject to the confirmation of the Chief Commissioner, there will be no complete contract till the acceptance of the highest bid is confirmed by the Chief Commissioner and the person whose bid has been provisionally accepted is entitled to withdraw his bid.

The bidder will have the right to withdraw his bid even where it is a condition of the auction sale that a bid which has been provisionally accepted cannot be withdrawn.<sup>75</sup> "Such a prohibition against withdrawal does not have the force of law unless there is some consideration to bind him down to the condition." In another case:<sup>76</sup>

A bid at an auction was accepted *kutcha pucca* and was referred to the owner of the goods for approval and sanction. The bidder was allowed to revoke his bid before the approval came in.

When a provisional acceptance is subsequently confirmed, the fact should be notified to the offeror, for it is only then that he becomes finally bound. An acceptance is not complete till communicated. A mere noting of acceptance in the auction file inside the office is not enough. Even if the bidder comes to know of that fact of his own, that will not do.<sup>77</sup> The Madras High Court, however, held in two cases,<sup>78</sup> that confirmation need not be notified. The court said: "The communication of acceptance twice, that is, once when the conditional acceptance is made and again when the condition is fulfilled is unnecessary." In Pollock and Mulla,<sup>79</sup> "it is submitted that these two cases were wrongly decided".

Where an offer for the sale of immovable property was accepted "subject to the condition that the title adduced should be to the satisfaction of the purchaser's solicitors", it was held that the offeror "must prove either that the solicitors did approve of the title or that there was such a title tendered as

74. AIR 1953 Punj 274. The auctioneer is not bound to accept the highest bid. See in connection with government contracts, *State of U.P. v Vijay Bahadur Singh*, (1982) 2 SCC 365: AIR 1982 SC 1234.

75. This was so held by the Madras High Court in *Somasundaram Pillai v Provincial Govt of Madras*, AIR 1947 Mad 366.

76. *Mackenzie Lyall & Co v Chamraooo Singh & Co*, ILR (1889-90) 16 Cal 702.

77. *DDA v Ravindra Mohan Aggarwal*, (1999) 3 SCC 172: AIR 1999 SC 1256.

78. *Rajanagaram Village Coop Society v P. Veerasami Mudaly*, AIR 1951 Mad 322.

79. INDIAN CONTRACT AND SPECIFIC RELIEF ACTS (9th Edn by J.L. Kapur, 1972) 76.

made it unreasonable not to approve of it".<sup>80</sup> Similarly, in *Koylash Chunder Doss v Tariney Churn Singhee*:<sup>81</sup>

The defendant accepted to buy the plaintiff's house for a specified price and called him to come to the attorney's house with title deeds and receive the earnest money. They met at the attorney's office in the absence of the attorney and no inspection of title deeds or payment of the earnest money, therefore, could take place.

CUNNINGHAM J observed: "If there be a distinct offer on one side, and a distinct acceptance on the other, a contract arises notwithstanding that the parties may have recorded their intention that it shall be put into a more formal shape by a solicitor. But, on the other hand, if on the true construction of the correspondence and evidence it appears to have been the intention of the parties that they are not to be bound till the agreement has been put into more formal shape and approved by them, then the parties ought not to be bound till the formal document has been executed." Applying this test to the facts of the present case the learned judge concluded that "both the parties having treated the payment of earnest money as an element in the contract, the contract could not be completed till the amount of earnest money had been ascertained".<sup>82</sup>

### Provisional or tentative arrangements

Thus, it is a question of fact in each case whether the parties intend to be bound by the provisional agreement or whether that is only a tentative arrangement. In *Winn v Bull*<sup>83</sup> the parties entered into an agreement for a lease "subject to the preparation and approval of a formal contract". When the final draft was prepared the parties could not agree on its terms. Holding that there was no contract, JESSEL MR said that this was an agreement subject to the terms being approved and the terms were not approved. Similarly, an agreement for the sale of a house stated that it is "subject to ! contract". The seller wrote to the buyer that he has signed the final agreement and would be glad to exchange it with the part of the contract which was to be signed by the buyer. the buyer thereupon sent the part signed by him but the seller changed his mind and refused to send his part in exchange. Lord GREENE MR held, for the Court of Appeal, that the agreement was subject to the parts being exchanged and, therefore, neither party was bound till the

80. *Treacher & Co Ltd v Mohomedally Adamji Peerbhoy*, ILR (1911) 35 Bom 110. *Rose Valley Real Estate & Construction Ltd v United Commercial Bank*, AIR 2008 Gau 38, deposit money not allowed to be forfeited on failure of the bidder to pay the balance money.

81. ILR (1884) 10 Cal 588.

82. R. *Elanchizhian v Secy to Govt of T.N.*, AIR 2008 NOC 973 (Mad), sale officer accepted plaintiff's bid, directed him to remit balance of the privilege amount and security deposit immediately, and to apply for liquor licence within seven days, failing which earnest money was to be forfeited, plaintiff not allowed to wriggle out.

83. (1877) 47 LJ Ch 139: (1877) LR 7 Ch D 29.

exchange actually took place.<sup>84</sup> His Lordship distinguished the case from his own decision in *Branca v Cobarro*.<sup>85</sup> An agreement for the sale of the lease and goodwill of a mushroom farm contained the terms of payment, a forfeiture clause and finally concluded: "This is a provisional agreement until a fully legalised agreement drawn up by a solicitor and embodying all the conditions herewith stated is signed." Lord GREENE MR held that the parties intended to be bound by this "provisional agreement" until it was replaced by a formal contract containing the same terms.

A tender was invited for settlement of sand *mahals*. The matter was provisionally settled with one of the tenderers. The relevant rule provided that the settlement order was to be treated as final only after 15 days. The tenderer received the order and revoked his tender the next day after receiving it. The court said that withdrawal took place before finality. No contract could arise and therefore there was no question of forfeiture of earnest money.<sup>86</sup>

The parties can make a contract with retrospective effect. The parties can say, "This contract is to be treated as applying, not only to our future relations, but also to what has been done by us in the past since the date of the tender in the anticipation of the making of this contract."<sup>87</sup>

### Acceptance and withdrawal of tenders and bids

A tender is in the same category as a quotation of prices. It is not an offer.<sup>88</sup> When a tender is approved, it is converted into a standing offer. A contract arises only when an order is placed on the basis of the tender. These

84. *Eccles v Bryant*, 1948 Ch 93 (CA); see also *Kollipara Sriramulu v T. Aswathanarayana*, AIR 1968 SC 1028: (1968) 3 SCR 387; *Union of India v Kishorilal Gupta & Bros*, AIR 1959 SC 1362: (1960) 1 SCR 493; *Jiwan Lal v Brij Mohan Mehra*, (1972) 2 SCC 757: AIR 1973 SC 559, where the purchaser paid earnest money, the balance being payable on registration of the deed, binding contract.
85. (1947) KB 854 (CA). See also the decision of the Supreme Court in *Badri Prasad v State of M.P.*, (1971) 3 SCC 23: AIR 1970 SC 706 and also *Rickmers Verwaltung GmbH v Indian Oil Corpn Ltd*, (1999) 1 SCC 1: AIR 1999 SC 504, arrangements could not go even up to the stage of letters of credit, no contract, arbitration clause could not be availed of.
86. *Homeswar Bora v State of Assam*, AIR 2010 Gau 167.
87. *Trollope & Colls Ltd v Atomic Power Constructions Ltd*, (1963) 1 WLR 333: (1962) 3 All ER 1035.
88. A tender which does not comply with the specified requirements is open to rejection. *N.O. Shetty v Karnataka SRTC*, AIR 1992 Kant 94, security deposit in the form of guarantee required for submitting a tender not complied with. Rejection of the tender upheld. *Sat Prakash Mehra v State of M.P.*, (1984) 29 MPLJ 318, a tenderer not permitted to complain that hand pumps to be installed were required to be approved by UNICEF; *P. Sreerama Reddy v Rajahmundry Municipality*, 1996 AIHC 2305 (AP), publication of tenders in violation of Municipal Rules, namely, non-publication in at least one local newspaper and the failure to give 15 days' time for submission, tender set aside. *Cambatta Aviation Ltd v Cochin International Airport Ltd*, AIR 1999 Ker 368, on the meaning and concept of a public tender. The requirements that tenderers must submit their tenders within a certain time on the last date, with bank guarantees with forfeiture clause, list of equipments, and statements of audited accounts, were held not to detract it from its being public tender.

principles were laid down by the Bombay High Court in the well-known case of *Bengal Coal Co Ltd v Homee Wadia & Co.*<sup>89</sup>

The defendants signed an agreement which, among other terms, provided: "The undersigned have this day made a contract with Messrs Homee Wadia for a period of 12 months for the supply of a kind of coal from time to time as required by the purchasers." Certain orders were placed and were complied with by the defendants. But before the expiry of 12 months they withdrew their offer and refused to comply with further orders. They were accordingly sued for breach of contract.

The court observed as follows:

"There is no contract, but simply a continuing offer, and that each successive order given by the plaintiffs under it was an acceptance of the offer as to the quantity ordered, and that thus the offer of the defendants and each successive order of the plaintiff together constituted a series of contracts. The defendants could not revoke their offer as to orders actually given, but except as to them, they had full power of revocation."<sup>90</sup>

Where purchase orders were issued in terms of an arrangement of supply but there was an option in the purchase order itself for the tenderer to refuse to supply, it was held that no concluded contract was made and therefore the contractor was entitled to refund of his security deposit.<sup>91</sup>

In reference to a tender the Supreme Court of India has observed: "As soon as an order was placed a contract arose and until then there was no contract."<sup>92</sup>

Also, "each separate order and acceptance constituted a different and distinct contract".<sup>93</sup> A tenderer can withdraw his tender before its final

89. ILR (1899) 24 Bom 97; *C. Jayasree v Commissioner M.C.H*, AIR 1994 AP 312, no contract till a tender is accepted. The tender inviting authority can cancel the tender before that. The tender provided that the corporation would accept a tender if the tenderer was willing to pay the entire bid amount within 60 days. The tenderer accepted this requirement in his tender, but even so the corporation could cancel the tender.
90. *Kalyanji Vithaldas & Sons v State of M.P.*, (1996) 10 SCC 762, revocation should reach before the order of acceptance is out of the hands of the other party. A revocation after receiving an order is of no effect. Overruling *Shiv Saran Lal v State of M.P.*, AIR 1980 MP 93: 1980 MPLJ 218; *K. Soosalrathnam v Civil Engineer, National Highway Circle*, AIR 1995 Mad 90, the last date for submission of tenders was declared to be a holiday, date became extended to the next working day automatically.
91. *Rajasthan SEB v Dayal Wood Works*, AIR 1998 AP 381: (1998) 2 ALD 599. Where one of the conditions of a tender was that after communication of acceptance, the tenderer must sign agreement papers, it was held that without such signature there was no concluded contract, *Lotus Constructions v Govt of A.P.*, AIR 1997 AP 200. Where the auction carried the stipulation that the acceptance of bid would be communicated through letter of intent and that would conclude the contract, held, contract arose on such communication in spite of the failure of the parties to sign formal papers because of differences in making some changes, *Progressive Constructions Ltd v Bharat Hydro Power Corp Ltd*, AIR 1996 Del 92.
92. *Chatturbhuj Vithaldas Jasani v Moreshwar Parashram*, AIR 1954 SC 236: 1954 SCR 817.
93. *Ibid*. See further *Dipak Kumar Sarkar v State of W.B.*, AIR 2004 Cal 182, right to accept or reject any tender without assigning any reason was reserved, no reasons were therefore required to be stated, no work order had been issued, no right accrued. Internal note sheets and notings had no face value. A tenderer having participated in the new tender could not



acceptance by a work or supply order even if there is a clause in the tender restricting his right to withdraw.<sup>94</sup> But once an order is placed that will have to be complied with. The order converts the tender into a contract: A tender which was filed along with a bank guarantee had to be accepted by the Authority within a certain time. The Authority asked the contractor for extension of time. The tenderer did not agree. The Authority then informed him that the contract was likely to be awarded to him. It was held that this did not amount to an acceptance of the tender. The bank guarantee was not absolute. An injunction against its encashment was granted.<sup>95</sup> Where a tenderer had revised his tendered rates before acceptance of his tender, but even so the Authority accepted his tender at the original tendered rates, it was held that no contract had arisen and, therefore, encashment of the bank guarantee was stayed.<sup>96</sup>

If you say to another, "If you will go to York, I will give you £100," that is in a certain sense a unilateral contract. He has not promised to go to York. But, if he goes, it cannot be doubted that he will be entitled to receive £100. His going to York at my request is a sufficient consideration for my promise. So, if one says to another, "If you will give me an order for iron, or other goods, I will supply it at a given price;" if the order is given, there is a complete contract which the seller is bound to perform.<sup>97</sup>

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complain of the cancellation of the earlier tender. Some guidelines have been provided in the Calcutta decision in *Aroma Enterprise v Murshidabad Zilla Parishad*, (2003) 2 ICC 745 (Cal), acceptance of highest or lowest bid cannot be the criteria of best deal by any State machinery, but rejection should be supported by reasons. Tenders should be opened under information to tenderers. An opportunity of revision should not be given to any selected tenderer. It can affect the rights of others. Quotation of a much less rate for a particular item as compared with the estimate of that item should not be a ground for rejection.

94. *Rajendra Kumar Verma v State of M.P.*, AIR 1972 MP 131. Where a tenderer communicated well in advance that he would not accept the work order unless certain changes in his tender document were permitted, it was held that no binding contract arose by accepting the tender without permitting the tenderer to introduce his modifications. *Arvind Coal & Construction Co v Damodar Valley Corpn*, AIR 1991 Pat 14; *Atma Singh v NTPC Ltd*, (1988) 2 An LT 421, right of withdrawal of tender even where the tender carried the condition that the tenderer would not withdraw the tender for 60 days. *Krishnaveni Constructions v Executive Engineer, Panchayat Raj, Darsi*, AIR 1995 AP 362, a stipulation that the tender would not be withdrawn for a certain period does not bind unless there is consideration for the promise not to withdraw. *Asia Tech Engineering Associates v Director General (Road Development)*, AIR 2010 Mad 54 (DB), tenders which remained unopened, opening having been postponed, their withdrawal was held to be justified.
95. *Kilburn Engg Ltd v ONGC Ltd*, AIR 2000 Bom 405. Another similar case is *Sekhsaria Exports v Union of India*, AIR 2004 Bom 35, a tender not accepted within reasonable time, tenderer withdrew much before acceptance, no contract, invocation of bank guarantee not proper.
96. *ONGC v Balaram Cements Ltd*, AIR 2001 Guj 287.
97. BRETT J in *Great Northern Rly Co v Witham*, (1873) LR 9 CP 16: 43 LJCP 1: 29 LT 471; *GPVREL-MEE (JV) v Govt of A.P.*, (2006) 3 ALD 703 (DB), a tender was submitted by two joint venturers but one of them withdrew from the venture, the Govt did not consider the tender because one of them was not qualified for tendering and by itself its annual business was not up to the requisite amount. The court cited *Goldstone Exports Ltd v Govt of A.P.*, (2003) 1 ALD 336; *Godavari Polymers (P) Ltd v Agricultural Products Commr*, (2004) 1 An LD 783, tender conditions have to be strictly complied with, be it at the pre-qualification stage or at the stage of consideration of bids.



A tender will, however, be irrevocable where the tenderer has, on some consideration promised not to withdraw it or where there is a statutory prohibition against withdrawal.<sup>98</sup> The Alberta Court of Appeal has gone a step further by holding that a term in the tender against withdrawal would be equally effective.

A construction contractor submitted a tender which stipulated that once the tender was opened, it would become irrevocable until such time as the contract had been signed by the successful tenderer. His tender was found to be the lowest, but prior to the award of the contract, he notified a clerical error resulting in a substantial underestimate. He offered to do the work for the tender as corrected (still the lowest tender). This was refused. The contract was awarded to the next lowest tenderer and he was sued for the difference between the two on the basis of the uncorrected tender.

He was held liable. The terms on which tenders were invited became a part of the offer and there was no obligation to accept the revised tender.<sup>99</sup> Explaining why such a clause is justified, the Bombay High Court said:<sup>100</sup>

“Municipal Corporation invites bids involving large financial implications and involving the interests of the community. Withdrawal of offers by bidders results in the escalation of costs of projects and also delays to the detriment of public interest. Hence, by demanding appropriate undertakings from bidders, it protects itself and also public interest. It is observed that the petitioner before it who withdrew part of his offer on the ground that quarry owner with whom he had contacted had declined to effect supply could not make grievance about forfeiture of tender deposit.”

Just as the tenderer has the right to revoke his tender as to future orders, so also the acceptor of the tender has a right to refuse to place any orders whatsoever. This appears from *Secy of State v Madho Ram*.<sup>101</sup>

98. See, *Secy of State for India v Bhaskar Krishnaji Samani*, AIR 1925 Bom 485: ILR (1925) 49 Bom 759, where certain rules prohibiting withdrawal of tenders framed under the provisions of the Indian Forest Act were held not to be *ultra vires*. *National Highways Authority of India v Ganga Enterprises*, (2003) 7 SCC 410: (2003) 4 ICC 786 where earnest money could be forfeited for refusing to enter into contract or for not performing it, the tenderer was allowed to withdraw the tender but could not ask for refund of earnest. *Omprakash & Co v City and Industrial Development Corp of Maharashtra Ltd*, (1994) 1 Bom CR 30: (1993) Mah LJ 1419; *State of A.P. v Singam Setty Yellamanda*, (2003) 2 An WR 154: AIR 2003 AP 182, suit for recovery of bid money allowed, Government could not claim damages because no loss was caused to it. *Bretton Woods Finlease Ltd v MTNL*, (2005) 125 DLT 69, black listing.

99. *Calgary v Northern Construction Co*, 1987 Construction Law Reporter 179 (Alberta CA).  
100. *Hasmukhlal and Co v Municipal Corp for Greater Mumbai*, (2005) 3 Mah LJ 149.

101. ILR (1929) 10 Lah 493; *Villayati Ram Mittal P Ltd v Union of India*, AIR 2011 SC 301, the tender stipulated for forfeiture of earnest money if the tender was revoked. The tenderer company revised its offer after making it. The court said that revision of an offer amounts to revocation of the original offer. Forfeiture of earnest money was proper.

A tender for the supply of certain goods at specified prices was accepted by the military authorities, but no requisition was issued during the period of the tender.

The court said: "The military authorities were not bound, by their acceptance of the tender, to purchase any or all of the said goods needed by them, from the plaintiff in the absence of a covenant to that effect. They were free to accept the offer or not as they would think fit and they could buy the goods from any other source without any reference to him." In other words, the party accepting a tender can always say: "We do not intend to give any further orders under this document and against such refusal there can be no remedy at all."<sup>102</sup>

It was pointed out by the Supreme Court in *Union of India v Maddala Thai*<sup>103</sup> that a clause in a tender authorising the party inviting tenders to terminate the contract at any time for future supplies does not destroy the very basis of the contract and the clause is valid.

A tender should be completed and submitted as required by its terms: Where signing of the tender document in full was one of the *requirements*, yet the tenderer did not sign it in full and only initialed it. Rejection of the tender was held to be not improper.<sup>104</sup> A tender contained instructions to bidders to state against each work item unit rates in Indian currency and in US Dollars or Japanese Yen. The tenderer stated 50 per cent of the unit rates in Indian currency and 50 per cent in foreign currency. This was held to be not a *clerical or mechanical error*. The tender was not allowed to be corrected. Errors in item rates were also not allowed to be rectified. Tender's request that errors should be ignored and his tender should be taken on the whole was ignored.<sup>105</sup>

Where the highest bidder who had already deposited the earnest money, participated in the auction, and deposited security money after approval of his tender, the court said that these were the relevant criteria for holding that there was a concluded contract. The execution of the formal contract is not the only criterion for the making of a contract.<sup>106</sup>

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102. Acceptance of bid money even though it was a part of the sale consideration was not an acceptance of the tender on final basis, *Veera Property Development (P) Ltd v T.N. Slum Clearance Board*, AIR 1999 Mad 304.
  103. (1964) 3 SCR 774: AIR 1966 SC 1724.
  104. *R.N. Ghosh v State of Tripura*, AIR 2000 Gau 114.
  105. *W.B. SEB v Patel Engg Co Ltd*, (2001) 2 SCC 451: AIR 2001 SC 682; *K.R. Rajaram v State*, 1999 AIHC 2585, the tenderer failed to deposit earnest money as required in the tender, he alleged oral promise giving him extended time for the deposit but failed to substantiate it, cancellation of the contract and forfeiture of the deposit were held to be justified. *Mega Enterprises v State of Maharashtra*, AIR 2007 Bom 156, conditions set by tendering authority cannot be questioned particularly by a bidder who participated in the process but was unsuccessful. The possible grounds could be that they were arbitrary, discriminatory and malafide.
  106. *Varghese v Divl Forest Officer*, AIR 2003 Ker 197: (2003) 1 KLT 892. *State of Maharashtra v A.P. Paper Mills Ltd*, (2006) 4 SCC 209: AIR 2006 SC 1788, withdrawal of bid before declaration of result. The tender was not withdrawable up to 45 days and no change of terms



### No obligation to accept tender or lowest tender

A party inviting tenders is not bound to accept any tender,<sup>107</sup> nor it is bound to accept the lowest tender. But where the party is a Government or any of its agencies, it should not arbitrarily pick and choose. It should have some rules and those rules must require reasons for departure from the normal principle to be recorded in writing. Accordingly, where an authority ignored the claim of the lowest tenderer because of his bad history and awarded the contract to the next lowest tenderer, the court did not interfere in the decision of the authority.<sup>108</sup> Explaining the principles which public authorities have to observe the court found it to be settled law that a public

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was allowable up to that time. Withdrawal before that period, valid forfeiture of earnest money. Failure to declare the result within the stipulated period was held to be not material. *State of Haryana v Malik Traders*, (2011) 13 SCC 200: (2012) 3 SCC (Civ) 429, a bid at an auction was not allowed to be withdrawn before the expiry of 90 days which was one of the conditions of the auction process. *Villayati Ram Mittal (P) Ltd v Union of India*, (2010) 10 SCC 532, after acceptance of tender, the tenderer wanted to change his rates bringing about revision of his quotation, held, this amounted to revocation of his tender justifying forfeiture of earnest money.

107. *Deepak Kumar Sarkar v State of W.B.*, AIR 2004 Cal 182, there was a clause in the tender documents for rejection or acceptance of any tender without assigning any reason. No liability for not accepting any tender. *Cama Hotels Ltd v Airports Authority of India*, AIR 2004 Guj 349, no *mala fide* shown in the withdrawal of a tender by Authorities, a mere apprehension on the part of the petitioner that this was done to favour his business rival was not sufficient to warrant interference by writ petition.
108. *N. Kunhiraman v Municipal Council*, (1992) 1 K LJ 191. See also *Suriya Das v Assam State Fisheries Devp Corpn Ltd*, 1995 AIHC 3617 (Gau), lowest tenderer ignored because he had not complied with the terms and conditions of the contract on an earlier occasion. *State of U.P. v Raj Narain*, (1975) 4 SCC 428: AIR 1975 SC 865, the authority ought to have recorded reasons for rejecting the tender which quoted the lowest price. In a tender for supply of drugs the decision to accept was to be that of the Minister of Commerce who reviewed the decision to accept the lowest tender, there was no *mala fide* and review was due to recommendation of the tender advisory committee, upheld, *Nestor Pharmaceuticals (P) Ltd v Union of India*, AIR 1995 Del 260. After negotiations with the lowest tenderer and others, Government preferred a Government undertaking under a statutory right of preference, no interference, *Babu Ram Gupta v Mahanagar Telephone Nigam Ltd*, AIR 1995 Del 223; *Red Rose Coop Labour and Construction (LOC) Ltd v State of Punjab*, AIR 1999 P&H 244, a tender was issued twice for the same items. Nobody was awarded after the initial tender. The quotations in response to the second tender showed that the petitioner had quoted lowest rates in the first tender in respect of 12 items. On that basis he was not allowed to claim award of contract in respect of those items. *Sri Sankaranarayana Construction Co v Konkan Rly Corpn Ltd*, (2004) 2 Bom CR 676, the obligation ordinarily is to accept the lowest tender. *Shree Gopal Bhagwan Das v State of Bihar*, (2004) 2 BLJR 1311 (Pat) failure to comply with the mandatory requirement of depositing the earnest money, tender ought not to have been accepted. *Ramana Dayaram Shetty v International Airport Authority of India*, (1979) 3 SCC 489: AIR 1979 SC 1628, tender of a person who does not fulfil the requisite qualification prescribed by the notice of tender cannot be accepted. *Maa Bindia Express Carrier v North-East Frontier Railway*, (2014) 3 SCC 760, bidder cannot insist that his bid should be accepted. All that the participating bidders are entitled to is fair, equal and non-discriminatory treatment. The court can examine whether the aggrieved party has been treated unfairly or discriminated against to the detriment of public interest. *Bhartiya State Bank v Bhanjan Singh*, 2014 SCC OnLine Chh 52: AIR 2015 Chh 15, the document of acknowledgement also carried an expression to pay the time-barred debt. Thus, it became a promise to pay. Dismissal of the suit was not proper.

authority cannot act arbitrarily even in the matter of awarding contracts or distributing largesse. There ought to be a public element in all its decisions and it must conform to the mandate of Article 14 and observe tenets of equality and fair action. The court said that the acceptance of a higher tender does not *ipso facto* make the acceptance illegal. A sixteen member elected council had taken the decision in accordance with the rules. The court continued:

“Even if two views are possible, there will be no justification for interference unless the view adopted by the authority is so grossly unreasonable or tainted by other vitiating circumstances.

The view does not become unreasonable, merely because another view would arise on the facts. The process of judicial review is not in the nature of an appeal against the decision. Only the decision-making process, is under review. Neither the view of the Municipality on facts, nor its assessment of future events based on past performance, can be labelled unreasonable. As observed by Lord HAILSHAM, two reasonable persons can perfectly reasonably come to opposite conclusions on the same facts, without forfeiting their title to be regarded as reasonable men. Unless the decision is so unreasonable that no reasonable person would come to it, it does not merit interference. As observed by the Court of Appeal in the *Tamside* case:<sup>109</sup> ‘No one can be properly labelled as being unreasonable, unless he is not only wrong, but so unreasonably wrong that no reasonable person could sensibly take that view’.

It is also useful to refer to the observations of SCARMAN LJ in *Nottinghamshire County Council R v Secy of State for Environment, Exp*:<sup>110</sup> ‘Unreasonableness must *prima facie* show that the official behaved absurdly or must have taken leave of his senses’.

The decision of the Municipal Council must be tested on the touchstone of these principles. The decision is not under appeal and the tenability

109. *Secy of State for Education and Science v Tameside Metropolitan Borough Council*, 1977 AC 1014; (1976) 3 WLR 641; *Pradeep Timber Co v H.P. State Forest Corp*n, 1984 Sim LC 245, cancellation of an auction so as to defeat the highest bidder and which had no other justification, cancellation quashed.

110. 1986 AC 240: (1986) 2 WLR 1 (HL). See also *Malu Khan v State of Rajasthan*, (1989) 1 Raj LR 890 where the highest bidder was ignored and the allotment of the liquor licence was being negotiated with a person who had not submitted the bid but who was offering more than the next highest bid, it was held that the next highest bidder should have been given opportunity to appear in negotiations. *Agarwal Roadlines (P) Ltd v Indian Oil Corp*n Ltd, (2003) 1 Bom CR 495, tender rejected because the tenderer by some mistake happened to submit the earnest money amount in the name of some other company. The court said that administrative decisions based on hypertechnical approach treating a non-essential condition as an essential condition was liable to be interfered with. The court followed Supreme Court authorities one of which was *Poddar Steel Corp*n v *Ganesh Engg Works*, (1991) 3 SCC 273: AIR 1991 SC 1579, where the Supreme Court did not uphold the sidelining of a tender on the ground that the earnest money draft was required to be that of the State Bank whereas the tenderer submitted a certified cheque of another bank. The court found the cheque to be equally safe. It could have been accepted by the authority by waiving the requirement because it was in their interest to get the highest bidder.

of another view will be no ground to stamp the decision with vice. As already noticed, the past performance of the petitioner-contractor, and the reports made by competent Authorities were considered and decision taken by an elected body of sixteen persons, after deliberation. The decision is not unreasonable."

Another case of this kind was before the Kerala High Court in *Cambatta Aviation Ltd v Cochin International Airport Ltd.*<sup>111</sup> The evaluation authority considered all the aspects and found the appellant to be the most competent tenderer to be awarded the contract. The Board of Directors selected another tenderer (the respondent). This decision was taken by the Board even before taking a decision on the soundness of the other tenderers. The minutes of the Board meeting did not give any reason as to why the Board decided to invite the respondent. The respondent was then persuaded to make a matching offer with that of the appellant. The court declared that the Board of directors adopted a procedure which was clearly violative of the principles of natural justice. The award was accordingly held to be arbitrary and illegal.<sup>112</sup>

A bidder at an auction acquires no vested right in the property under auction until his bid has been accepted. The mere deposit of 20 per cent of the bid amount by the highest bidder does not amount to acceptance of his bid. Communication of acceptance of his bid to the highest bidder is necessary for concluding the contract.<sup>113</sup>

Where there was nothing on record to show favouritism,<sup>114</sup> the court refused to interfere and cited the following Supreme Court statement:<sup>115</sup>

111. AIR 1999 Ker 368.

112. Still another similar ruling is in *Lanco Constructions Ltd v Govt of A.P.*, AIR 1999 AP 371, it was a tender for a World Bank Project. The lowest tender was rejected by the Government without giving any reasons. The World Bank also noted that the rejection of the lowest bid was without any convincing reasons and, therefore, not fair and reasonable. The decision was liable to be set aside because it was based upon incorrect information. *Chandragiri Construction Co v State of Kerala*, (2003) 1 KLT (SN) 14, negotiating with one of the tenderers behind the back of others, held arbitrary. *Sandhu Tractors v Orissa Small Industries Corp Ltd*, (2004) 4 BC 60 (Ori), public interest being paramount in the tendering process, there should be no arbitrariness in award of contracts, all tenderers should be treated alike. *Gupta Enterprises v Govt of A.P. Revenue & Endowments Deptt*, (2003) 2 BC 4 (AP), scope of judicial review of administrative action in award of contracts is much limited. *Kaikkara Construction Co v Govt of Kerala*, (1999) 2 BC 338 (Ker DB), decision of the single judge upsetting the award of a contract work without inviting tenders from public was held to be illegal and was set aside. There were no vitiating circumstances. *Coal India Ltd v Indian Explosives Ltd*, (2006) 3 CHN 433, a contract of sale or supply of goods to the State, no element of public interest in it so as to enable the State to exercise any superior power.

113. *U.P. Avas Evam Vikas Parishad v Om Prakash Sharma*, (2013) 5 SCC 182: (2013) 2 SCC (Civ) 737.

114. *Arun Kumar Agarwal v Bihar State Food Civil Supply Corpn*, (2005) 1 BLJR 29 (Pat).

115. *Tata Cellular v Union of India*, (1994) 6 SCC 651; *Jaykrishna Industries Ltd v Economic Development Corpn*, (2005) 4 Bom CR 218 scope of judicial review is confined to the processing of tenders so as to ensure that powers are not abused, there can be no interference in matters of business. *Hasmukhlal and Co v Municipal Corpn for Greater Mumbai*, (2005) 3 Mah LJ 149, forfeiture of earnest money in accordance with a clause in the contract but black

“It cannot be denied that the principles of judicial review would apply to the exercise of contractual powers by Government bodies in order to prevent arbitrariness or favouritism. However, it must be clearly stated that there are inherent limitations in exercise of that power of judicial review. Government is the guardian of the finances of the State. It is expected to protect the financial interest of the State. The right to refuse the lowest or any other tender is always available to the Government. But, the principles laid down in Article 14 of the Constitution have to be kept in view while accepting or refusing a tender. There can be no question of infringement of Article 14 if the Government tries to get the best person or the best quotation. The right to choose cannot be considered to be an arbitrary power. Of course, if the power is exercised for any collateral purpose the exercise will be struck down.”

BCCI (Board of Control for Cricket in India) though not a part of the superstructure of the State is nevertheless performing an important public function involving huge amounts and public interest. A writ under Article 226,<sup>116</sup> but not under Article 32 can, therefore, lie against it.<sup>117</sup>

The debarring of a company from tendering because one of its directors had assaulted an employee of the Authority was held to be not *mala fide* or with oblique motives.<sup>118</sup>

**Letter of intent to accept.**—Sometime a letter of intent to accept is issued before final acceptance. It has no binding efficacy on either party.<sup>119</sup> The letter of acceptance only stated the corporation’s intention about acceptance of the tender. The same was not reduced into writing. The court said that there was no concluded contract and no work order had been issued. The amount deposited by the tenderer could not be forfeited. He was entitled to refund.<sup>120</sup>

#### *Liability for failure to consider tender*

A valid tender must be opened and duly considered by the inviting authority, otherwise it would be unfairness. In a case of this kind where a valid

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listing for a certain period in the absence of any contract clause required decision on merits after hearing parties. *Andhra Pradesh Paper Mills Ltd v State of Maharashtra*, (2005) 4 Bom CR 274 (DB), the bidder was fully aware of the terms and conditions of the bidding process and also of the fact that it was wholly a commercial matter with no public interest, writ did not lie to question the validity of the terms on the ground of being arbitrary. *Popcorn Properties (P) Ltd v State of Maharashtra*, (2005) 6 Bom CR 518, fresh bidding ordered because of lack of transparency in previous bidding, Government agreed to it.

116. *Board of Control for Cricket in India v Zee Telefilms Ltd*, 2005 SCC OnLine Mad 373: (2005) 2 LW 567, Zee had withdrawn its tenders and had the right to do so. It had no right to file a writ. Approved in *Zee Telefilms Ltd v UOI*, (2005) 4 SCC 649: AIR 2005 SC 2677.

117. *Zee Telefilms Ltd v UOI*, (2005) 4 SCC 649: AIR 2005 SC 2677.

118. *DDA v UEE Electricals Engg (P) Ltd*, (2004) 11 SCC 213: AIR 2004 SC 2100, the debarring was for a period of five years.

119. *Hansa V. Gandhi v Deep Shankar Roy*, (2013) 12 SCC 776: (2013) 116 Cut LT 457.

120. *Dibakar Swain v Cashew Development Corpn*, 2014 SCC OnLine Ori 376: AIR 2015 Ori 6.

tender was not considered, the Court of Appeal observed:<sup>121</sup> “In certain circumstances an invitation to tender can give rise to binding contractual obligations on the part of the invitor to consider tenders which conformed with the conditions of tender. Since, in this case, tenders had been solicited by the Council from selected parties, and since the Council’s invitation to tender prescribed a clear, orderly and familiar procedure, which included draft contract conditions available for inspection but not open to negotiation, a prescribed common form of tender, the supply of envelopes designed to preserve the absolute anonymity of tenderers and an absolute deadline, it was to be implied that if an invitee submitted a conforming tender before the deadline he would be entitled as a matter of contractual right to have his tender opened and considered along with any other tenders that were considered. Damages were to be assessed in respect of the Council’s failure in accordance with its Standing Orders.”

Where the contract was awarded to an unqualified tenderer at the cost of the petitioner-tenderer who was qualified for the job, the court allowed the awardee to complete the work and also allowed the aggrieved party a compensation of Rs 1,00,000 to be recovered from the salary of guilty officers.<sup>122</sup> The court followed the following observation of the Supreme Court:<sup>123</sup>

“In a work of this nature and magnitude where bidders who fulfil pre-qualification alone are invited to bid, adherence to the instructions cannot be given a go-by by branding it as a pedantic approach, otherwise it will encourage and provide scope for discrimination, arbitrariness and favouritism which are totally opposed to the rule of law and our constitutional values. The very purpose of issuing rules/instructions is to ensure their enforcement lest the rule of law should be a casualty. Relaxation or waiver of a rule or condition, unless so provided under the ITB, by the State or its agencies in favour of one bidder would create justifiable doubts in the minds of other bidders. It would impair the rule of transparency and fairness and provide room for manipulation to suit the whims of the

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121. *Blackpool and Fylde Aero Club Ltd v Blackpool Borough Council*, (1990) 1 WLR 1195 (CA); *Vijay Kumar Ajay Kumar v Steel Authority of India Ltd*, AIR 1994 All 182, tenders for management of materials and port, restricting the tender to handling stockyard for the purpose of testing their experience, held, not wrong, *New Horizons Ltd v Union of India*, (1995) 1 SCC 478; (1997) 89 Comp Cas 849, disqualification of a company tenderer on the ground that it had no requisite experience was held to be wrongful, the shareholders enjoyed the requisite experience.

122. *A.K. Construction v State of Jharkhand*, (2004) 1 BLJR 516 (Jhar).

123. *W.B. SEB v Patel Engg Co Ltd*, (2001) 2 SCC 451: AIR 2001 SC 682. Also citing *Monarch Infrastructure (P) Ltd v Ulhasnagar Municipal Corp*n, (2000) 5 SCC 287: AIR 2000 SC 2272; *Bhupendra Engg & Construction (P) Ltd v State of Jharkhand*, (2004) 1 BLJR 237 (Jhar), there was no explanation for 18 days delay in scrutinising tenders after opening them and why another tender was scrutinized just the next day after opening. The court said that transparency should be maintained in awarding contracts, set aside. *Arun Kumar Agarwal v Bihar State Food Civil Supply Corpn*, (2005) 1 BLJR 29 (Pat) no record showing any favour to any body, no infirmity in the decision.

State agencies in picking and choosing a bidder for awarding contracts as in the case of distributing bounty or charity.”

### *Refund of earnest money*

Where the opening and acceptance of tenders was postponed because of a High Court order, it was held that the tenderer was entitled to withdraw his tender and he, having effectively withdrawn it, was entitled to refund of his earnest money. The retention of the money by the department after revocation was unreasonable. An order for refund could be granted with interest.<sup>124</sup> Where the earnest money of a tenderer was forfeited before acceptance of the tender and conclusion of the contract and the dispute between the parties was also not related with the contract, a writ petition challenging the forfeiture was held to be maintainable.<sup>125</sup> Forfeiture of bid security on the ground that the bidder had indulged in a fraudulent practice was held to be not proper because no such ground was mentioned in the bid documents.<sup>126</sup> Where the lowest tenderer was found to be lacking in eligibility criteria at the pre-qualifying stage itself, the court said that his tender could be rejected. But forfeiture of his earnest money and that too without giving him show-cause notice was illegal *per se* and violative of the principles of natural justice.<sup>127</sup>

### *Non-compliance with Requirements*

A tender-inviting authority made it clear to the tenderers that only one brand of pump sets would be accepted. They gave even the last-minute opportunity before opening the tenders to enable the tenderers to change their quotations accordingly. The tenderer to whom the contract was awarded refused to comply with the supply order. The authority cancelled the contract and the order. The authority was held to be within its right to do so. Its action could not be regarded as arbitrary.<sup>128</sup>

124. *Aditya Mass Communications (P) Ltd v A.P. SRTC*, AIR 1998 AP 125; *Vinod J. Agarwal v Chief Officer, Mira Bhayander Municipal Council*, (2006) 4 Bom CR 356: AIR 2006 Bom 254: 2006 AIHC 2461: (2006) 4 Mah LJ 126, tender withdrawn before acceptance, and after expiry of validity period tenderer entitled to refund of earnest money. *A.P. Paper Mills Ltd v State of Maharashtra*, (2003) 4 Mah LJ 760, time for accepting tenders had expired, the tenderers who were awarded were allowed to withdraw their earnest money. *Narendrakumar Nakhat v Nandi Hasbi Textile Mills Ltd*, AIR 1997 Kar 185, fully deposited money including earnest allowed to be refunded because of sale by the court owing to objectionable conduct of both parties.

125. *Food Corporation of India v Sujit Roy*, AIR 2000 Gau 61.

126. *Sanicons v Govt of A.P.*, AIR 2006 AP 282.

127. *SRS Infra Project P Ltd v Gwalior Development Authority*, AIR 2010 NOC 955 MP.

128. *Vijay Fire Protection Systems Ltd v Visakhapatnam Port Trust*, (1997) 3 An WR 261. The court added that the whole arrangement being contractual and part of private law and not a part of statutory or public law, the matter could not be raked up in a writ petition under Article 226 of the Constitution. *Dipak Handling Agency v Minerals & Metals Trading Corpn Ltd*, (1997) 84 Cal LT 560, where a tender required that a labour licence under the Contract Labour (Regulation & Abolition) Act, 1970 should be filed along with the

Where one of the conditions in the tender was that the tenderer should have one year experience in the work involved, the court said that such a condition could be relaxed in favour of an otherwise competent contractor and he could be required to produce the certificate of work later. His tender was also the lowest one.<sup>129</sup>

It has been held that a tender inviting quotations for disposal of trees should mention the approximate value of the trees. It could be assessed by the tenderers and on that basis they could quote their figures.<sup>130</sup>

A tender was submitted without complying with the requirement of submitting the performance bank guarantee. But even so the other party placed a supply order in terms of the tender. The tenderer immediately wrote back to say that the term of performance bank guarantee was not acceptable to it. The court said that this amounted to cancelling one's tender. No binding order could be placed on the bases of a tender which was still in its fluid state.<sup>131</sup>

#### *Tender with concessional rate*

A tender offered firm rates but also offered concessional rates if the tender was finalised within shorter period than otherwise allowed. It was held that this did not amount to a conditional offer. It was only an inducement for bringing about more expeditious acceptance.<sup>132</sup>

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tender, it was held that more time should have been given to the tenderer to comply with the requirement and non-consideration of his tender only because the licence was not filed was not proper. *Soorajmull Baijnath (P) Ltd v Indian Oil Corp Ltd*, (2004) 3 ICC 539 (Cal), requirements of tender notice were not at all fulfilled. *Hem Raj Goyal v State of Punjab*, (2009) 1 RCR (Civil) 151 P&H, DB, lowest bid not considered because of not being absolute and unqualified.

129. *Kesulal Mehta v Rajasthan Tribal Areas Development Coop Federation Ltd*, AIR 2005 Raj 55; *Sical Logistics Ltd v Karnataka Power Corp Ltd*, (2006) 6 AIR Kant 394, none of the tenderers was found to be not qualified, yet one of them was ruled out in violation of applicable rules, the whole process was held to be vitiated. *Kay Vee Enterprises v Jawaharlal Nehru Technological University*, AIR 2006 NOC 488 (AP); (2006) 1 ALD 126, issue of tender and award of contract against rules to a contractor who was not registered, not proper.
130. *K.M. Pareeth Labha v Kerala Livestock Development Board Ltd*, AIR 1994 Ker 286; *Shiv Singh v Union of India*, AIR 2007 NOC 1879 (MP), tender submitted his tender, but did not sign each and every page as required. He was not allowed to say that his tender should not have been accepted for want of signature at certain places. The tenderer should have specifically indicated term and conditions not acceptable to him. He participated in negotiation proceedings. It was not open to him to say that there was no concluded contract. His earnest money was forfeited because he did not perform.
131. *Vishwa Industrial Co (P) Ltd v Mahanadi Coalfields Ltd*, AIR 2007 Ori 71 (DB).
132. *Kanhaiya Lal Agrawal v Union of India*, (2002) 6 SCC 315; AIR 2002 SC 2766; *Directorate of Education v Educomp Datamatics Ltd*, (2004) 4 SCC 19; (2004) 3 ICC 398, the terms of a tender cannot be made the subject-matter of judicial review. Freedom of contract is as much essential to the Government as to any individual. *S. Umamaheswara Rao v Nabard Roads and Buildings*, (2003) 2 ICC 737 (AP), terms and conditions necessary for getting work done depends upon various factors, the matter belongs to the domain of expert bodies. The court cannot interfere in such matters and say that a particular condition or technical specification is onerous or impracticable to be complied with and liable to be set aside.



### *Certainty of terms*

An agreement to sell immovable property must identify the property with certainty. It should fix the price and should be based on mutuality.<sup>133</sup> The notice inviting tenders for hiring of services of vehicles did not stipulate any period. The contract was awarded to the lowest tenderer for three years. It was held that there was nothing wrong in it. An open ended tender cannot be regarded as void for vagueness. The tender required that vehicles should not be more than six months old. The manufacturer had given up the specified model. The acceptance of substitute vehicles of equal efficiency and cost was not arbitrary.<sup>134</sup>

### **Government contracting**

The judgment of the Supreme Court in *Mahabir Auto Stores v Indian Oil Corp*n<sup>135</sup> is of extreme relevancy. SABYASACHI MUKHERJI CJ observed as follows:

“The State acts in its executive power under Article 298 of the Constitution in entering or not entering in contracts with individual parties. Article 14 of the Constitution would be applicable to such exercise of power. The action of State organ can be tested under Article 14. Every action of the State executive authority must be subject to the rule of law and must be informed of reason. So, whatever be the activity of the public authority, it should meet the test of Article 14 of the Constitution. *If a Government action even in the matters of entering or not entering into contract, fails to satisfy the test of reasonableness, the same would be unreasonable.* Rule of reason, rule against arbitrariness and discrimination, and rules of fair play and natural justice are all a part of the rule of law applicable to dealings with citizens. Even where the rights of citizens are in the nature of contractual rights, the manner, the method and motive of a decision of entering or not entering into a contract, are subject to judicial review on the touchstone of relevance and reasonableness, fair play, natural justice, equality and non-discrimination. It is well settled that there can be ‘malice in law’. Indeed ‘malice in law’ is a part of the dimensions of the rule of relevance and reason as well as the rule of fair play in action.”

133. *Mirahul Enterprises v Vijaya Srivastava*, AIR 2003 Del 15.

134. *New Golden Bus Service v State of Punjab*, AIR 2006 P&H 141; *Mohd Tajuddin v Joint Collector*, AIR 2006 NOC 490 (AP): (2006) 1 An LD 351, no minimum rate was stipulated in notice inviting tenders, no condition was stipulated that rates below a certain amount would not be accepted. The writ petitioner's tender was rejected on the ground that the rate was so low that it was not workable, not proper. *Sainik Mining & Allied Services Ltd v Mahanandi Coal Fields Ltd*, AIR 2010 NOC 683 Ori, details were there in the original tender carrying “instructions to bidders”, and there was also detailed work order and letter of intent, execution of a written agreement would have been a bare formality.

135. (1990) 3 SCC 752: AIR 1990 SC 1031.

The court could not sit in appeal against the decision of the Tender Committee which consisted of experts to substitute its own decision. Scope of interference by the court is very limited and only when the court is satisfied that the decision making process of the Tender Committee was actuated by *mala fides*, the court might interfere in the same.<sup>136</sup>

There can be no contractual obligation on the part of government in conflict with the constitutional obligations. Obligations flowing from contract must necessarily yield to obligations flowing from the Constitution and laws.<sup>137</sup>

### *Preventing from tendering and blacklisting*

A bidder was prevented by some elements inside the office from submitting his tender. An inquiry conducted by the authorities verified the allegation. The person so ruled out was permitted to submit his tender after two intervening holidays. His tender was accepted. No prejudice was caused to other tenderers. The work order issued to him was not interfered with.<sup>138</sup>

The condition of blacklisting a contractor arises only if the contract is awarded and the tenderer fails to perform any part of the contract. Some material fact may be required from the bidder about his experience for the purpose of seeking permission for making his proposal. If any such fact is concealed, it may disentitle the bidder from getting the contract. It may lead to forfeiture of earnest money but not to blacklisting.<sup>139</sup>

The power of blacklisting a contractor is inherent in a party allotting contracts. But when the party is a State, the decision to blacklist is open to judicial review on the touchstone of proportionality and principle of natural justice.<sup>140</sup>

## LAPSE OF OFFER

Acceptance should be made before the offer lapses. An offer lapses in the circumstances provided for in Section 6.

### **S. 6. Revocation how made.—A proposal is revoked—**

- (1) by the communication of notice of revocation by the proposer to the other party;
- (2) by the lapse of the time prescribed in such proposal for its acceptance or, if no time is so prescribed, by the lapse of a reasonable time, without communication of the acceptance;

136. *Prmod Kumar Rath v State of Orissa*, (2005) 99 Cut LT 299.

137. *Bharti Airtel Ltd v Union of India*, (2015) 12 SCC 1. The question was whether auctioning cell phone licences was likely to create unhealthy competition.

138. *Utpal Mitra v Chief Executive Officer*, AIR 2006 Cal 74.

139. *Meritrac Services (P) Ltd v Post Graduate Institute of Medical Education and Research*, AIR 2015 P&H 174.

140. *Kulja Industries Ltd v Western Telecom Project BSNL*, (2014) 14 SCC 731: (2013) 6 ALD 142.

- (3) by the failure of the acceptor to fulfil a condition precedent to acceptance; or
- (4) by the death or insanity of the proposer, if the fact of his death or insanity comes to the knowledge of the acceptor before acceptance.

### 1. Notice of revocation

Section 5 provides that “a proposal may be revoked at any time before the communication of its acceptance is complete as against the proposer, but not afterwards”. It has already been seen that as against the proposer, the communication of acceptance is complete “when it is put in a course of transmission to him, so as to be out of the power of the acceptor”. It means, therefore, that the communication of revocation to be effective must reach the offeree before he mails his acceptance and makes it out of his power. A revocation is effective only when it is brought to the mind of the person to whom the offer is made. This was laid down in *Henthorn v Fraser*.<sup>141</sup>

The secretary of a building society handed to the plaintiff in the office of the society an offer to sell a property at £750 giving him the right to accept within fourteen days. The plaintiff resided in a different town and took away with him the offer to that town. The next day at about 3.50 p.m. he sent by post his letter of acceptance. This letter was received at the society's office at 8.30 p.m. But before that at about 1.00 p.m. the society had posted a letter revoking its offer. The revocation and the acceptance crossed in the course of post. The plaintiff received the letter of revocation at 5.30 p.m. The revocation was held to be ineffective.

Explaining the principle, Lord HERSCHELL observed: “If the acceptance by the plaintiff of the defendant's offer is to be treated as complete at the time the letter containing it was posted, I can entertain no doubt that the society's attempted revocation of the offer was wholly ineffectual. I think that a person who has made an offer must be considered as continuously making it until he has brought to the knowledge of the person to whom it was made that it is withdrawn.”

Thus the communication of revocation should reach the offeree before the acceptance is out of his power. An illustration to Section 5 explains the matter. A proposes by letter sent by post, to sell his house to B. B accepts the proposal by a letter sent by post. A may revoke his proposal at any time before or at the moment when B posts his letter of acceptance, but not afterwards.<sup>142</sup>

The provisions relating to communication of proposal, acceptance and revocation are to be found in Sections 4 and 5. These sections are as follows:

141. (1892) 2 Ch 27. To the same effect, *Manchester Diocesan Council for Education v Commercial and General Investment Ltd*, (1970) 1 WLR 2041.

142. See also *Nutakki Sesharatnam v Sub-Collector (LA)*, (1992) 1 SCC 114: AIR 1992 SC 131, landowner offering land for acquisition if lump sum price was paid. He withdrew his offer before the Acquisition officer prepared his award of acceptance. Held, withdrawal good.

**S. 4. Communication when complete.**—The communication of a proposal is complete when it comes to the knowledge of the person to whom it is made.

The communication of an acceptance is complete,—

as against the proposer, when it is put in a course of transmission to him, so as to be out of the power of the acceptor;

as against the acceptor, when it comes to the knowledge of the proposer.

The communication of a revocation is complete,—

as against the person who makes it, when it is put into a course of transmission to the person to whom it is made, so as to be out of the power of the person who makes it;

as against the person to whom it is made, when it comes to his knowledge.

**S. 5. Revocation of proposals and acceptances.**—A proposal may be revoked at any time before the communication of its acceptance is complete as against the proposer, but not afterwards.

An acceptance may be revoked at any time before the communication of the acceptance is complete as against the acceptor, but not afterwards.

#### *Withdrawal before expiry of fixed period*

Where an offeror gives the offeree an option to accept within a fixed period, he may withdraw it even before the expiry of that period. The decision of the Madras High Court in *Alfred Schonlank v Muthunyna Chetti*<sup>143</sup> is an illustration in point. The defendant left an offer to sell a quantity of indigo at the plaintiff's office allowing him eight days' time to give his answer. On the 4th day however the defendant revoked his proposal. The plaintiff accepted it on the 5th day.

Holding the acceptance to be useless, the court said: "Both on principle and on authority it is clear that in the absence of consideration for the promise to keep the offer open for a time, the promise is mere *nudum pactum*."

Notice of revocation shall be deemed to have been served when it reaches the offeree's address. A notice for the withdrawal of a ship from the charterers' services was sent by telex and was received by the plaintiff's telex machine during normal business hours, but the plaintiff read the message the next day. He was, however, held bound by the notice when his machine received it.<sup>144</sup> The court said: "If a notice arrives at the address of a person to be notified, at such a time and by such a means of communication that it would in the natural course of business come to the attention of that person on its arrival, that person cannot rely on some failure of himself or his servants to act in a normal businesslike manner in respect of taking cognizance of the communication, so as to postpone the effective time of the notice until some later time when it in fact came to his attention."

Where the question was whether the notice for withdrawal of a ship under a charterer-party for default in payment of hire was effective when

143. (1892) 2 MLJ 57.

144. *Tenax Steamship Co Ltd v Brimnes*, 1975 QB 929 (CA).

it was recorded on the telex machine of the charterer or on the opening of the office on the next working day when the message was actually read, the court upheld the decision of the arbitral tribunal that the message was deemed to have been delivered when it was read on the machine on the next working day.<sup>145</sup>

#### *Acceptance of proposal under Voluntary Retirement Scheme [VRS]*

The employees were given the right to apply under a voluntary retirement scheme. The authorities had, under the scheme, an absolute discretion to accept or reject the request of an employee. The retirement was to take effect only after the request had been accepted in writing. The scheme was held to be only an invitation to offer. An employee's application had the effect of making an offer. He could withdraw it before it was accepted. A term in the scheme which prevented the employee from withdrawing his request was held to be not binding. It had the effect of a promise not to withdraw the request and there was no consideration for the promise to make it binding.<sup>146</sup>

An employee first proposed to take voluntary retirement and then requested that his resignation be kept in abeyance. The Government accepted the resignation. The court said that the mere assertion without any proof or affidavit that the retraction was served on the Government before acceptance could not be accepted. The court further said that a request for keeping the proposal in abeyance was not the same thing as withdrawing it.<sup>147</sup> An employee can withdraw his proposal of resignation. It is possible up to the time when the acceptance of the proposal has been communicated to him. The court did not consider it tenable that the employee in question should have been permitted to withdraw her proposal till she received the cash.<sup>148</sup> A resignation was submitted and it was accepted on March 31, 2003, but that it would take effect from June 23, 2003 after expiry of the notice period of three months. The court said that the effective date of resignation was the date on which the employee was going to be released and not the date of acceptance and, therefore, in the meantime resignation could be withdrawn.<sup>149</sup>

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145. *Schelde Delta Shipping B.V. v Astarte Shipping Ltd, (The Panela)* (1995) 2 Lloyd's Rep 249, telex message was recorded by the machine at about 11.00 p.m. on a Friday, Saturday and Sunday being holidays the message was received at the opening hours on Monday. *J.K. Enterprises v State of M.P.*, AIR 1997 MP 68, communication of revocation sent to a wrong fax number, ineffective.

146. *Bank of India v O.P. Swarnakar*, (2003) 2 SCC 721: AIR 2003 SC 858; *State Bank of Patiala v Romesh Chander Kanoji*, (2004) 2 SCC 651: AIR 2004 SC 2016, no withdrawal allowed where the scheme became closed after receiving all applications. *Punjab National Bank v Virender Kumar Goel*, (2004) 2 SCC 193, application for retirement accepted, a part of the retirement benefits paid and used by employee, withdrawal not allowable.

147. *Shashikalab Parashar v State of Goa*, (1998) 2 Bom CR 427.

148. *Asha v U.P. State Sugar Corp Ltd*, (2006) 1 All LJ 808.

149. *K. Appa Rao v Tungabhadra Steel Products Ltd*, (2006) 5 AIR Kant R 296; *Balram Gupta v Union of India*, 1987 Supp SCC 228: AIR 1987 SC 2354, employer cannot refuse to accept resignation, employees are entitled to their freedom. *Shambhu Murari Sinha v Project &*

An employee made a conditional proposal of retirement and one of the conditions was a higher amount of gratuity. The offer was accepted by the employer. In view of the provisions of Section 4(5) of the Payment of Gratuity Act, 1972 which have an overriding effect, the employee became entitled to receive better terms of gratuity.<sup>150</sup>

The employer is not necessarily bound to accept the proposal of premature retirement. No action lies against refusal to accept. In this case the applications for retirement happened to be more than expected and the number of retirements that the employers could afford to accept was exhausted when some applications were still left out. It was held that the employer could not be forced to accept the whole number.<sup>151</sup>

Where the scheme stipulated that an application once made could not be withdrawn, no withdrawal was allowed after the closure of the scheme.<sup>152</sup> The general principles of contracting were held to be not applicable where the voluntary retirement was under a statutory scheme which categorically barred the employee from withdrawing the option once exercised. The terms of a statutory scheme would prevail over the general principles.<sup>153</sup>

#### *Agreement to keep offer open for specified period*

Where the agreement to keep the offer open for a certain period of time is for some consideration, the offeror cannot cancel it before the expiry of that period. The owner of a house agreed, in consideration of the sum of one pound, to give the plaintiff an option to purchase the house for ten thousand pounds within a stated period. He was not allowed to revoke

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*Development India*, (2002) 3 SCC 437: AIR 2002 SC 1341, though resignation accepted, employee was asked to continue up to a certain date. That date became the effective date. Resignation could be withdrawn up to that date. *H.L. Nagaraju v Vijaya Bank*, ILR 1999 Kant 197: 1999 Lab IC 2354, employer cannot refuse voluntary retirement. *Srikantha S.M. v Bharath Earth Movers Ltd*, 2005 8 SCC 314: (2005) AIR Kant 2993, employee resigning and acceptance with immediate effect. Subsequently, another letter told him that his application for casual leave had been accepted up to a certain date and his resignation would become effective on the expiry of that date. A week before that date the employee withdrew his resignation. Withdrawal became effective. *N. Dinakara Shetty v Union of India*, (2005) 6 Bom CR 470 (Panaji), once the application has been accepted, the employee becomes bound to take his retirement. *Kuldip Gandotra v Union of India*, (2005) 125 DLT 5 (DB), employee withdrew before acceptance, filed petition, money sent to him during pendency, acceptance under protest, termination of job not proper. The Supreme Court relied upon earlier decisions in *Union of India v Gopal Chandra Misra*, (1978) 2 SCC 301: AIR 1978 SC 694; *Balram Gupta v Union of India*, 1987 Supp SCC 228: AIR 1987 SC 2354; *J.N. Srivastava v Union of India*, (1998) 9 SCC 559: AIR 1999 SC 1571; *Power Finance Corp Ltd v Pramod Kumar Bhatia*, (1997) 4 SCC 280 in which it was held that a resignation which has already been accepted can be withdrawn before the "effective date."

150. *Digamber Yeshwantrao Watane v Agricultural Produce Market Committee*, (2004) 3 Mah LJ 603: (2004) 6 Bom CR 678.
151. *Vishakhapatnam Port Trust v T.S.N. Raju*, (2006) 7 SCC 664; *Digamber Yeshwantrao Watane v Agricultural Produce Market Committee*, (2004) 3 Mah LJ 603: (2004) 6 Bom CR 678, acceptance of voluntary retirement, difference over amount of gratuity, amount due has to be paid, reaction of other employees immaterial.
152. *State Bank of Patiala v Romesh Chander Kanoji*, (2004) 2 SCC 651: AIR 2004 SC 2016.
153. *New India Assurance Co Ltd v Raghvir Singh Narang*, (2010) 5 SCC 335.

the proposal within that time. One pound was a sufficient consideration because it was valuable. The effect was that the offer was irrevocable for the specified period of time and the offeree could accept it notwithstanding the purported revocation.<sup>154</sup>

The bid carried a condition that the bid security would be forfeited in case the bid was withdrawn during its validity period. It was held that withdrawal of the bid during validity period even before acceptance did not nullify the right of the offeree to forfeit the bid security.<sup>155</sup>

#### *Communication of revocation should be from offerer himself*

It is, of course, necessary that the communication of revocation should be from the offeror or from his duly authorised agent. But it has been held in England in *Dickinson v Dodds*<sup>156</sup> that it is enough if the offeree knows reliably that the offer has been withdrawn. The facts were:

The defendant signed and delivered to the plaintiff an offer to sell a property at a price fixed and added a postscript saying: 'This offer to be left open until Friday 9 o'clock, a.m., 12th June.' A day before the expiry of this period the plaintiff was informed by a third person that the property had already been sold to another. However, the plaintiff, before 9 a.m. of 12th June, found the defendant entering a railway carriage and handed him the notice of acceptance.

The court held "that the document amounted only to an offer, which might be withdrawn at any time before acceptance, and that a sale to a third person which came to the knowledge of the person to whom the offer was made was an effectual withdrawal of the offer". JAMES LJ added: "In this case, beyond all question, the plaintiff knew that Dodds was no longer minded to sell the property to him as plainly and clearly as if Dodds had told him in so many words, 'I withdraw the offer'."

It is suggested in Pollock and Mulla, that this rule will not be applicable in India for the simple reason that Section 6(1) requires in so many words that the notice of revocation should be "by the proposer to the other party."<sup>157</sup>

#### *Revocation of general offers*

Where an offer of a general nature is published through newspapers, it can be withdrawn by the same media and the revocation will be effective even if a particular person, subsequent to the withdrawal, happened to perform its terms in ignorance of the withdrawal. In an American case, the announcement through newspapers of a reward for reporting certain criminals was withdrawn by a subsequent notification. But a person who was

154. *Mountford v Scott*, 1975 Ch 258: (1975) 2 WLR 114 (CA).

155. *State of Haryana v Malik Traders*, AIR 2011 SC 3574: (2011) 13 SCC 200.

156. (1876) LR 2 Ch D 463 at p. 472.

157. INDIAN CONTRACT AND SPECIFIC RELIEF ACTS (8th Edn by Setalvad and Gooderson, 1957) 49.

working on the track of the criminals detected and reported them. He was absolutely unaware of the revocation. He could not recover. "It was withdrawn through the same channel in which it was made. The same notoriety was given to the revocation that was given to the offer."<sup>158</sup>

### *Superseding proposal by fresh proposal*

Where, before acceptance, a proposal is renewed in some parts of it and not in its entirety as proposed earlier (proposal to sell salvage claims in respect of 9 vessels, superseded by a subsequent proposal to sell only 4) and the letter purports to supersede the earlier communication, such proposal is no longer available for acceptance. The acceptance can be only of the renewed part. The allotment of the rest of the work to another buyer would give him a good right.<sup>159</sup>

### *Cancellation of allotment of land*

An allotment of land was made under the order of a Development Authority. The allottee deposited the money and an agreement was signed by the parties. This brought about a concluded contract. A subsequent cancellation of the allotment by the Authority was held to be not proper. The court said that the Authority was under a binding obligation to approve building plans for the land. The pendency of a criminal investigation regarding the allotment was held to be of no relevance.<sup>160</sup>

### *Revocation of bid*

In the case of an auction, "the assent is signified on the part of the seller by knocking down the hammer". "A bid may be retracted before the hammer is down".<sup>161</sup> In a Madras case:<sup>162</sup>

The appellant made a bid at an auction (the highest bid that was made) but before the property was knocked down, he discovered that the property was subject to a mortgage and retracted his bid. But even so the auctioneer knocked down the property to him. The owner of the property sued him.

The court held that "the plaintiff's bid was no more than an offer and he was entitled to withdraw the same before it was accepted by the property being knocked down to him by the auctioneer".<sup>163</sup>

158. *Shuey v United States*, 23 L Ed 697: (1875) 92 US 73. The burden is on the proposer to prove his revocation failing which he becomes bound and liable for breach. *Ramanathan Chettiar v National Textile Corpn Ltd*, AIR 1985 Ker 262.

159. *Banque Paribas v Citibank NA*, (1989) 1 Malaysian LJ 329 (CA) (Singapore).

160. *Rochees Hotels (P) Ltd v Jaipur Development Authority*, AIR 2002 Raj 316.

161. *Per BEST J in Agra Bank v Hamlyn*, ILR (1890) 14 Mad 235, 236.

162. *Joravarmull Champalal v Jeygopaladas Ghanshamdas*, AIR 1922 Mad 486.

163. The court cited *Raja of Bobbili v Suryanarayana Rao Gara*, ILR (1917) 42 Mad 776. See also *Agra Bank v Hamlyn*, ILR (1890) 14 Mad 235 where BEST J applied the rule to court auctions as well. He said: "A bidding at an auction is a mere offer which may be retracted

In a subsequent case,<sup>164</sup> the same High Court extended this principle to cases where a bid has been provisionally accepted and is subject to confirmation by higher officers. The bidder can withdraw before any such confirmation takes place. This principle has been endorsed by the Supreme Court in *Union of India v Bhim Sen Walaiti Ram*.<sup>165</sup>

A liquor shop was knocked down to a bidder at a public auction. This was subject to the confirmation by the Chief Commissioner who had the power before granting the licence to inquire into the financial condition of the bidder. The bidder had to pay one-sixth part of the price immediately and in case of any default on his part the Government had the power to re-auction the shop and the shortfall, if any, was recoverable from the bidder. He failed to pay one-sixth part and, therefore, the Chief Commissioner did not confirm the bid and ordered resale. Resale realised much less than the original bid and the question of bidder's liability to pay the shortfall arose.

The court said: "It is not disputed that the Chief Commissioner has disapproved of the bid offered by the respondent. If the Chief Commissioner had granted sanction in favour of the respondent, then there would have been a completed transaction and he would have been liable for any shortfall on the resale."

The question arises that when the bidder by not making the deposit had committed a default, where was the necessity of any final confirmation, which, even if given, would have meant nothing. If the Supreme Court equated the default in making the deposit with a formal revocation, then it would not have been necessary to say that if the confirmation had been given the respondent would have been liable, for if the bid had been withdrawn by the default, its confirmation would have made no difference.

The reason why the bidder has the liberty to withdraw is that the contract is concluded only when the bid is confirmed and formal communication of it is given to the bidder. This has been further pointed out by the Supreme Court in *Haridwar Singh v Bagun Sumbrui*.<sup>166</sup> A forest was knocked down



CASE PILOT

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before the hammer is down. Such is the rule with regard to auctions in general, and the same must be held applicable also to court auctions, in the absence of any law or rule to the contrary."; *State of Punjab v Kishan Lal*, (1991–92) PLR 283 where the provisional acceptance was not approved for a long period and the bidder withdrew his bid and he was allowed 6 per cent interest on his earnest money.

164. *Somasundaram Pillai v Provincial Govt of Madras*, AIR 1947 Mad 366. Followed in *State of Kerala v A.R.A.S. Armughamsamy Nadar & Co*, 1964 KLT 203; *Abdul Rahim Khan v Union of India*, AIR 1968 Pat 433; *State of M.P. v Firm Gobardhan Dass Kailash Nath*, (1973) 1 SCC 668: AIR 1973 SC 1164, when deposit is a condition precedent for the acceptance of a tender, the acceptance cannot be treated as valid without the condition being satisfied; *State of U.P. v Kishori Lal*, (1980) 3 SCC 8: AIR 1980 SC 680, the highest bidder, though he affixed his signature in the bid sheet in token of his acceptance, did not deposit one-sixth of the bid amount as was required. It was held that no contract resulted.

165. (1969) 3 SCC 146: (1970) 2 SCR 594.

166. (1973) 3 SCC 889: (1972) 3 SCR 629: AIR 1972 SC 1242.

to a bidder below the minimum price. Its confirmation was still in the process that the bidder agreed to pay the minimum. The department accepted this and telegraphed its acceptance to the forest officer for onward transmission to the bidder. The forest officer never received the telegram. Meanwhile another person offered a still higher price. The department accepted this and informed the forest officer, who received this communication and passed it on to the new bidder. It was held that no contract had been made on the earlier bid. Whatever acceptance had taken place that was still within the department and not communicated to the bidder.<sup>167</sup>

The auctioneer can provide the manner in which bids can be revoked. In a case before the Supreme Court,<sup>168</sup> one of the auction rules provided that “telegraphic bids or telegraphic instructions regarding bidding” will not be considered. The defendant had made his bid by filling a bid form at the spot. Subsequently, before the results were announced, he sent a telegram revoking his bid. But the Board accepted his bid. On his refusal to perform, he was held liable for breach. The Supreme Court felt that the words “telegraphic instructions regarding bidding” were wide enough to include all kinds of instructions about bids, including their revocation.

A tender was withdrawn at the stage when financial bids were still in sealed cover and the offeree was still to take decision on awarding the contract. On opening of financial bids it was found that the petitioner firm was not the lowest bidder and no loss would have been caused due to withdrawal. Withdrawal as made before acceptance was complete. Revocation was permissible and therefore forfeiture of earnest money was not proper.<sup>169</sup>

Where an auction bid was accepted being the highest and no further communication was necessary and the bidder had only to deposit money and subsequently the full payment within the specified time, the court said that

167. A bidder is bound by the bargain made if he has participated in the auction with full knowledge, *State of Punjab v Dial Chand Gian Chand & Co*, (1983) 2 SCC 503: AIR 1983 SC 743 where the bidder did not deposit 25 per cent of the money, as required by the rules, no contract arose even when his bid was accepted, *State of M.P. v Firm Gobardhan Dass Kailash Nath*, (1973) 1 SCC 668; *Varghese v Divl Forest Officer*, AIR 2003 Ker 197: (2003) 1 KLT 892, auction to collect forest usufruct from trees in cashew plantations. The auction was confirmed to the bidder. He was not permitted subsequently to resile from it by saying that the cost structure had altered. The court referred to *Kunjukrishnan v State of Kerala*, AIR 1983 Ker 73, wherein it was held that the failure to execute a formal agreement is not the criterion of a concluded contract and to *Syed Israr Masood v State of M.P.*, (1981) 4 SCC 289: AIR 1981 SC 2010, on the basis of which the court said that the very fact of depositing earnest money, participation in the auction and remitting the deposit on the same day were relevant criteria to hold that the contract had been concluded. *Hubli Dharwad Municipal Corpn v Chandrashekhar*, AIR 2012 Kant 41, auction bid, provisional acceptance, withdrawal before final acceptance, forfeiture of 50 per cent of the earnest money would be penalty.

168. *M. Lachia Setty & Sons Ltd v Coffee Board*, (1980) 4 SCC 636: AIR 1981 SC 162; *Birbadra Singh Parihar v State*, 2003 AIHC 980 (MP), conditions of auction applicable to group bidding and auctions applied subsequently to cases of individual bidding also. The same was held to be binding. The words “successful bidder of group” would include successful individual bidder for a shop.

169. *Raju Jyrwa v Union of India*, AIR 2014 Gau 163.

he was not entitled to extension of time for making payment and also not entitled to refund of his earnest money.<sup>170</sup> Where the tenderer sought upward revision of his bid after it had already been accepted, the earnest money was held to be not refundable.<sup>171</sup>

## 2. Lapse of time

An offer lapses on the expiry of the time, if any, fixed for acceptance.<sup>172</sup> Where an offer says that it shall remain open for acceptance up to a certain date, it has to be accepted within that date. It has been suggested by the Calcutta High Court that in such a case it is enough if the acceptor has “posted the acceptance before the stipulated time”, even if it reaches the offeror after the stipulated date. The court said, “that an effective date on which the option of acceptance is exercised by a party is to be ascertained from the date when the acceptance is put in transmission and the letter is posted”.

Where an offer was to last until the end of March and the offeree sent a telegram accepting the offer on 28 March which was received by the offeror on 30 March, it was held that the option was duly exercised.<sup>173</sup>

Where an application for admission to an institution had to be filed within the prescribed time by sending it either by registered post or in person and the candidate sent it by registered post some four days before the last date but it reached after the expiry of time, it was held that the application was too late.<sup>174</sup> A majority of two judges were of the view that where delivery can be made in a mode at the option of the sender, the agency through whom delivery is made acts as the agent of the sender, whereas if the delivery is made in a mode prescribed by the addressee, the agency acts as the agent of the addressee. In the first case, delivery to the agency is not delivery to the addressee, but in the later case it is. The dissenting judge was of the view that if the candidate selected one of the two modes prescribed by the addressee, the prescribed agency, i.e., post office, would be the agent of the addressee.

Where no time for acceptance is prescribed, the offer has to be accepted within a reasonable time. What is “reasonable time” will depend upon the

170. *Steel Union P Ltd v Commissioner of Customs*, AIR 2009 NOC 1215 Cal; *Sujit Das Gupta v SBI*, AIR 2015 Cal 246; SARFAESI Act, S. 13(6), at an auction of secured asset, successful bidder deposited earnest money, but did not deposit full auction price because the bank did not give him documents as to title of the property. The court said that the relevant documents could have been obtained by exercise of ordinary diligence. Even otherwise the bank sells the secured assets as owner. Bidder's plea was untenable. Forfeiture of earnest money was proper.

171. *Villayati Ram Mittal P Ltd v Union of India*, (2010) 10 SCC 532.

172. A lease terminates on the expiry of its term. It would require a fresh term. The lessee's remaining in possession does not revive the lease by itself. *Dhondu Undru Choudhary v Ganpat Lal Shankar Lal Agarwal*, 1991 Supp (1) SCC 513: AIR 1991 SC 1037.

173. *Bruner v Moore*, (1904) 1 Ch 305.

174. *R. Vinoth Kumar v Secretary, Kilpauk Medical College, Madras*, 1995 SCC OnLine Mad 78: (1995) 1 LW 351.

facts and circumstances of each case.<sup>175</sup> The definition of “a reasonable period” is a question of fact depending on the surrounding circumstances in which the agreement was made. Where the subject-matter of the contract is an article, like gold, the prices of which rapidly fluctuate in the market, very short period will be regarded as reasonable, but not so in reference to land. An offer for sale of shares allowed a month in which to accept, but both parties agreed that a reasonable period for acceptance was an implied term. The offeree felt that he could not make an informed decision within one-month time and argued that a reasonable period in this context would be one that would allow an informed decision as to whether the acceptance was in their best financial interest. The court did not agree with this contention. The offer was made at an uncertain time. Yet the offeree wanted that he should be allowed to accept after the uncertainties were over. This would be unusual in this type of commercial agreement.<sup>176</sup>

### 3. By failure to accept condition precedent

Where the offer is subject to a condition precedent, it lapses if it is accepted without fulfilling the condition. Where a salt lake was offered by way of lease on deposit of a sum of money within a specified period, and the intended lessee did not deposit the amount for three long years, it was held that this entailed cancellation of the allotment.<sup>177</sup>

### 4. By death or insanity of offerer

An offer lapses on the death or insanity of the offeror, provided that the fact comes to the knowledge of the offeree before he makes his acceptance.

In England it was felt at one time that an offer terminates at once on the death of the offeror, whether or not the fact has come to the notice of the offeree. MELISH LJ suggested (*obiter*) in *Dickinson v Dodds*<sup>178</sup> that an offer cannot be accepted after the death of the offeror. But in an earlier case,<sup>179</sup> where a creditor continued to act on a guarantee without knowledge of the surety's death, the court pointed out that an offer is not necessarily terminated with the death of the offeror. It may remain open until the offeree comes to know of death.

There is no provision in the Act about the effect of the death of an offeree. But as an offer can be accepted only by an offeree and not by any other

175. See further, *Shree Jaya Mahal Coop Housing Society Ltd v Zenith Chemical Works (P) Ltd*, AIR 1991 Bom 211, membership of a Society with tenancy rights for shops offered, response after six months, held too late. *Sekhsaria Exports v Union of India*, AIR 2004 Bom 35: (2004) 1 Mah LJ 415, a tender which was not accepted within reasonable time and it was revoked by the tenderer much before its acceptance could not give rise to a contract. Invocation of bank guarantee was improper.

176. *Barings v Internationale Nederladden Group N V*, 1995 Current Law Year Book 183.

177. *State of W.B. v Mahendra Chandra Das*, (1990) 2 Cal LJ 1.

178. (1876) LR 2 Ch D 463, 475.

179. *Bradbury v Morgan*, (1862) 1 H&C 249: 31 LJ Ex 462: 7 LT 104.

person, it should not be capable of being accepted by the offeree's executor also.<sup>180</sup>

### REVOCATION OF ACCEPTANCE

According to English law an acceptance once made is irrevocable. In the words of Anson: "Acceptance is to offer what a lighted match is to a train of gunpowder. Both do something which cannot be undone."<sup>181</sup> This rule is obviously confined in its operation only to postal acceptance. It is suggested in Anson that in other cases "an acceptance can be revoked at any time before acceptance is complete, provided, of course, that the revocation itself is communicated before the acceptance arrives".<sup>182</sup>

In India, on the other hand, acceptance is generally revocable. An acceptor may cancel his acceptance by a speedier mode of communication which will reach earlier than the acceptance itself. Section 5 is the relevant provision:

An acceptance may be revoked at any time before the communication of the acceptance is complete as against the acceptor, but not afterwards.

Thus the communication of revocation should reach earlier than the acceptance itself. What will be the result if they reach together. The section does not make this point clear. But the only illustration appended to the section seems to show that in such a case also the acceptance will be deemed to have been revoked. The illustration is as follows:

"A proposes, by letter sent by post, to sell his house to B. B accepts the proposal by a letter sent by post. B may revoke his acceptance at any time before or at the moment when the letter communicating it reaches A, but not afterwards."

That this should be the principle is further borne out by *Countess of Dunmore v Alexander*.<sup>183</sup>

A proposal of service made by a letter was sent through an agent. The agent received the acceptance and forwarded it to the principal, but the principal was away that day. The next day the agent received the revocation and forwarded it to the principal, who received the two letters together.

The revocation was held to be effective, the court saying that "the admission that the two letters were received together puts an end to the case."

180. See, for example, *Reynolds v Atherton*, (1921) 125 LT 690, 695–96 (CA) and the Canadian case of *Irvine, re*, (1928) 3 DLR 268.

181. THE LAW OF CONTRACT (23rd Edn 1972 by A.G. Guest) 50.

182. *Ibid.*

183. (1830) 9 Shaw 190: (1830) 9 Court of Sessions 190. *Vadada Ganeswara Rao v Mummidisetti Vijaya Chamundeswari*, AIR 2010 AP 74, revocation is an independent cause of action which comes into being at the place from where the notice of revocation is despatched. The courts at that place would have territorial jurisdiction to entertain suit for refund of the amount covered by the agreement of sale.

## Jurisdiction

In a suit for recovery of damages on account of breach of contract, the notice terminating the contract was received by the plaintiff at a place in Hyderabad. It was held that a part of the cause of action could be said to have arisen at that place. The suit filed at that place was maintainable.<sup>184</sup>

## STANDARD FORM CONTRACTS

### Exploitation of weaker party

The law of contract has in recent times to face a problem which is assuming new and wide dimensions. The problem has arisen out of the modern "large-scale and widespread" practice of concluding contracts in standardised forms.<sup>185</sup> The Life Insurance Corporation of India, for example, has to issue thousands of insurance covers every day.<sup>186</sup> Similarly, the railway administration of India has to make innumerable contracts of carriage. It would be difficult for such large-scale organisations to draw up a separate contract with every individual. They, therefore, keep printed forms of contract. Such standardised contracts contain a large number of terms and conditions in "fine print" which restrict and often exclude liability under the contract. The individual can hardly bargain with the massive organisations and, therefore, his only function is to accept the offer whether he likes its terms or not. "He cannot alter those terms or even discuss them; they are there for him to take or leave. He therefore does not undertake the laborious and profitless task of discovering what the terms are."<sup>187</sup> Lord DENNING MR pointed out in *Thornton v Shoe Lane Parking Ltd.*<sup>188</sup>

No customer in a thousand ever read the conditions. If he had stopped to do so, he would have missed the train or the boat.

This gives a unique opportunity to the giant company to exploit the weakness of the individual by imposing upon him terms which often look like a kind of private legislation and which may go to the extent of exempting the company from all liability under the contract. "The battle against abuse has fallen to the courts." The courts have found it very difficult to come to the rescue of the weaker party particularly where he has signed the document. In such cases the courts have been constrained to hold that he will be bound by the document even if he never acquainted himself with its terms. This has come to be known as the rule in *L' Estrange v F. Graucob Ltd.*<sup>189</sup>

184. *State of AP v T V Krishna Reddy*, AIR 2009 NOC 647 AP, DB.

185. See A.J. Kerr, *Imposed Terms in Standard Form Contracts*, (1981) 98 SALJ 15.

186. See *LIC v Consumer Education and Research Centre*, (1995) 5 SCC 482: AIR 1995 SC 1811.

187. To what extent they have eroded freedom of contract, see F. Kessler, *Contract of Adhesion—Some Thoughts About Freedom of Contract* (1943) 43 Columbia LR 629.

188. (1971) 2 QB 163 (CA).

189. (1934) 2 KB 394.

Mrs L signed an agreement without reading it under which she purchased a cigarette vending machine. The agreement excluded liability for all kinds of defect in the machine. The machine was totally defective.

The court found it as a fact that the supplier had made no effort to bring the sweeping exemption term to the notice of Mrs L. Even so the court held: "Where a document containing contractual terms is signed, then, in the absence of fraud, or misrepresentation, the party signing it is bound, and it is wholly immaterial whether he has read the document or not."<sup>190</sup> The result would have been different if the plaintiff had not signed.

Such contracts have been variously described. "Contracts of Adhesion", which means that the individual has no choice "but to accept; he does not negotiate, but merely adheres";<sup>191</sup> "compulsory contracts", they being a kind of imposition;<sup>192</sup> and "private legislation", they being a kind of code of bye-laws on the basis of which the individual can enjoy the services offered.<sup>193</sup>

### Protective devices

The individual, therefore, deserves to be protected against the possibility of exploitation inherent in such contracts. Following are some of the modes of protection which have been evolved by the courts.<sup>194</sup>

#### 1. Reasonable notice

In the first place, it is the duty of the person delivering a document to give adequate notice to the offeree of the printed terms and conditions. Where this is not done, the acceptor will not be bound by the terms. This was laid down by the House of Lords in *Henderson v Stevenson*.<sup>195</sup>

The plaintiff bought a steamer ticket on the face of which were these words only: "Dublin to Whitehaven"; on the back were printed certain conditions one of which excluded the liability of the company for loss,

190. See the judgment of SCRUTTON LJ. See also S.S. Singhi, *Some Reflections on the Problem of Adhesion Contracts*, AIR (1979) 22 Journal Section. Consumer legislation would have helped despite signature if it had been a consumer sale and not a trade sale.

191. Anson's LAW OF CONTRACT, 142 (23rd Edn by A.G. Guest, 1971).

192. Linhoff, *Scope of Compulsory Contracts Proper*, (1943) 43 Col LR 586.

193. Lord DENNING, ROAD TO JUSTICE, 93. *Economic Transport Organisation v Charan spg Mills P Ltd*, (2010) 4 SCC 114: (2010) 88 AIC 177, the Supreme Court has suggested that all institutions using this method of contracting should throw out clauses which have become time-worn and therefore redundant and inappropriate.

194. Following learned articles on the subject are suggested for study: *Freedom of Contract and Adhesion Contracts*, (1965) 14 International and Comparative Law Quarterly 173; Gower, *Exemption Clauses—Contractual and Tortious Liability*, (1954) 17 MLR 155; Sales, *Standard Form Contracts*, (1953) 16 MLR 318; *Contract Clauses in Fine Print*, (1950) 63 Harv L Rev 494; Kesler, *Adhesion Contracts*, (1943) 43 Col LR 329; Reynolds, *Warranty, Condition and Fundamental Terms*, (1963) 79 LQR 534; Linhoff, *The Scope of Compulsory Contracts Proper*, (1943) 43 Col LR 586; Chin Nyuk Yin, *EXCLUDING LIABILITY IN CONTRACTS*, 1985.

195. (1875) 2 Sc & Div 470: (1875) 32 LT 709 (HL).

injury or delay to the passenger or his luggage. The plaintiff had not seen the back of the ticket, nor was there any indication on the face about the conditions on the back. The plaintiff's luggage was lost in the shipwreck caused by the fault of the company's servants. He was held entitled to recover his loss from the company in spite of the exemption clauses.

The House of Lords observed that the plaintiff could not be said to have accepted a term "which he has not seen, of which he knew nothing, and which is not in any way ostensibly connected with that which is printed and written upon the face of the contract presented to him". The result would have been otherwise if words like "*For conditions see back*" had been printed on the face of the ticket to draw the passengers' attention to the place where the conditions were printed. The principle would, therefore, seem to be that where a written document is presented to a party for acceptance, a reasonably sufficient notice must be given to him of the presence of terms and conditions. Notice will be regarded as sufficient if it will "convey to the minds of people in general that the ticket contains conditions". This was clearly recognised in the subsequent case of *Parker v South Eastern Railway Co.*<sup>196</sup>

The plaintiff deposited his bag at the cloakroom at a railway station and received a ticket. On the face of the ticket were printed, among other things, the words, "see back" and on the back there was a notice that "the company will not be responsible for any package exceeding the value of £ 10". A notice to the same effect was also hung up in the cloakroom. The plaintiff's bag was lost and he claimed the full value of his bag which was more than £ 10. The company relied upon the exemption clause. The plaintiff contended that although he knew there was some writing on the ticket, he did not see what it was as he thought that the ticket was a mere receipt for the money paid by him.

MELLISH LJ pointed out that if the plaintiff "knew there was writing on the ticket, but he did not know or believe that the writing contained conditions, nevertheless he would be bound", for there was reasonable notice that the writing contained conditions.

Where, on the other hand, a folded up ticket was handed over to a passenger and the conditions printed on it were also obliterated in part by a stamp in red ink<sup>197</sup> and where in another case, the words on a ticket, "For conditions see back", were obliterated by the date stamp,<sup>198</sup> it was held in either case that no proper notice of the terms had been given.

196. (1877) LR 2 CPD 416 (CA).

197. *Richardson, Spence & Co and Lord Gough SS Co v Rwntrie*, 1894 AC 217 (HL).

198. *Sugar v London Midland & Scottish Rly Co*, (1941) 1 All ER 172. For comments see Turpin: *Contract and Imposed Terms*, (1956) 73 South African Law Journal 144 at p. 154. A consignment note signed neither by the consignor nor consignee and containing a clause on the back excluding the jurisdiction of all the courts except one was held not binding. There was no proper notification, *Road Transport Corp v Kirloskar Bros Ltd*, AIR 1981 Bom 299. A

The principle has been cited with approval by the Calcutta High Court in two cases<sup>199</sup> and was applied by it in *Mackillican v Compagnie Des Messageries Maritimes de France*.<sup>200</sup>

The plaintiff accepted a steamer ticket containing conditions printed in the French language. He claimed that he was not bound by them, being unable to read French.

Rejecting this contention, GARTH CJ said: "Although he may not understand French, he was a man of business contracting with a French company, whose tickets he knew very well were written in the French language. He had ample time and means to get the tickets explained and translated to him before he went on board; and it very plainly disclosed upon the face of it that the conditions endorsed were those upon which the defendants agreed to carry him." "Similarly, it has been held that where reasonably sufficient notice of existence of the terms is given, it would be no defence to say that the plaintiff was illiterate or otherwise unable to read."<sup>201</sup>

#### *Difference between contractual documents and receipts, etc.*

In the application of this principle the courts have had to distinguish between two kinds of documents, namely, contractual documents and mere receipts and vouchers. Emphasising this distinction in *Parker v South Eastern Railway Co*<sup>202</sup> MELLISH LJ said: "I think there may be cases in which a paper containing writing is delivered by one party to another in the course of a business transaction, where it would be quite reasonable that the party receiving it should assume that the writing contained in it no condition, and should put it in his pocket unread. For instance, if a person driving through a turnpike-gate received a ticket upon paying the toll, he might reasonably assume that the object of the ticket was that by producing it he might be free from paying toll at some other turnpike-gate, and might put it in his pocket unread. On the other hand, if a person who ships goods to be carried on a voyage by sea receives a bill of lading signed by the master, he would plainly be bound by it, although afterwards in an action against the shipowner for the loss of the goods, he might swear that he had never read the bill of lading and that he did not know that it contained the terms of the contract of carriage." A document is said to be contractual if it embodies the contract, that is to say, if the persons to whom it is delivered should know that it is supposed to contain conditions. But where the paper is not supposed to express the conditions of the contract, it will be regarded

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lottery ticket containing at the back small print as to jurisdiction, held, not binding, *Govt of Rajasthan v Venkataramana Seshiyer*, AIR 1984 AP 5.

199. *Madras Railway Co v Govinda Rau*, ILR (1898) 21 Mad 172, 174; *Sk Dawood v S.I. Rly Co Ltd*, ILR 1945 Mad 194, 178.

200. ILR (1881) 6 Cal 227 at p. 234.

201. *Thompson v London, Midland & Scottish Rly Co*, (1930) 1 KB 41 (CA). For a criticism of this decision see *Winfield, Some Aspects of Offer and Acceptance*, (1939) 55 LQR 499, 518.

202. (1877) LR 2 CPD 416 (CA).

as a mere voucher etc., and extra care will have to be taken to communicate its terms than mere warning on the face. A good illustration is *Chapelon v Barry UDC*:<sup>203</sup>

The plaintiff went on to a beach and hired two chairs from a pile of deck chairs belonging to the defendant Council. He received two tickets from the attendant, glanced at them, and slipped them into his pocket. While he was sitting on one of the chairs, he had the misfortune to go through the canvas with the result that he suffered injury. Tickets carried the words: "The Council will not be liable for any accident or damage arising from hire of chairs." He said that he had no idea that there were any conditions on these tickets and that he did not know anything about what was on the back of them. The Council was held liable for his injury.

SLESSER LJ said: "In my opinion, this ticket is no more than a receipt, and is quite different from a railway ticket which contains upon it the terms upon which a railway company agrees to carry the passenger." The object of the ticket was that the person taking it might have evidence that he had paid the hire and the term printed on it was no part of the contract.

In such cases, Lord DENNING MR pictorially remarked in *Thornton v Shoe Lane Parking Ltd*:<sup>204</sup> "In order to give sufficient notice, it would need to be printed in red ink with a red hand pointing to it, or something equally startling." If this is not done, the condition would not form part of the contract. The facts of the case were:

The plaintiff parked his car in an automatic car park. A notice at the entrance stated: "Cars parked at the owner's risk". The plaintiff slipped the money into a machine which brought forth a ticket. The barrier at the gate was then automatically raised and the plaintiff parked in his car. He looked at the ticket to see the time of parking, and noticed some other words, but did not pay further attention to them. These words drew the attention of the customer to a poster inside the garage which displayed the conditions one of which excluded liability for any injury to the car or customer. While taking back his car, the plaintiff was injured, for which he brought an action and the defendants sought the protection of the exemption clause.

But they were held liable. "The exempting condition is so wide and so destructive of rights that the court should not hold any man bound by it unless it is drawn to his attention in the most explicit way."

A lorry load of whisky was delivered to warehouse-keepers under a delivery note which stated that they would be liable for any loss of the goods. The warehouse-keepers stamped the delivery note on receiving the goods and this carried a condition limiting their liability to £800 per ton. The

203. (1940) 1 KB 532 (CA).

204. (1971) 2 QB 163 (CA).

goods were lost by theft and the question arose as to whose terms governed the contract. The court said that the warehouse-keepers' conditions were incorporated into the contract and not those of the owner and therefore the liability was limited to £800 per ton subject to further reduction for the bottles which were recovered after the theft.<sup>205</sup>

The mere existence of a clause in a consignment note restricting jurisdiction to one court only was held to be not capable of binding the other party. The term, being too serious, required special notification.<sup>206</sup> The court cited the following passage from CHITTY ON CONTRACTS:<sup>207</sup>

“The document must be of a class which either the party receiving it knows, or which a reasonable man would expect, to contain contractual conditions. Thus a cheque-book,<sup>208</sup> a ticket for a deck-chair,<sup>209</sup> a ticket handed to a person at a public bath house,<sup>210</sup> and a parking-ticket issued by an automatic machine<sup>211</sup> have been held to be cases where it would be quite reasonable that the party receiving it should assume that the writing contained no conditions and should be put in his pocket unread.”

Lord DENNING MR in *George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd*<sup>212</sup> observed:

“The clause was not negotiated between persons of equal bargaining power. It was inserted by the seed merchants in their invoices without any negotiations with the farmers.”

Exhibited notices can become a part of the contract if they are displayed so prominently as to bring them home to the other party before or at the time of contracting. Thus, where a receipt issued for a deposit showed that it was subject to the conditions exhibited on the premises and the notices were displayed in prominent places in the premises, that was held to be a reasonably sufficient notice.<sup>213</sup>

#### *Contract signed by acceptor*

Where a written contract is signed by the party accepting, he becomes bound by all its terms, whether he has read it or not. “In an ordinary case, where an action is brought on a written agreement which is signed by the defendant, the agreement is proved by proving his signature, and, in the

205. *British Road Services Ltd v Arthur V. Crutchley & Co Ltd*, (1968) 1 All ER 811 (CA).

206. *Road Transport Organisation of India v Barunai Powerloom Weavers' Coop Society Ltd*, (1997) 84 Cut LT 174.

207. 313, para 677, Vol II (24th Edn, 1977).

208. *Burnett v Westminster Bank Ltd*, (1966) 1 QB 742: (1965) 3 WLR 683.

209. *Chapelton v Barry UDC*, (1940) 1 KB 532 (CA).

210. *Taylor v Glasgow Corpn*, 1952 SC 440 (Scotland).

211. *Thornton v Shoe Lane Parking Ltd*, (1971) 2 QB 163 (CA).

212. 1983 QB 284 (CA).

213. *Watkins v Rymill*, (1883) LR 10 QBD 178 (DC).

absence of fraud, it is wholly immaterial that he has not read the agreement and does not know its contents.”<sup>214</sup>

This principle was laid down in *L'Estrange v F. Graucob Ltd*<sup>215</sup> and has already been noted. But even in cases like this, the affected party can be protected by the doctrine of fundamental breach or by finding that the terms are unreasonable or that there was misrepresentation about them. The former two modes of protection will be noted subsequently, the effect of misrepresentation may be illustrated here. The leading authority is *Curtis v Chemical Cleaning & Dyeing Co.*<sup>216</sup>

The plaintiff delivered a white satin wedding dress to the defendants for cleaning. On being asked to sign a receipt, she inquired why she was to sign it and was told that she was to take responsibility for any damage to beads and sequins. The plaintiff then signed the receipt without reading it. The receipt, in fact, contained a condition excluding liability for any damage howsoever caused. When the dress was returned there was a stain on it. To the plaintiff's action for damages, the cleaners pleaded the exemption clause.

But they were held liable. Lord DENNING MR said: “In those circumstances by failing to draw the attention to the width of the exemption clause, the assistant created the false impression that the exemption only related to beads and sequins, and that it did not extend to the material of which the dress was made,” and this was sufficient to disentitle them from relying on the exemption clause.

In a Canadian case,<sup>217</sup> a vendor fraudulently misrepresented the capacity of a boiler. He was held liable in damages for the fraud, despite the presence of an exemption clause. “A party to a contract cannot rely on an exclusion clause to avoid liability for fraud.”

Where a statement accompanies the delivery of a document, an oral assurance may prevail over what the document provides.

A person parked his car in a garage. The attendant told him not to lock the car. He told the attendant that there were valuable articles in the car. The attendant told him that he would lock it after moving it to the proper place. The briefcase containing valuables was stolen. Though the garage owner had excluded liability for the loss of the contents of a car, he was held liable. The attendants in such cases get an apparent authority to give

214. *Per* MELLISH LJ in *Parker v South Eastern Railway Co*, (1877) LR 2 CPD 416 (CA). This statement was relied upon by SUBRAMANIA AYYAR J in *Madras Railway Co v Govinda Rau*, ILR (1898) 21 Mad 172, 174; *Gautam Constructions & Fisheries Ltd v National Bank for Agriculture and Rural Development*, (2000) 6 SCC 519: AIR 2000 SC 3018, arbitrators and courts must adhere to contract terms. The court did not approve interference in rates for construction and the interest rate.

215. (1934) 2 KB 394.

216. (1951) 1 KB 805.

217. *Chau v Van Pelt*, (1977) 74 DLR (3d) 244 (BCSC).

assurances about the safety of the vehicles and garage users could rely on the assurance.<sup>218</sup>

The modern development in this connection is reflected by AMERICAN RESTATEMENTS OF CONTRACTS. [S. 11, Part 13] The rule stated is that when the other party has reason to believe that the party manifesting written assent would not do so if he knew that the writing contained a particular term; the term is not a part of the agreement. "Reason to believe" may be inferred from the fact that the term is bizarre or oppressive, or from the fact that it eliminates the dominant purpose of the transaction. An application of this principle is exemplified by *Tilden Rent-A-Car v Clendenning*.<sup>219</sup> The plaintiff signed a motor car insurance document which carried a warning on the face that no liability would arise if the provisions were not observed. On the back there were terms in fine and faint print one of which was that there would be no liability if the driver had taken any drink. The driver who caused the accident testified that though he had consumed some alcohol, he was not intoxicated and was capable of controlling the vehicle. Holding the company to be liable, the court said that a signature can be relied on as manifesting assent to a document when it is reasonable for the party relying on the signed document to believe that the signer really did assent to its contents. Hence the plaintiff was not bound by unusual and onerous printed terms which were not drawn to his attention.

#### *Notice of unusual terms*

Another example is *Interfoto Picture Library Ltd v Stiletto Visual Programmes Ltd*.<sup>220</sup> The defendants, an advertising agency, required photographs for a 1950's presentation. The plaintiffs dispatched 47 transparencies with a delivery note which stated that the same were to be returned in 14 days and that a holding fee of £5 per day for each transparency would be charged if they were not so returned. The defendants did not use the transparencies, put them to one side and forgot about them for a further two weeks. To their utter and considerable consternation an invoice arrived for £3783 holding fee. The court said that where a condition is particularly onerous or unusual, the party seeking to enforce it has to show that a clear, fair and reasonable effort was made to bring it to the attention of the other party. The condition, in this case, was unreasonable and extortionate and had not been sufficiently brought to the defendant's attention, it did not form part of the contract.

In another case,<sup>221</sup> the party was sent two apparently similar documents for counter-signature, and one for return to the sender had additional clauses

218. *Mendelsohn v Normand Ltd*, (1970) 1 QB 177; *J. Evans & Son (Portsmouth) Ltd v Andrea Merzario Ltd*, (1976) 1 WLR 1078, repugnancy between oral statement and printed terms, the former prevailed.

219. (1978) 83 DLR (3d) 400 (Ont CA).

220. 1989 QB 433; (1988) 2 WLR 615 (CA).

221. *Harvey v Ventilatorenfabrik Oeledge*, Financial Times, Nov 11, 1988 (CA).

on the reverse side which were written in a foreign language and to which the other party's attention had not been drawn in any way. That party was held to be not bound by those terms even though he signed and returned those documents.

These cases show the importance of the remark of DENNING LJ in *Spruling (J.) Ltd v Bradshaw*<sup>222</sup> to the effect that:

“The more startling a clause is, the greater the notice which must be given of it. Some clauses would need to be printed in red ink with a red hand pointing to it before the notice could be held to be sufficient.”

The court attached equal importance to the view of the matter as expressed by MEGAW LJ in *Thornton v Shoe Lane Parking Ltd*:<sup>223</sup>

When a particular condition relied on involves a sort of restriction which is not usual in that class of contracts, a defendant must show that his intention to attach an unusual condition of that particular nature was fairly brought to the notice of the other party. How much is required depends upon the nature of the restrictive condition.

In addition to this the courts are also under the statutory duty to consider reasonableness of the clause in the light of the circumstances which were known or which should have been known at the time of contracting.<sup>224</sup>

## 2. Notice should be contemporaneous with contract

Secondly, notice of the terms should be given before or at the time of the contract. A subsequent notification will indeed amount to a modification of the original contract and will not bind the other party unless he has assented thereto. A man and his wife hired a room in a hotel and paid a week's rent in advance. When they went up to occupy the room there was a notice on one of the walls to the effect that: “The proprietors will not hold themselves responsible for articles lost or stolen, unless handed to the managers for safe custody.” Their property having been stolen owing to the negligence of the hotel staff, the defendants were held liable as the court held that the notice was not a part of the agreement.<sup>225</sup>

Where the making of a contract is symbolised by the issue of a ticket by an automatic machine, the question arises whether the notice printed on the ticket has been given contemporaneously with the contract or subsequent to it. This aspect of the matter was considered by Lord DENNING MR in *Thornton v Shoe Lane Parking Ltd*.<sup>226</sup> In the case of tickets issued by clerks the theory is that the company makes the offer of the ticket and the customer by paying for the ticket without objection accepts it with all its terms.

222. (1956) 1 WLR 461 (CA).

223. (1971) 2 QB 163 (CA).

224. The duty is under the Unfair Contract Terms Act, 1977 (UK). See Elizabeth MacDonald, *The Duty to Give Notice of Unusual Contractual Terms*, 1988 JBL 375.

225. *Olley v Marlborough Court Ltd*, (1949) 1 KB 532 (CA).

226. (1971) 2 QB 163 (CA).

He has a chance of rejecting the ticket. But where the ticket is issued by an automatic machine, the customer cannot refuse it. He cannot get back his money. He is committed beyond recall at the very moment when he puts his money into the machine. The installation of the machine as ready to receive the money is an offer and the conduct of the customer in putting his money into the slot is an acceptance. The contract is then made. The terms of the offer are contained in the notice placed on or near the machine. The customer is bound by those terms if they are sufficiently brought to his notice beforehand, but not otherwise. He is not bound by the terms printed on the ticket if they differ from the notice, because the ticket comes too late. The contract has already been made. The ticket is no more than a mere voucher or receipt for the money. Applying these principles to the facts, his Lordship said:

In the present case the offer was contained in the notice at the entrance giving the charges for garaging and saying 'at owner's risk'. The offer was accepted when the plaintiff drove up to the entrance... and the ticket was thrust at him. The contract was then concluded, and it could not be altered by any words printed on the ticket itself.

Thus it is the duty of the party relying on an exclusion clause to make it clear to the other at the time of the contract that the same is incorporated into the contract.

A vehicle was offered for sale at an auction; the auction conditions, advertised by posters in the auction room, excluded all rights of buyer to return the vehicle or claim damages. The vehicle failed to reach the reserve price. The auction ended. It was then bought by a person by private negotiation. The vehicle broke down almost immediately. The buyer returned it and stopped the payment of the cheque for the price. The seller sued him for the price.

The court delivered a judgment for the buyer. The vehicle was not of merchantable quality. It was purchased at a private sale where the seller did not point out to the buyer that the auction conditions would be applicable.

#### *Imputed notice*

The court said in the case of an e-ticket for contract of carriage of passengers, there is the possibility of the passenger not having read the contract or not demanding a copy of the contract and even if a particular term is not within the knowledge of the passenger, it could not be ignored. The passenger would be bound by the terms of the contract. The term related to exclusive jurisdiction of courts at Delhi. Such term could not be allowed to be ignored.<sup>227</sup>

227. *Inter-Globe Aviation Ltd v N Sachidanand*, (2011) 7 SCC 463; (2011) 104 AIC 101. The court conceded that the Lok Adalat at Hyderabad too had jurisdiction because the passenger having been detained there, a part of the cause of action arose there.

### 3. Theory of fundamental breach

The third method is the doctrine of fundamental breach. It is a method of controlling unreasonable consequences of wide and sweeping exemption clauses. Even where adequate notice of the terms and conditions in a document has been given, the party imposing the conditions may not be able to rely on them if he has committed a breach of the contract which can be described as "fundamental". The rule has been thus stated by Lord DENNING LJ:<sup>228</sup>

These exempting clauses are now a days all held to be subject to the overriding proviso that they only avail to exempt a party when he is carrying out his contract, not when he is deviating from it or is guilty of a breach which goes to the root of it. Just as a party who is guilty of a radical breach is disentitled from insisting on the further performance by the other, so too he is disentitled from relying on an exempting clause.

An easy illustration is to be found in cases where goods different from those contracted are delivered. For example, a car was sold on "as is" basis and without any warranty or guarantee whatever. Even so the seller was held liable when five days later the engine of the car blew up. It was not a "car" which was delivered. Hence the contract was fundamentally broken.<sup>229</sup> If the car had shown any other defect which a used car is to everybody's knowledge likely to develop, such as, for example, a transmission problem, it would not have been regarded as a fundamental breach.<sup>230</sup>

#### "Core" of contract

What constitutes fundamental breach? "Every contract contains a 'core'<sup>231</sup> or fundamental obligation which must be performed. If one party fails to perform this fundamental obligation, he will be guilty of a breach of the contract whether or not any exempting clause has been inserted which purports to protect him."<sup>232</sup> This may be illustrated with the facts of *Davies v Collins*:<sup>233</sup>

The plaintiff entrusted to a dyer and cleaner a uniform for cleaning. On the docket given to him when he handed over the uniform were the following clauses: "Whilst every care is exercised in cleaning and dyeing garments, all orders are accepted at owner's risk entirely and we are

228. *J. Spurling Ltd v Bradshaw*, (1956) 1 WLR 461, 465. See also the decision of the Supreme Court in *B.V. Nagaraju v Oriental Insurance Co Ltd*, (1996) 4 SCC 674: AIR 1996 SC 2054, explaining fundamental breach.

229. *Findlay v Couldwell*, (1976) 69 DLR (39) 320 (Canada).

230. *Peters v Parkway Mercury Sales Ltd*, (1975) 10 NBR (2d) 703 (SC App Div).

231. Per Lord GREENE MR in *Alderslade v Hendon Laundry Ltd*, (1945) 1 KB 189, 193 (CA).

232. See A.G. Guest, *Fundamental Breach of Contract*, (1961) 77 LQR 98, 99. See also L.W. Melville, *The Core of a Contract*, (1956) 19 MLR 26; L.J. Montrose, *Some Problems About Fundamental Terms*, (1964) Camb LJ 60, 64.

233. (1945) 1 All ER 247, see Lord GREENE MR at p. 249.

unable to hold ourselves responsible for damage, shrinkage, colour or defects developed in necessary handling. The proprietor's liability for loss is limited to an amount not exceeding ten times the cost of cleaning." The defendant sent the uniform to be cleaned by a sub-contractor and it was never returned. The plaintiff claimed the full value of the uniform.

It was held that the mere fact of the particular limitation clause in the contract was sufficient to exclude any right to sub-contract the performance of the substance of the contract. Limitation clauses of this kind do not apply where the goods are lost not within the four corners of the contract but while something was being done which was outside the terms of the contract altogether, or when loss takes place in the course of some operation which was never contemplated by the contract at all. In *Alderslade v Hendon Laundry Ltd*<sup>234</sup> on the other hand, the plaintiff's handkerchiefs were lost in the laundry itself and, therefore, the exemption clause effectively limited the defendant's liability to twenty times the charge made for laundering.

Another illustration of fundamental breach is *Alexander v Railway Executive*.<sup>235</sup>

On depositing his luggage at the parcel office of a railway station, paying ordinary rates, the plaintiff received a ticket containing conditions one of which exempted the defendants from liability for misdelivery or loss of any article exceeding £5 in value unless a special charge for the same was paid. The defendants allowed the plaintiff's friend to take away the luggage and in an action by the plaintiff relied on the above exemption clause.

But it was held that "an essential part of the executive's duty was to take care of the deposited goods; that they had committed a fundamental breach of the contract in allowing an unauthorised person to have access to the goods and to take them away and, therefore, they could not rely on the exemption clause to shield them from liability."

#### *Departure from main purpose*

In the following two cases, however, the bailees were held not liable as the court did not find any fundamental departure from the main purport of the contract. One of them is *Gibaud v Great Eastern Rly Co.*<sup>236</sup> Here a cycle deposited at a station of the defendant-railway company was not in fact taken to the cloakroom, but was left in the booking hall itself and from there it was stolen, the company was held to be protected by the clause in the ticket which exempted the company from liability. The Court of Appeal could find no fundamental breach as it was no part of the contract that the cycle should be necessarily stored in the cloakroom.

234. (1945) 1 KB 189 (CA).

235. (1951) 2 KB 882.

236. (1921) 2 KB 426 (CA).

The other case is *Hollins v J. Davey Ltd.*<sup>237</sup> The plaintiff's car was garaged at the defendants' garage. One of the conditions of the contract exempted the defendant from loss or misdelivery. One of the plaintiff's former servants called at the garage and successfully persuaded the attendant to deliver the car to him telling him that he had been authorised by the plaintiff. The defendants were held not liable. The attendant made the innocent mistake in believing in the holding out by the servant. But if the attendant had delivered the car to a complete stranger, there would have been fundamental breach.

### *Rule of construction*

The results of these cases have been variable because it seems that the theory of fundamental breach is not an independent rule of law, but is only a rule of construction. A rule of law operates irrespective of the parties' intentions. But a rule of construction is one of the methods of ascertaining the parties' intention. This approach was "most clearly and accurately" enunciated by PEARSON LJ in *U.G.S. Finance Ltd v National Mortgage Bank of Greece, S.A.*<sup>238</sup> His Lordship said:

As to the question of 'fundamental breach',...there is a rule of construction that normally an exception or exclusion clause or a similar provision in a contract should be construed as not applying to a situation created by a fundamental breach of contract. This is not an independent rule of law imposed by the courts on the parties willy-nilly in disregard to their contractual intention. On the contrary, it is a rule of construction based on the presumed intention of the contracting parties. It involves the implication of a term to give to the contract that business efficacy which the parties reasonably must have intended it to have. This rule of construction is not new in principle but it has become prominent in recent years in consequence of the tendency to have standard forms of contract containing exception clauses drawn in extravagantly wide terms, which would have produced absurd results if applied literally.

This passage was cited with approval by the House of Lords in *Suisse Atlantique Societe D'Armement S.A. v N.V. Rotterdamsche Kolen Centrale.*<sup>239</sup>

The defendants chartered the plaintiff's ship for carriage of coal from the United States to Europe for two years. The contract set out the rates of loading and also provided that in case of any delay in loading the defendants would have to pay demurrage at the rate of one thousand dollars a day. The defendants caused delays for which the plaintiffs claimed that the contract was repudiated but nevertheless, without prejudice to



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237. (1963) 1 QB 844: (1963) 2 WLR 201.

238. (1964) 1 Lloyd's Rep 446, 453.

239. (1967) 1 AC 361: (1966) 2 WLR 944 (HL).

their rights, allowed the defendants to use the ship. At the end of the term they claimed damages for the delays in excess of the demurrage clause.

The House of Lords held that there was no fundamental breach. The defendants were guilty of conduct which entitled the plaintiffs to repudiate the contract, but they, in fact, affirmed it. The contract remained in force including the demurrage clause. Moreover, the demurrage clause was not an exception or limiting clause; it only stipulated liability for breach of contract and, therefore, the principle of fundamental breach was not applicable. But even so their Lordships explained (*obiter*) the meaning of fundamental breach or a breach going to the root of the contract. "These expressions", observed Lord WILBERFORCE, "are used in the cases to denote two quite different things, namely: (i) a performance totally different from that which the contract contemplates, (ii) a breach of contract more serious than one which would entitle the other party merely to damages and which (at least) would entitle him to refuse performance or further performance of the contract."

His Lordship then explained that if fundamental or total breach means a departure from the contract, the question will arise how great a departure and if it means supply of a different thing, the question will be how different? And added: "No formula will solve this type of question, and one must look individually at the nature of the contract, the character of the breach and its effect on future performance and expectation and make a judicial estimation of the final result."

These observations of the House of Lords on the question of fundamental breach being in the nature of *obiter dicta*, it left the Court of Appeal free to reconsider the question. This opportunity came in *Harbutt's "Plasticine" Ltd v Wayne Tank & Pump Co Ltd*.<sup>240</sup>

The defendants agreed with the plaintiff to design and install equipment for storing and dispensing stearine in a molten state at their factory. The defendants specified durapipe, a form of plastic pipe. In fact this was wholly unsuitable for the purpose. It burst at the very first testing leading to a fire which destroyed the factory. The defendants had limited their liability under the contract for any accident, etc., to £2330. The plaintiff's loss was much greater.

The Court of Appeal held that the defendants were guilty of fundamental breach and, therefore, they could not avail of the limitation clause and were liable for the cost of reinstating the factory. The court pointed out that one must look not merely at the quality of the breach but also at its results. If the result of breach is the total destruction of the subject-matter of the contract (factory in this case) then the contract is automatically at an end along with all its exception clauses. Lord DENNING MR considered the effect of the decision of the House of Lords in the *Suisse Atlantique Societe D'Armement*

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240. (1970) 1 QB 447: (1970) 2 WLR 198 (CA).

*S.A. v N.V. Rotterdamsche Kolen Centrale*<sup>241</sup> and their Lordships' emphasis upon the rule of construction, and remarked.<sup>242</sup>

So, in the name of construction, we get back to the principle that, when a company inserts in printed conditions an exception clause purporting to exempt them from all and every breach, that is not readily to be construed or considered as exempting them from liability for a fundamental breach; for the good reason that it is only intended to avail them when they are carrying out the contract in substance; and not when they are breaching it in a manner which goes to the very root of the contract.<sup>243</sup>

The contrast between the *Suisse Atlantique* case and this case is that though in each the defendant had limited his liability under the contract, that is, in the *Suisse Atlantique* case liability for delay was £1000 a day and in this case £2330 for any accidental damage, in the former the delay did not operate as a fundamental breach, but in the latter the supply of unsuitable material destroyed the very substratum of the contract.

That these two cases were not contradictory, but reconcilable, further appears from the judgment of DONALDSON J in *Kenyon Son & Craven Ltd v Barter Hoare & Co Ltd*.<sup>244</sup>

The plaintiff stored in the defendant's warehouse 250 tons of ground-nuts packed in bags. The warehouse was suitable for the purpose and was otherwise also structurally sound. The defendants had excluded their liability for any loss or damage unless it was due to the wilful neglect or default of the company or its own servants. The warehouse was not, however, rat-proof and the groundnuts were badly damaged by rats.

DONALDSON J referred to three categories of cases in which the rule of fundamental breach has been applied as stated by Lord WILBERFORCE in the *Suisse Atlantique* case. They are: (i) Supply of a different article; (ii) Hire-purchase cases; and (iii) Marine cases relating to deviation. The learned judge then stated that the Court of Appeal considered the *Harbutt's "Plasticine"* case as one of deviation from the main purpose of the contract. "The breach found consisted of the design, supply and the creation of a system or installation that was wholly unsuitable for its purpose."

Coming to the facts of the present case, the learned judge found that the case did not fall in any of Lord WILBERFORCE's categories. He said: "Had the defendants stored these nuts in the open or in an area which was prohibited by the contract or had they even stored them in a warehouse which was structurally or by reason of its other contents so unsuited to such storage as

241. (1967) 1 AC 361; (1966) 2 WLR 944 (HL).

242. (1970) 1 All ER at pp. 235–36; see Malcolm Clark, *Fundamental Breach is Dead! Long Live... The Rule Against Absurdity*, (1984) Camb LJ 32.

243. For an appreciation of this decision see Professor Brian Coote, *The Effect of Discharge by Breach on Exception Clauses*, (1970) Camb LJ 221.

244. (1971) 1 WLR 519.

to destroy the whole contractual substratum of the contract, then none of the defendant's conditions would have applied. That was not, however, the position. The warehouse itself, although not perfect and therefore requiring special vigilance against infiltration by rats, was not unsuitable and the other goods stored there caused no damage to the nuts.<sup>245</sup>

It has been laid down by the Court of Appeal<sup>246</sup> that where the goods are lost from the custody of a bailee (a carpet-cleaner in this case) fundamental breach would be presumed unless he accounts for the loss. The bailee must show that the loss had not occurred in consequence of a fundamental breach on his part since he is in a better position than the bailor to know what had happened to the goods while they were in his possession. Since the cleaner could not account for the loss he was not permitted to rely upon a clause by which he had limited his liability to a negligible figure. Lord DENNING went to the extent of saying that limitation clauses should not be given effect to in contracts in standard forms where there is inequality of bargaining power.

In a contract of carriage entered into on standard conditions of the forwarding trade, the parties orally agreed that the goods would be carried under the deck of the ship and not on the deck. The goods were by mistake put on the deck and lost. The cargo-owner was allowed to recover his loss notwithstanding the exemption clause in the standard form limiting the carrier's liability, because the oral promise was to be treated as overriding the printed conditions.<sup>247</sup>

A contract for hire-purchase of a motor cycle stated that the motor cycle was subject to no conditions or warranties whatsoever, express or implied. The machine was defective. It was returned for remedying the faults. It was delivered again to the buyer but all the faults were not rectified. Ultimately there was breakdown of the chain damaging also some other parts. The buyer finally rejected the machine and sought refund of the hire instalments he had already paid. He succeeded. The supply of a defective machine was a fundamental breach, this cancelled out all the exemption clauses. There was no affirmation of the contract on the buyer's part simply by asking for and accepting repairs.<sup>248</sup>

Fundamental breach was also inferred where the plaintiff's factory was burnt down by a security guard who had been provided by the defendants to protect the factory against fire. The defendants were held liable despite a number of exemption clauses. The limit of £25,000 as stated in the contract was held to be not applicable.<sup>249</sup>

245. *Shivaraj Vasant Bhagwat v Shevanta D. Indulkar*, (1997) 2 Bom CR 384, overloading an insured vehicle was a mere irregularity and not a fundamental breach so as to enable the insurer to get rid of his liability.

246. *Levison v Patent Steam Carpet Cleaning Co Ltd*, 1978 QB 69: (1977) 3 WLR 90 (CA).

247. *J. Evans & Son (Portsmouth) Ltd v Andrea Merzario Ltd*, (1976) 1 WLR 1078.

248. *Farnwooth Finance Facilities Ltd v Attride*, (1970) 1 WLR 1053 (CA).

249. *Photo Production Ltd v Securicor Transport*, (1978) 1 WLR 856 (CA).

### *Definition of breach in Unfair Contract Terms Act*

The theory of fundamental breach has now found statutory recognition to some extent in the (English) Unfair Contract Terms Act, 1977. The Act says that a party who commits breach of his contract cannot take the advantage of any clause in the contract which either excludes or limits his liability. Further, if there is any provision in the contract to the effect that "no performance" or "substantially different performance" will be taken as equivalent to performance, that will be of no avail. Thus the term "breach" will include a performance which is substantially different from that contemplated by the contract.

### *Resort to "fundamental breach" no longer necessary*

The effect of the provision is that it is no longer necessary for the courts to resort to "fundamental breach". The same result can be attained by resorting to the test of reasonableness under Section 11 of the Unfair Contract Terms Act, 1977 (English). This approach was in evidence in the decision of the House of Lords in *George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd*.<sup>250</sup>

The plaintiffs, who were farmers, ordered a quantity of seeds from seed merchants. It was known to the sellers that the seed should be for winter white cabbage fit for human consumption. The supply was on standard terms which limited liability in case of defective goods to replacement or refund of price. The seeds grew into unusable weeds and not fit for human consumption.

The defendants were not allowed to claim the protection of the exemption clause and were held liable for the plaintiffs' loss. The plaintiffs had based their claim on fundamental breach and requirement of reasonableness. But their Lordships preferred to go by the statutory ground.

Where as a result of the breach, the injured party rescinds the contract, all the exemption clauses will fall with it. But if he treats the contract as still subsisting and wants only to be compensated, it will be a matter of construction whether the type of breach which has occurred will be covered by the exemption clause or not.

An electrical equipment was supplied under a contract to the plaintiff to be used by him for producing chemicals. The machine turned out to be defective so that it could not operate at full capacity. It was set right two-and-a-half months later and then it functioned to its full capacity. The plaintiff sued for the loss of earnings for the two-and-a-half months' period.<sup>251</sup>

250. (1983) 2 AC 803: (1983) 3 WLR 163 (HL).

251. *Canso Chemicals Ltd v Canadian Westinghouse Co*, (1974) 54 DLR (3d) 517 (NSSC App Div). For an example of limitation clauses which would apply even when there has been a total failure to perform see *Ailsa Craig Fishing Co Ltd v Malvern Fishing Co Ltd*, (1983) 1 WLR 964 (HL).

He had to face a formidable exemption clause by which the supplier had undertaken the responsibility for repair but no responsibility for consequential damage. But even so the defendant was held liable. The court said that by supplying equipment which suffered from an error in design, the supplier had done something which was essentially different from what was contemplated by the parties. The plaintiff was entitled to repudiate the contract and was, therefore, entitled to compensation in lieu of repudiation. The court construed the exemption clause as confined only to cases requiring repair and not to be extensive enough to cover errors in design also.

A term in a sale of potato seeds excluded all liability unless the buyer gave notice of any defects within three days of delivery has been held to be unreasonable. In such cases the defect is likely to be discovered only when the seed has been planted and it comes out. The other term which restricted the seller's liability to contract price was found to be reasonable because it was there with the approval, and as a common practice, of the whole trade.<sup>252</sup>

#### 4. Strict construction

Exemption clauses are construed strictly particularly where a clause is so widely expressed as to be highly unreasonable. Any ambiguity in the mode of expressing an exemption clause is resolved in favour of the weaker party. An illustration of this principle of construction is afforded by *Lee (John) & Sons (Grantham) Ltd v Railway Executive*.<sup>253</sup>

Goods stored in a railway warehouse let to a tenant were damaged by fire and the tenant brought an action against the railway executive alleging that the accident was due to their negligence because a spark ejected from their railway engine had caused the fire. The defendants set up a clause in the tenancy agreement which exempted them for loss of or damage to property however caused (whether by act or neglect of the company or their servants or agents or not) which "but for the tenancy hereby created would not have arisen". The company was nevertheless held liable. The court was of opinion that the words "but for the tenancy hereby created" were confined to liabilities which arose by reason of the relationship of landlord and tenant.

Another illustration of strict interpretation is *Akerib v Booth*:<sup>254</sup>

By a written agreement the defendants let to the plaintiffs a few rooms on the second and third floors of their premises for office and store purposes. They retained in their possession a water-closet on the fourth floor. The agreement provided that the plaintiffs would exclusively employ the

252. *R.W. Green Ltd v Code Bros Farmers*, (1978) 1 Lloyd's Rep 602.

253. (1949) 2 All ER 581 (CA). *Sumitomo Heavy Industries Ltd v ONGC Ltd*, (2010) 11 SCC 296: AIR 2010 SC 3400, it is not appropriate to construe international commercial contracts strictly. Meaningful and purposive interpretation should be put on the clauses in question. For a study of Rules relating to interpretation of contracts, see Dr A.M. Abdul Rub, ORIENTAL JOURNAL OF LAW AND SOCIAL SCIENCES (2016) 15.

254. (1961) 1 WLR 367.

defendants in making up and packing all the goods brought by them for business on the premises and that the defendants would not in any circumstances be responsible for damage caused by water, insects, vermin or fungi to any goods. Owing to the negligence of the defendants or their servants water escaped from the closet and caused damage to the plaintiffs' goods.

It was held that the exception clause must be limited to the purpose of the contract. The purpose was to exempt the defendants from liability to goods that came to their possession for packing or making up, etc. The exemption clause must be confined to this and was not to apply to any other goods and accordingly the defendants were liable.

An insurance covered loss by flood and inundation but excluded liability for events like earthquake, typhoon, etc. Loss took place due to floods and subsidence of the building. The court said that in view of the non-inclusion of subsidence, the insurer's contention that the policy did not cover subsidence was not sustainable. The insurer had also certified that the building was a first class construction and, therefore, was estopped from saying that there were structural defects.<sup>255</sup>

### *Contra proferentem*

Where the words used in an exclusion clause are capable of two constructions, a wider construction and a limited construction, then the limited construction would be preferred, for the rule of law is that "every exception clause is to be interpreted, in case of ambiguity, *contra proferentem*".<sup>256</sup> This means that "if there is any doubt as to the meaning and scope of the excluding or limiting term, the ambiguity will be resolved against the party who has inserted it...."<sup>257</sup> These principles were applied by the Court of Appeal in *Hollier v Rambler Motors AMC Ltd*.<sup>258</sup>

*H* inquired of *R* over telephone whether *R* could repair his car. *R* told *H* to bring the car and that it would be repaired in due course. On three or four occasions during the last five years *R* had carried out servicing for

255. *United India Insurance Co Ltd v Kiran Combers & Spinners*, (2007) 1 SCC 368: AIR 2007 SC 393.

256. See Professor Brian Coote, *Breach and exception Clauses*, (1970) Camb LJ at p. 238.

257. Cheshire and Fifoot, THE LAW OF CONTRACT, 129 (8th Edn, 1972). *Bank of India v K Mohandas*, (2009) 5 SCC 313, in case of unclear term or expression, interpretation against the party is to be preferred who used such expressions, (*verba chartarum fortius accipiuntur contra proferentem*) *DDA v Jitender Pal Bhardwaj*, (2010) 1 SCC 146: AIR 2010 SC 497, where the terms of exemption are specific, unambiguous and plain, they should be taken in their plain meaning.

258. (1972) 2 QB 71: (1972) 2 WLR 401. It was held in *Archdale & Co Ltd v Comservices Ltd*, (1954) 1 WLR 459 (CA) that this doctrine would apply only when the parties leave their intention in doubt. But when the parties have clearly expressed what their intention is, there is no necessity to refer to the principle. In this case insurance against fire during the execution of the works was made by the contractor a responsibility of the owner, he was not allowed to hold the contractor liable even when the fire was due to the contractor's negligence.

H. On each occasion R was required to sign an invoice which described the work and mentioned the charge and gave warning below the customer's signature that "the company is not responsible for damage caused by fire to the customer's car on the premises". On this occasion the customer did not sign any such invoice and this time his car was destroyed by a fire which occurred due to R's negligence. R was held liable.

This doctrine applies in the case of a commercial contract since the clauses of the contract are bilateral and mutually agreed upon.<sup>259</sup>

The Court of Appeal had to face two formidable questions, namely, whether the signature on the previous occasions amounted to a notice of the term for this occasion also and, secondly, if it did, whether negligent fire was within the scope of the exclusion clause. In reference to the first question SALMON LJ had to consider two earlier House of Lords' decisions. One of them is *Henry Kendall & Sons v William Lillico & Sons Ltd.*<sup>260</sup> In this case during the past three years three or four times in every month goods were supplied on oral orders followed by signature on sold notes which excluded liability for latent defects. It was held that this practice was a sufficient notice of the terms. Distinguishing this case from the present the court said that that was a typical case where a consistent course of dealing between the parties made it imperative for the court to read into the contract the terms printed on the sold notes, whereas in the present case there had been only three or four dealings during the past five years. This was not sufficient to establish a course of dealing. Moreover, the dealing was not consistent as on this occasion the customer was not required to sign any invoice.

The other case is *MacCutcheon v David McBrayne Ltd.*<sup>261</sup> In this case M had asked his brother-in-law to have a car shipped from the Isle of Islay to the mainland. M had personally consigned goods on four previous occasions and each time he signed what was called a "risk" note. The risk note made it plain that the company was accepting the goods on its ship on the condition that they would not be responsible for any damage by negligence that the goods might suffer during the course of the voyage. The ship sank through negligence and the car was lost. M's brother-in-law had also consigned goods on several previous occasions. Sometimes he signed a risk note and sometimes not. On this occasion no such note was presented to him for signature. The House of Lords held that there was no previous course of dealing from which the term of inclusion could be implied into the contract which had been made on behalf of M by his brother-in-law.

259. *Export Credit Guarantee Corp of India Ltd v Garg Sons International*, (2014) 1 SCC 686: (2013) 178 Comp Cas 341; *Rashtriya Ispat Nigam Ltd v Dewan Chand Ram Saran*, (2012) 5 SCC 306: (2012) 93 ALR 257.

260. (1969) 2 AC 31: (1968) 3 WLR 110 (HL).

261. (1964) 1 WLR 125: (1964) 1 All ER 430 (HL). See also *HMK Kamaluddin Ansari & Co v Union of India*, (1983) 4 SCC 417: AIR 1984 SC 29, on interpretation of the terms of a contract. *Union of India v Gosalia Shipping (P) Ltd*, (1978) 3 SCC 23: AIR 1978 SC 1196, on interpretation of a charter-party contract.

After considering the case, SALMON LJ concluded: "If it was impossible to rely on a course of dealing in the *McCutcheon* case, still less would it be possible to do so in this case, when the so-called course of dealing consisted only of three or four transactions in the course of five years."

This should have been sufficient to dispose of the case. But SALMON LJ went further to examine that supposing that the clause had become a part of the contract, would it have covered fire by negligence. "It is well-settled that a clause excluding liability for negligence should make its meaning plain on the face of it to an ordinary literate and sensible person.... The defendant should not be allowed to shelter behind language which might lull the customer into a false sense of security by letting him think that he would have redress...for any damage which he might suffer by the negligence of that person."

A car insurance policy excluded liability for "Loss, damage, and/or liability caused or arising while any such car is conveying any load in excess of that for which it was constructed." At the time of the accident under which the car became a total loss there were six persons in the five-seater car. The court said that any doubt about the use of the word "load" would be construed in favour of the assured. The clause should have been spelled out in terms of specified weight. The court also gave this advice that if any insurance company wishes to put forward a policy which would be inapplicable when an extra passenger is carried, they should print that provision in red ink so that the assured would have it drawn to his particular attention.<sup>262</sup>

Cotton threads delivered under a contract were found to be 6 per cent shorter than they should have been and the seller sought to get rid of the liability for short delivery by sheltering himself under the exemption clause which said that the goods actually delivered would be taken to be in accordance with the contract in all respects unless the sellers were informed within 14 days of delivery of something wrong. The buyers discovered the shortage when they put the threads to actual use and that was much later than 14 days. The court did not permit the seller to use his clause for creating this phenomenon that goods not delivered should be taken to have been delivered. There was no warrant for an implication to the effect that non-delivery in length or small measure was included in the objections which should, within the time-limit, be made to goods delivered.<sup>263</sup>

262. *Houghton v Trafalgar Insurance Co Ltd*, (1954) 1 QB 247 (CA); *United India Insurance Co Ltd v Pushpalaya Printers*, (2004) 3 SCC 694: AIR 2004 SC 1700, damage to building by "impact" covered in insurance policy, damage caused by bulldozer moving on the road closely to the building, held, fell within the expression damage by "impact". Even if its meaning was not clear, it was to be taken in favour of the insured.

263. *Beck & Co v Szymanowski & Co*, 1923 AC 43 (HL). Though the terms have to be strictly construed, that construction must not be a strained one. Limitation of liability for any lapse in security services was stated in the contract to be £ 1000. The provision being clear, recovery for the actual loss which was much greater was not allowed, *Ailsa Craig Fishing Co Ltd v Malvern Fishing Co Ltd*, (1983) 1 WLR 964 (HL).

*Interpretation of price review and escalation clauses*

In a case before the Supreme Court<sup>264</sup> a clause in a contract for supply of electricity provided:

“The rate of supply as determined in Clause 17 shall be reviewed every fifth year provided the component of the cost of generation out of the total cost varies by 25 per cent or more.”

The consumer contended that this was a price escalation clause and would permit increase from the base price only according to a rise in the cost of production. The Supreme Court did not accept this. Explaining the distinction between an “escalation” clause and a “price review” clause, A.K. SEN J said:

An escalation clause, according to its accepted legal connotation means a clause which takes care of the rise and fall of prices in the market, whereas the right to review confers the power to revise the rate of supply. The word ‘review’ necessarily implies the power of the Board to have a second look and to so adjust from time to time its charges so as to carry on its operation under the Act without sustaining a loss.

The court referred to Butterworth’s *ENCYCLOPAEDIA OF FORMS AND PRECEDENTS*,<sup>265</sup> Hudson’s *BUILDING AND ENGINEERING CONTRACTS*,<sup>266</sup> Keating’s *BUILDING CONTRACTS*<sup>267</sup> and Black’s *LAW DICTIONARY*,<sup>268</sup> which portray different forms of “rise and fall” or escalator clauses in building and commercial contracts. The court cited the following passage from *AMERICAN JURISPRUDENCE*.<sup>269</sup>

In some contracts there is what is known as an escalator or fluctuation clause which is defined as one in which the contract fixes a base price but contains a provision that in the event of specified cost increase, the seller or contractor may raise the price up to a fixed percentage of the base and such escalator clauses are generally held to be sufficiently definite for enforcement.

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264. *Delhi Cloth and General Mills Co Ltd v Rajasthan SEB*, (1986) 2 SCC 431 at p. 455. See also *Shiv Pal Karan Kholi v State of U.P.*, AIR 1988 All 268, revision of housing prices. *Ramachandra Reddy v Union of India*, (2009) 6 SCC 414, a contract requires interpretation or construction when its terms are vague and unambiguous. *Udaipur Sahkari Upbhokta Thok Bhandar Ltd v CIT*, (2009) 8 SCC 393; (2009) 315 ITR 21, a contract has to be interpreted on its own terms. Conduct of parties also plays an important role. *Bank of India v K Mohandas*, (2009) 5 SCC 313, the nature and purpose of the contract is also an important guide. *Commercial Auto Sales P Ltd v Auto Sales Properties*, (2009) 9 SCC 620, intention of the parties to an instrument must be gathered from its terms in the light of surrounding circumstances.

265. (Vol 3, 4th Edn) 148.

266. 10th Edn.

267. (4th Edn) 498.

268. (4th Edn) 639.

269. (Vol 17, 2nd Edn) 786.

The court also cited the following passage from CORPUS JURIS SECUNDUM:<sup>270</sup>

[A] contract giving one of the parties the right to vary the price is not unenforceable for lack of mutuality where the right is not an unlimited one, as where its exercise is subject to express or implied limitation, such as that the variation must be in proportion to some objectively determined base, or must be reasonable, and this rule has been applied to contracts containing so-called 'escalator' clauses.

Where under a housing scheme, the price to be charged is made expressly variable, the allottees cannot claim any estoppel against variation nor seek refund on the ground of any proposed, but reasonable, variation.<sup>271</sup>

The Supreme Court held that the power to vary terms relating to quantum of work cannot be unlimited. Any clause giving absolute power to one party to modify the contract terms would amount to interfering with the integrity of the contract. Under the general law of contract, once the contract is entered into, any clause giving absolute power to one party to modify the terms of the contract at his sweet will or to cancel the contract would be in essence a negation of the contract.<sup>272</sup>

**Purposive interpretation.**—A contract has to be interpreted according to its purpose. Consistent with the character of purposive interpretation, the court is required to determine the ultimate purpose of the contract primarily by looking at the joint interest of the parties.<sup>273</sup> It is not appropriate to put strict construction upon an international commercial contract. Meaningful and purposive interpretation should be given to its clauses.<sup>274</sup> In another decision the Supreme Court deprecated another kind of practice in the use of standard form contracts. It observed that use of such contract forms in a blanket manner without paying attention leads to the fact that many of its general clauses are inapplicable to the transaction in hand. The court viewed it with disapproval that a party using a standard form does not take care to check it in the context of a particular contract and to delete clauses which are not applicable to the transaction in hand. The document should be transaction specific. The court has to ignore the inapplicable clauses to find out the intention of the parties and nature of the transaction, for example to know whether the transaction is simply that of subrogation or assignment or subrogation-cum-assignment, etc. Even where the document was meant to apply to carriage of goods by road, it seemed to pertain to carriage by air, or rail. Claims and remedies against a road carrier were not

270. (Vol 17) 406.

271. *Shiv Pal Karan Kholi v State of U.P.*, AIR 1988 All 268.

272. *National Fertilizers v Puran Chand Nangia*, (2000) 8 SCC 343; AIR 2001 SC 53.

273. *DLF Universal Ltd v Town & Country Planning Deptt*, (2010) 14 SCC 1; (2011) 4 SCC (Civ) 391.

274. *Sumitomo Heavy Industries Ltd v ONGC*, (2010) 11 SCC 296.

even mentioned. When all superfluous matter was excluded, the document seemed to be purely one of subrogation.<sup>275</sup>

### 5. Liability in tort

Even where an exemption clause is exhaustive enough to exclude all kinds of liability under the contract, it may not exclude liability in tort. Thus in *White v John Warwick & Co Ltd*:<sup>276</sup>

The plaintiff hired a cycle from the defendants. The defendants agreed to maintain the cycle in working order and a clause in the agreement provided: ‘nothing in this agreement shall render the owners liable for any personal injuries...’. While the plaintiff was riding the cycle the saddle tilted forward and he was thrown and injured.

It was held that although the clause exempted the defendants (even if they were negligent) from their liability in contract, it did not exempt them from liability in negligence.<sup>277</sup>

It is, however, open to the parties to exclude liability even for negligence by express words or necessary implication. For example, in *Rutther v Palmer*<sup>278</sup> a car was given to the defendants for sale under a contract which provided that while on trial the cars would be driven at the customer’s risk. An accident took place while the car was on a trial run. The defendants were held not liable, for they had by express words shifted the risk to the customers.

#### *Liability for negligence*

The results of such cases should now be different. The (English) Unfair Contract Terms Act, 1977, expressly provides that any clause in a contract which excludes or restricts liability for death or personal injury resulting from negligence shall be absolutely void. The expression “negligence” is defined in the Act to mean the breach of any common law or contractual duty.

### 6. Unreasonable terms

Another mode of protection is to exclude unreasonable terms from the contract. A term is unreasonable if it would defeat the very purpose of the

275. *Economic Transport Organisation v Charan Spg Mills (P) Ltd*, (2010) 4 SCC 114: (2010) 3 All LJ 281.

276. (1953) 1 WLR 1285 (CA).

277. Besides these, the courts have tried other ways of controlling the undesirable consequences of exemption clauses. This is indeed the only way to protect the individual and make up for the growing loss of individual freedom of contract. For a summary of such techniques, see Gower, *Exemption Clauses: Contractual and Tortious Liability*, (1959) 17 MLR 155. For an assessment of the need and propriety of such contracts see Bowes Egan, *Standard Contracts*, 1968 JBL 204; G.H. Treitel, *Exclusion Clauses, Possible Reforms*, (1967) JBL 209 and 334.

278. 1922 2 KB 87 (CA).

contract or if it is repugnant to public policy. Pointing this out in the *Suisse Atlantique* case,<sup>279</sup> Lord WILBERFORCE said:

One may safely say that the parties cannot, in a contract, have contemplated that a clause shall have so wide an ambit as in effect to deprive one party's stipulations of all contractual force: to do so would be to reduce the contract to a mere declaration of intent.

An example of an unreasonable term is to be found in *Lily White v Muniswami*.<sup>280</sup> A laundry receipt contained a condition that a customer would be entitled to claim only fifteen per cent of the market price or value of the article in case of loss. The plaintiff's new sari was lost. The court observed:

Certainly the conditions printed on the reverse of a bill may govern or modify any simple contract... subject to the obligation on the part of the businessman to perform the process properly and to return the article safe and intact. But, if a condition is imposed which is in flagrant infringement of the law relating to negligence... the court will not enforce such a term which is not in the interest of the public, and which is not in accordance with public policy. And there is certainly justification for the observation that this (enforcement of the condition) may well be putting a premium upon the abstraction of clothes, which may be committed by an employee of the firm, intent on private gain, though the firm itself may be blameless with regard to the actual loss.<sup>281</sup>

Explaining the justification for not enforcing unreasonable terms in *Lee (John) & Sons (Grantham) Ltd v Railway Executive*,<sup>282</sup> Lord DENNING LJ remarked:

There is the vigilance of the common law which, while allowing freedom of contract, watches to see that it is not abused.

The importance of this vigilance was amply demonstrated by his Lordship in *Levison v Patent Steam Carpet Cleaning Co Ltd*.<sup>283</sup>

A carpet was delivered to a cleaning company under the signature of the carpet-owner. Immediately above the space for signature the form stated that the undersigned agreed to the terms and conditions set out above. One of the clauses fixed the value of the carpet at £ 40 and another

279. *Suisse Atlantique Societe D'Armement S.A. v N.V. Rotterdamsche Kolen Centrale*, (1967) 1 AC 361: (1966) 2 WLR 944 (HL).

280. AIR 1966 Mad 13 at pp. 13–14.

281. See also *M. Siddalingappa v T. Nataraj*, AIR 1970 Mys 154, where a condition that only eight per cent of the cost of a garment would be payable in case of loss was held to be unreasonable. *R.S. Deboo v M.V. Hindlekar*, AIR 1995 Bom 68, laundry receipt contained printed condition restricting liability for loss or damage to 20 times laundering charges or half the value of the garment, whichever was less. The condition was held to be unreasonable.

282. (1949) 2 All ER 581, 584 (CA). See also *Indian Airlines Corp v Madhuri Chowdhuri*, AIR 1965 Cal 252.

283. 1978 QB 69: (1977) 3 WLR 90.(CA).



stated that the goods had been accepted at the owner's risk and the customers should insure their goods. The carpet was never returned and the cleaners informed the customer that it had been stolen. The customer recovered the full value of the carpet from his insurer and recovered £900 from the cleaners.

The clause which fixed the liability at £40 was regarded as unreasonable and, therefore, the cleaners were required to pay the full value of the carpet. Not to have returned the carpet also amounted to a fundamental breach. Lord DENNING reiterated that an exemption or limitation clause should not be given effect to if it was unreasonable or if it would be unreasonable to apply it in the circumstances of the case. The cleaners knew that the carpet was worth a lot of money and it would be most unreasonable to limit liability to £40. It was equally unreasonable to impose a term on the customers that their goods were accepted only at their risk.

It is not reasonable to exclude liability for breach of a term which is fundamental to the contract.

A photocopying machine was taken on lease. The machine was supposed to contain a particular feature. The machine which was actually supplied did not have that feature. The lease excluded liability for representations, if any, made about the machine.

It was held that the exclusion clause was unreasonable. It became overridden by the representations made by the copier salesman.<sup>284</sup>

#### *Statutory definition of reasonableness*

The principle of excluding unreasonable clauses has now found statutory recognition in the (English) Unfair Contract Terms Act, 1977. The Act provides that in respect of any loss caused by the breach of contract, any restricting or excluding clause shall be void unless it satisfies the requirement of reasonableness. A term will be regarded as reasonable if it is "a fair and reasonable one to be included having regard to the circumstances which were, or ought reasonably to have been known to or in the contemplation of the parties when the contract was made".<sup>285</sup>

284. *Lease Management Services Ltd v Purnell Secretarial Services Ltd*, (1994) 13 Tr LR 337 (CA).

285. In AMERICAN RESTATEMENT [2nd Edn, S. 211 (Part 3)] the modern doctrine is thus stated: Where the other party has reason to believe that the party manifesting such (written) assent would not do so if he knew that the writing contained a particular term, the term is not a part of the agreement. Reason to believe may be inferred from the fact that the term is bizarre or oppressive, from the fact that it eviscerates the non-standard terms explicitly agreed to, or from the fact that it eliminates the dominant purpose of the transaction. See Todd D. Rakoff, *Contracts of Adhesion: An Essay in reconstruction*, (1983) 96 Harv LR 1174; J.H. Baker, *From Sanctity of Contract to Reasonable Expectation*, CURRENT LEGAL PROBLEMS, 1979 where it is said that judges are to impose reasonableness. Whatever is not reasonable is not law. If the parties have agreed to something unreasonable they should be treated as if they have not agreed and they should be released. This brings in the doctrine of reasonable expectation. *Policing Unfairness in Contracts*, (1984) 47 Mod LR 523 in Reuben Hassen's

A local authority entered into a contract with a supplier for purchase of computer software designed to administer the collection of community charge according to population. The software contained an error which led to wrong count and, therefore, loss of revenue. The supplier company had limited its liability under the standard terms to £ 100,000. The court allowed the authority to recover its whole loss of revenue and not merely the amount under the limitation clause, which was held to be unreasonable. The supplier was a substantial company with ample resources to meet any liability and was insured under a worldwide policy for fifty million pounds. There were very few companies who could meet the authority's requirements and, therefore, the supplier was in a very strong bargaining position. The supplier company failed to adduce any evidence as to why the limit of £ 100,000 was justified. It was irrelevant to the defendant company's liability that the authority had made up its loss by increasing the community charge the following year.<sup>286</sup>

In reference to statutory contracts, the Supreme Court observed:

A statutory contract cannot be varied, added to, or altered by importing the doctrine of fairness. In a commercial or mercantile contract between parties of equal bargaining power, more so in a contract for liquor vend, the licensee takes a calculated risk of being put under the burden of rules and regulations.<sup>287</sup>

#### *Removal simpliciter clauses in contracts of employment*

A term in a contract of employment being offered by a Government corporation providing for the removal of a permanent employee without inquiry has been regarded by the Supreme Court to be unreasonable.<sup>288</sup> The Supreme Court has gone further still by laying down that in all its affairs, including economic and contractual matters, the state and its instrumentalities have to observe the mandate of Article 14 of the Constitution and offer equal opportunities and make a fair and reasonable selection of the party, including the selection of a Government District Counsel, on whom benefits of a Government contract are going to be conferred.<sup>289</sup>

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*The Special Nature of the Insurance Contract.* Steve Hedley, *Quality of Goods, Information and the Death of Contract*, 2001 JBL 114, considering the position of the doctrine of *caveat emptor* in the light of statutory developments.

286. *St Albans City and District Council v International Computers*, 1995 FSR 686. See also to the same effect, *Salvage Assn v Cap Financial Services*, 1995 FSR 654, where also the computers with accounting software contained numerous errors causing huge losses and, therefore, the limit of £25,000 upon liability was held to be unreasonable. In the meantime the defendant company had also increased its limit upon liability to £100,000.

287. *Mary v State of Kerala*, (2014) 14 SCC 272: (2013) 4 KLT 466.

288. *Central Inland Water Transport Corpn v Brojo Nath Ganguly*, (1986) 3 SCC 156.

289. *Shrilekha Vidyarthi v State of U.P.*, (1991) 1 SCC 212: AIR 1991 SC 537. Relying upon its own earlier decisions in *Dwarkadas Marfatia & Sons v Port of Bombay*, (1989) 3 SCC 293 the State has to show fairness in evicting its tenants; *Mahabir Auto Stores v Indian Oil Corp*, (1990) 3 SCC 752, terminating the agency of a distributor without proper

### *Compromise of existing contract*

The purpose of the Unfair Contract Terms Act, 1977 (English) is to invalidate exemption clauses in the strict sense, its clauses in a contract which modify prospective liability. The Act does not affect retrospective compromises of existing claims. Section 10 of the Act on its true construction does not apply to a contract to settle disputes which have arisen concerning the performance of an earlier contract. Furthermore, Section 10 does not apply where parties to both contracts (namely, the earlier contract and agreement of its accord and satisfaction) are the same. Thus a compromise would not be bad in law even if some of the clauses of the contract were unreasonable either generally or within the meaning of the English Act.<sup>290</sup>

## 7. Exemption clauses and third parties

One of the basic principles of the law of contract is that a contract is a contract only between the parties to it and no third party can either enjoy any rights or suffer any liability under it.<sup>291</sup> This should apply to standard form contracts also. The effect would be that where goods are supplied or services rendered under a contract which exempts the supplier from liability and a third party is injured by the use of them, the supplier is liable to him notwithstanding that he has purchased his exemption from the other party to the contract. If, for example, a contractor agrees to maintain and repair a lift in certain premises under contract with the owner who exempts him from liability, that exemption would be of no avail to the contractor against a person who is injured owing to bad repairs. If this were not so, the life and security of millions of people would be in the hands of the two parties to a contract. They would then make law not only for themselves, but also legislate for countless others. Obviously, therefore, in *Haseldine v C.A. Daw & Son Ltd*,<sup>292</sup> the abovementioned lift case, the defendants were held liable for the tort of negligence. GODDARD LJ reminded the contractor "that the duty to the third party does not arise out of contract, but independently of it".

Just as a third party is not affected by the terms of a contract, so also a third party cannot claim the advantage of them. If, for example, a sea-line company exempts itself from any liability to its passengers for the negligence of its employees, a passenger injured by the negligence of an employee will nevertheless be entitled to sue the negligent employee.<sup>293</sup> In another case, a shipping company limited its liability to a fixed amount for any loss of or damage to goods. The stevedores in England agreed with the company

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opportunity to enable him to come under the new policy. The court also relied upon Wade's ADMINISTRATIVE LAW and JUDICIAL REVIEW AND CONTRACTUAL POWER OF PUBLIC AUTHORITIES, (1990) 106 LQR 277–92.

290. *Tudor Grange Holdings Ltd v Citibank NA*, 1992 Ch 53: (1991) 3 WLR 750. (See also Notes under the heading "Consent Decrees" under comments on S. 74).

291. The doctrine of privity of contract is more fully discussed in the third chapter.

292. (1941) 2 KB 343 (CA) at p. 379.

293. So held in *Adler v Dickson*, (1955) 1 QB 158: (1954) 3 WLR 450 (CA).

to handle cargo subject to the same condition, but the plaintiff had no knowledge of this agreement. His consignment having been lost through the negligence of the stevedores, they were held not entitled to the protection of the limiting clause.<sup>294</sup>

Looking at this state of the law transport companies began to draft their exclusion clauses so as to provide that neither they nor their employees would incur any liability. In two such cases, in both of which two free pass-holders of a bus company were injured, one through the negligence of the driver and the other of the conductor, they were allowed to proceed against the negligent employees, in the one case because the free pass was a licence and not a contract and the driver was not a party to it<sup>295</sup> and in the other because it was a contract and was void under Section 151 of the (English) Road Traffic Act, 1960.<sup>296</sup>

The only way of conferring the benefit of exception clauses upon employees or sub-contractors, etc., seems to be the principle of vicarious immunity or implied contract as suggested by the House of Lords in *Elder, Dempster & Co v Paterson Zochonis & Co.*<sup>297</sup> In this case the plaintiff contracted with a charterer and the latter hired a ship from the shipowner for carriage of oil casks. The bill of lading as drawn between the plaintiff and charterer exempted both the charterer and shipowner from consequences of bad stowage. The oil was lost in circumstances covered by the exception clause. The plaintiff sued both of them, but they were held liable, either because the bill of lading became an implied contract between the plaintiff and shipowner or because the shipowner was acting as an agent of the charterer. A different result followed where the exclusion clause not merely protected the carrier, but also his agents and contractors and the stevedores contracted to unload the ship as agents for the carrier. They were accordingly held not liable for damage caused to the plaintiff's machinery through their negligence in the act of unloading.<sup>298</sup> Now under the (English) Unfair Contract Terms Act, 1977, a clause which excludes liability for negligence would be enforced only if it is reasonable in the circumstances of the case. Another case of the same kind is *Norwich City Council v Harvey*.<sup>299</sup>

A contract for the erection of a building contained a provision that the building owner was to bear the risk of loss or damage caused to the building by fire. A sub-contractor had contracted with the contractor on that basis. The court said that it would not be just and reasonable to exclude the sub-contractor from the protection of that provision in the main contract if the building was damaged by fire as the result of the

294. *Scrutons Ltd v Midland Silicones Ltd*, 1962 AC 446: (1962) 2 WLR 186 (HL).

295. *Genys v Matthews*, (1966) 1 WLR 758.

296. *Gore v Van de Lann*, (1967) 2 QB 31: (1967) 2 WLR 358 (CA).

297. 1924 AC 522. See further, Professor B. Coote, *Exception Clauses and Those to Whom They are Addressed*, (1973) Camb LJ 14, 104.

298. *New Zealand Shipping Co Ltd v A.M. Satterthwaite & Co Ltd*, (1974) 2 WLR 865.

299. (1989) 1 WLR 828 (CA).

negligence of the sub-contractor, even though there was no privity of contract between him and the building owner. In such circumstances there was not such a close and direct relationship between the building owner and the sub-contractor for the latter to owe a duty of care to the former. It followed that the sub-contractors were entitled to the benefit of the exemption from liability under the main contract in respect of the claim brought against them by the building owners in respect of their employees' negligence.

Where a person is entitled to the benefits of a contract he would have to accept its burdens also.<sup>300</sup>

In conclusion, the following statement of Lord REID in the *Suisse Atlantique* case may be cited:<sup>301</sup>

Exemption clauses differ greatly in many respects. Probably the most objectionable are found in the complex standard conditions which are now so common. In the ordinary way the customer has no time to read them and, if he did read them, he would probably not understand them. If he did understand and object to any of them, he would generally be told that he could take it or leave it. If he then went to another supplier, the result would be the same. Freedom to contract must strictly imply some choice or room for bargaining.

At the other extreme is the case where the parties are bargaining on terms of equality and a stringent exemption clause is accepted for a *quid pro quo* or other good reason; but this rule appears to treat all cases alike. There is no indication in the recent cases that the courts are to consider whether the exemption is fair in all the circumstances or is harsh and unconscionable, or whether it was freely agreed to by the customer. It does not seem to be satisfactory that the decision must always go one way if, e.g., defects in a car or other goods are just sufficient to make the breach of contract a fundamental breach, but must always go the other way if the defects fall just short of that. This is a complex problem which intimately affects millions of people, and it appears to me that its solution should be left to Parliament.

### Unfair Contract Terms Act, 1977 (UK)

The (UK) Unfair Contract Terms Act, 1977, which came into force on February 1, 1978, improves or affects some of the principles established by the courts in reference to business contracts. The Act tries to improve the situation by completely overruling certain types of exemption clauses and subjecting all of them to the test of reasonableness.

300. *Pyrene Co v Scindia Navigation Co*, (1954) 2 QB 402: (1954) 2 WLR 1005 where it was held that a person who accepts the benefit of a contract shall have to take its burdens also.

301. *Suisse Atlantique Societe D'Armement S.A. v N.V. Rotterdamsche Kolen Centrale*, (1967) 1 AC 361, 406: (1966) 2 WLR 944 (HL). Parliament has partly dealt with this problem in the (UK) Unfair Contract Terms Act, 1977.

The Act provides, for the first time, a statutory definition of the term "negligence" which is applicable both to tort and breach of contract cases. In the terms of the definition, negligence means:

- (a) breach of any obligation, arising from the express or implied terms of a contract, to take reasonable care or exercise reasonable skill in the performance of the contract;
- (b) breach of any common law duty to take reasonable care or exercise reasonable skill (but not a stricter duty); or
- (c) breach of the duty of care imposed by the Occupiers' Liability Act, 1957.

The second important effect of the Act is that any clause in a contract which excludes or restricts liability for death or personal injury resulting from negligence shall be absolutely void.

The third noteworthy provision of the Act is that in regard to other types of loss, not being death or physical injury, any restricting or excluding clause shall also be void unless it satisfies the requirement of reasonableness. The test will be deemed to be satisfied if the term is "a fair and reasonable one to be included having regard to the circumstances which were, or ought reasonably to have been, known to or in the contemplation of the parties when the contract was made". It means that reasonableness depends upon the unfairness of the terms in the light of the circumstances which ought to have been either known or to be in the contemplation of the parties. A chartered surveyor who gave a negligent mortgage valuation of a bungalow upon which the plaintiff relied in purchasing the property was held liable in spite of a clause excluding his liability in the matter. The clause was found to be not reasonable in the circumstances.<sup>302</sup>

The fourth important provision of the Act is concerned with the protection of the consumer and those who have been subjected to a standard form contract. The Act says that a person who deals with a consumer on his own standard terms, will not be allowed to claim the protection of any clauses restricting or excluding liability if he himself commits breach; nor can he claim substantially different performance as equivalent to performance. He can, however, take advantage of such terms if they are reasonable.

The fifth important part of the Act extends the scope of the Supply of Goods (Implied Terms) Act, 1973. This Act does not permit in reference to consumer sales the liability for breach of implied conditions and warranties to be excluded. This will now apply to all contracts under which possession of or property in goods passes from one person to another, for example,

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302. *Davil v Parry*, (1980) 20 Estate Gazette 92: 1988 CLY 435. A similar advice by a local authority under exclusion of liability protected the authority because it was not the professional business of the authority. *Harries v Wyre Forest District Council*, (1990) 1 AC 831: (1989) 2 WLR 790 (HL).

contracts of renting or leasing of appliances. In non-consumer contracts the exception clauses will be subjected to the test of reasonableness.<sup>303</sup>

A plant hire company, hired an excavator to the plaintiff together with the first defendant, a driver, for use in building work consisting of an extension to the plaintiff's factory. A condition was that the drivers were to be regarded for all purposes as the servants or agents of the hirer who alone will be liable for the consequences of the operation by them. An accident occurred as a result of the driver's negligence, causing considerable damage to the plaintiff's factory.

Going by the substance and effect of the term, rather than by its form, the court held that the term had the effect of excluding the common law duty in tort. It had the effect of excluding liability which fell within the purview of the Act and was, therefore, not fair and reasonable.<sup>304</sup> The court relied upon the speech of Lord BRIDGE in *George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd*:<sup>305</sup>

303. For further study see Brian Coote, *Unfair Contract Terms Act, 1977*, (1978) 41 MLR 312; Peter Arsonstam, CONSUMER PROTECTION, FREEDOM OF CONTRACT AND THE LAW, (Juta & Co, South Africa). The author finds that many firms which dominate a particular market abuse their economic power by means of oppressive standard contracts. Courts have often expressed their unwillingness to delve into the problem of contractual morality and unfairness. The author regrets that our judges have not been prepared to formulate a general theory of contractual conscientiousness which could govern all instances of abuse of bargaining power; *Unfair Contract Terms in Civil Law Systems*, (1980) 4 Can Bus Law Journal 429; (1981) 98 SALJ 70, where it is observed that sentiment on the sanctity of contract has undergone a sea-change. The decline of *laissez faire* and the concomitant growth of State intervention in the economy, the strongly felt need to protect the poor and the ignorant from exploitation by the rich and shrewd operators, the emergence and spread of the standard form contract, all these have combined to erode the *pacta sunt servanda* principle. Today all western legal systems have a multiplicity of protective laws, ranging from anti-monopoly legislation to consumer protection laws, from rent control to legislation regulating sales on instalments; Edward H. Hondius, *Unfair Contract Terms: New control System*, (1978) 26 American Journal of Comparative Law 525, 526; A.J. Kerr, *Terms in Standard Form Contract*, (1981) 98 SALJ 15; Todd D. Rakoff, *Contracts of Adhesion: An Essay in Reconstruction*, (1983) 96 Harv LR 1174. For the concept of "dealing as a consumer" see *R&B Customs Brokers Co Ltd v United Dominions Trust Ltd*, (1988) 1 WLR 321 (CA), here a company purchasing a motor car for the use of its director was held to be dealing as consumer so that the exclusion of merchantability was not binding on the parties. *Rasbora Ltd v JCL Marine Ltd*, (1977) 1 Lloyd's Rep 645, the same conclusion was reached with reference to the term "a consumer sale" in its application to purchase of a boat by a company for the private use of the owner of the whole of the issued share capital of the company. *Chester Grosvenor Hotel Co Ltd v Alfred McAlpine Management Ltd*, (1991) 56 Build LR 115 (QB), the meaning of a standard form of contract and dealing on the other's written standard terms of business. *Smith v Eric S. Bush*, (1990) 1 AC 831; (1989) 2 WLR 790 (HL), their Lordships considered the question whether professional valuer can exclude his liability for negligence and whether it would be reasonable and fair to do so. *Stag Line Ltd v Tyne Shiprepair Group Ltd*, (1984) 2 Lloyd's Rep 211 QB, consideration of the question whether the Act nullifies all clauses which purport to limit liability. Sealy, *Unfair Contract Terms Act, 1977*, (1978) CLJ 15.

304. *Phillips Products Ltd v Hyland*, (1987) 1 WLR 659 (CA).

305. (1983) 2 AC 803; (1983) 3 WLR 163 (HL); *Amiri Flight Authority v BAE Systems Plc*, 2002 EWHC 2481 (CA), where the requirements of the Act were applied to an international

In considering the requirement of reasonableness, the court must entertain a whole range of considerations, put them in the scales on one side or other and decide at the end of the day on which side the balance comes down. There will sometimes be room for a legitimate difference of judicial opinion as to what the answer should be, where it will be impossible to say that one view is demonstrably wrong and the other demonstrably right.

### Exclusion of right of set-off

The right of set-off being an instrument of justice and equity, its exclusion under contract clauses has been held to be *prima facie* unreasonable and hit by Section 13 of the Act. Accordingly, a counter-claim raised by way of set-off against the contractor's bill for final payment was allowed to be raised despite a clause in the contract excluding the right of set-off. The court put the burden upon the contractor to prove the reasonableness of the clause and added that the question whether a contract term satisfied the requirements of reasonableness in Section 13 of the 1977 Act has to be determined by considering the term as a whole and not merely that part of it relied on by the plaintiffs to defeat the defendant's set-off.<sup>306</sup>

### Exclusion clauses and disclaimer

The House of Lords have laid down that negligent advice given by a professional man would make him liable to his immediate advisee even if the advice was given under a clause containing disclaimer of all liability. The disclaimer would have to pass the test of reasonableness under the 1977 Act.<sup>307</sup> A house was purchased by the plaintiffs, price being paid on the basis of the advice sought from a local authority whose surveyors prepared a negligent report and advice. The advice was offered under disclaimer of liability. The house turned out to be unusable and required an amount for repair which was more than the cost of the purchase price. The authority was held liable to the plaintiffs. Their Lordships said that having regard to the high cost of the house it would not be fair and reasonable for valuers to impose on purchasers the risk of loss arising out of incompetence or carelessness on the part of valuers. It followed, therefore, that the disclaimer was not effective to exclude liability for the negligence of the valuers.

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contract for the sale of an aircraft which proved to be defective and had to be sold off at a loss. The court said that the Act was not confined in its application only to sale of goods transactions. That would have defeated the intention of Parliament to accord freedom of contract to parties involved in substantial transactions of an international character.

306. *Stewart Gill Ltd v Horatio Myer & Co Ltd*, 1992 QB 600: (1992) 2 WLR 72 (CA).

307. The case before their Lordships was *Smith v Eric S. Bush*, (1990) 1 AC 831: (1989) 2 WLR 790 (HL); *Harries v Wyre Forest District Council*, (1990) 1 AC 831: (1989) 2 WLR 790 (HL).

### Discretion to lender to set interest rates

Power given to a lender by mortgage agreements, to set interest rates from time to time, has been held to be not an unfettered power. Such power cannot be used dishonestly, for an improper purpose, capriciously or arbitrarily. The lender cannot set exorbitant or unreasonable rates.<sup>308</sup>

308. *Paragon Finance Plc v Staunton*, (2002) 1 WLR 685: (2002) 2 All ER 248 (CA).

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- *Brogden v Metropolitan Railway Co*, (1877) LR 2 AC 666 (HL)
- *Entores Ltd v Miles Far East Corporation*, (1955) 2 QB 327: (1955) 3 WLR 48
- *Felthouse v Bindley*, (1863) 7 LT 835
- *Haridwar Singh v Bagun Sumbrai*, (1973) 3 SCC 889
- *Indian Airlines Corp v Madhuri Chowdhuri*, AIR 1965 Cal 252
- *Kanhaiya Lal Agrawal v Union of India*, (2002) 6 SCC 315
- *Progressive Constructions Ltd v Bharat Hydro Power Corp Ltd*, AIR 1996 Del 92
- *Rajendra Kumar Verma v State of M.P.*, AIR 1972 MP 131
- *Suisse Atlantique Societe D'Armement S.A. v N.V. Rotterdamsche Kolen Centrale*, (1967) 1 AC 361: (1966) 2 WLR 944 (HL)
- *Union of India v Maddala Thai*, (1964) 3 SCR 774: AIR 1966 SC 1724



## Consideration

Section 25 of the Indian Contract Act opens with the declaration that “an agreement made without consideration is void...”.<sup>1</sup> In England also “promises without consideration are not enforced, because they are gratuitous”.<sup>2</sup> In *Rann v Hughes*<sup>3</sup> Lord Chief Baron SKYNNER observed: “It is undoubtedly true that every man is by the law of nature bound to fulfil his engagements. It is equally true that the law of the country supplies no means, nor affords any remedy, to compel the performance of an agreement made without sufficient consideration.”

### DEFINITION AND ITS REQUIREMENTS

Consideration has been variously defined. The simplest definition is by Blackstone:<sup>4</sup> “Consideration is the recompense given by the party contracting to the other.”

In other words, it is a price of the promise. In the words of Pollock, “Consideration is the price for which the promise of the other is bought, and the promise thus given for value is enforceable.”<sup>5</sup> Another simple definition is by Justice PATTERSON:<sup>6</sup> “Consideration means something which is of some

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1. The section then goes on to provide certain exceptions to the rule. Questions of consideration do not arise unless there is an agreement. *Associated Bombay Cinemas (P) Ltd v Urmi Developers P Ltd*, 1996 SCC OnLine Bom 319: (1997) 2 Bom CR 257, an agreement to form partnership for developing the land of the owner; the land to become partnership property on payment of Rs 1.25 crore to the owner; consideration not paid, held, no question of the land becoming partnership property. *Kampa Prasad v Addl District Judge, Mainpuri*, AIR 1997 All 201, judgment-debtor agreeing to pay decretal amount by stipulated date allowing dismissal of objections but getting no benefit under the agreement, agreement without consideration, void. The agreement was also void by reason of non-compliance with U.P. Regulation of Money Lending Act, 1976. *Jupudi Venkata Vijaya Bhaskar v Jupudi Kesava Rao*, AIR 1994 AP 134, agreement by a would-be adoptee that he would not claim the coparcenary rights of his would-be parents is not void for want of consideration and also does not involve any surrender of rights so as to attract S. 17 of the Registration Act, 1908. *Udho Bai v Ambika Tiwary*, AIR 2007 Pat 136, a piece of land belonged to five brothers, one of them alone sold off the entire chunk of land for a single consideration of Rs 25,000, the sale was held to be void, it could not be specifically enforced.

2. See HEATH J in *Lee v Muggridge*, (1813) 128 ER 599.

3. House of Lords, (1778) 7 Term Reports 350n (HL).

4. COMMENTARIES.

5. Sir Frederick Pollock, POLLOCK ON CONTRACTS (13th Edn) 133.

6. In *Thomas v Thomas*, (1842) 2 QB 851, 859.

value in the eyes of the law .... It may be some benefit to the plaintiff or some detriment to the defendant.”

But the most commonly accepted definition is that which was attempted by LUSH J in *Currie v Misa*:<sup>7</sup> “A valuable consideration in the sense of the law, may consist either in some right, interest, profit or benefit accruing to the one party, or some forbearance, detriment, loss, or responsibility given, suffered or undertaken by the other.”

The definition of consideration as a “price of the promise” has been commended by Cheshire and Fifoot. According to the learned writers, “it is easier to understand, it corresponds more happily to the normal exchange of promises and it emphasises the commercial character of the English contract. It reveals the essential simplicity of the concept.”<sup>8</sup> The Calcutta High Court has observed in a case that “consideration is the price of a promise, a return or *quid pro quo*, something of value received by the promisee as inducement of the promise.”<sup>9</sup>

In Section 2(d) of the Indian Contract Act consideration is defined as follows:

When, at the desire of the promisor, the promisee or any other person has done or abstained from doing or does or abstains from doing, or promises to do or to abstain from doing, something, such act or abstinence or promise is called a consideration for the promise.

This is rather a practical definition. The purpose is to emphasise the simple fact that consideration is some act, done or promised to be done, at the desire of the promisor. It also avoids the practical difficulties caused by the theory of consideration as consisting of some act which is beneficial to one party or detrimental to the other. This antithesis has been described to be not altogether happy. The Act simplifies the matter by saying that any kind of act or abstinence which is done or undertaken to be done at the desire of the promisor is a sufficient consideration.

The definition of consideration in Section 2(d) requires, in the first place, that the act or abstinence, which is to be a consideration for the promise, should be done *at the desire of the promisor*; secondly, that it should be done by *promisee or any other person* and, lastly, that the act or abstinence may

7. (1875) LR 10 Ex 153, 162.

8. LAW OF CONTRACT (8th Edn, 1972) 60.

9. *Fazalaldin Mandal v Panchanan Das*, AIR 1957 Cal 92. The same court had held in *Fanindra Narain Roy v Kachhemen Bibi*, AIR 1918 Cal 816; ILR (1917) 45 Cal 774 that consideration received by two mortgagors was good enough to bind all the four who executed the mortgage deed. This was followed in *Andhra Bank v Anantnath*, AIR 1991 AP 245 so as to hold all the joint promisors executing a promissory note liable though consideration was handed over to only one of them. *Prakashwati Jain v Punjab State Industrial Development Corp*n, AIR 2012 P&H 13, detriment suffered by the promisor for the benefit of another person (not party to consideration) was held as good consideration. Accordingly, the collateral security offered by the surety for the benefit of the principal debtor was regarded as sufficient consideration to make it enforceable.

have been already executed or is in the process of being done or may be still executory, that is to say, it is promised to be done.

### **“At the desire of the promisor” (*promissory estoppel*)**

The definition of consideration in Section 2(d) clearly emphasises that an act or abstinence which is to be a consideration for the promise must be done or promised to be done in accordance with the desire of the promisor. In other words, an act<sup>10</sup> shall not be a good consideration for a promise unless it is done at the desire of the promisor. In *Durga Prasad v Baldeo*:<sup>11</sup>

The plaintiff, on the order of the Collector of a town, built at his own expense, certain shops in a bazaar. The shops came to be occupied by the defendants who, in consideration of the plaintiff having expended money in the construction, promised to pay him a commission on articles sold through their agency in the bazaar. The plaintiff’s action to recover the commission was rejected.

“The only ground for the making of the promise is the expense incurred by the plaintiff in establishing the Ganj (market) but it is clear that anything done in that way was not ‘at the desire’ of the defendants so as to constitute consideration.”<sup>12</sup> The act was the result not of the promise but of the Collector’s order.

### ***Acts done at request***

On the other hand, an act done at the promisor’s desire furnishes a good consideration for his promise even though it is of no personal significance or benefit to him. The decision of the Calcutta High Court in *Kedarnath Bhattacharji v Gorie Mahomed*<sup>13</sup> has become well-known in this connection.

It was thought advisable to erect a town hall at Howrah provided sufficient subscription could be got together for the purpose. To this end the Commissioners of Howrah municipality set out to work to obtain necessary funds by public subscription. The defendant was a subscriber to this fund for Rs 100 having signed his name in the subscription book for that



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10. The word “act”, for the purpose of this definition, includes “abstinence” also. *Bank of Baroda v Kayenkay Agencies*, (2003) 1 BC 59 (Del), in connection with the grant of overdraft facility, fee of Rs 5000 for execution of documents was held to be a valuable consideration. *K. S. Bakshi v State*, AIR 2008 NOC 998 (Del), contract between landowner and builder for construction of multistoreyed building, the owner agreeing to block his assets till completion, good consideration, cheque issued in that connection was presumed to be for consideration.
11. ILR (1881) 3 All 221, *OLDFIELD* J at p. 228.
12. See also *Raja of Venkatagiri v Rao Bahadur Krishnayya*, (1948) 61 LW 545: AIR 1948 PC 150; *Adaitya Das v Prem Chand Mondal*, AIR 1929 Cal 369. In this case the defendant promised to bring a Thakur to the plaintiff’s house to preside over a dinner to be given to the plaintiff’s guests. The defendant failed to bring the Thakur and consequently the dinner was wholly wasted as no guest partook of it in the absence of the Thakur. The plaintiff’s action for damages was dismissed as he had done nothing on the desire of the promisor.
13. ILR (1886) 14 Cal 64.

amount. On the faith of the promised subscriptions the plaintiff entered into a contract with a contractor for the purpose of building the hall. But the defendant failed to pay the amount and contended that there was no consideration for his promise.

He was, however, held liable: Persons were asked to subscribe knowing the purpose for which the money was to be applied, they knew that on the faith of their subscription an obligation was to be incurred to pay the contractor for the work. The promise is: "In consideration of your agreeing to enter into a contract to erect, I undertake to supply money for it." The act of the plaintiff in entering into contract with the contractor was done at the desire of the defendant (the promisor) so as to constitute consideration within the meaning of Section 2(d).

It was indeed a promise to pay for the performance of an act and it could not have been revoked once the promisee entered performance. In England also "the law for centuries has been that an act done at the request of another, express or implied, is sufficient consideration to support a promise".<sup>14</sup> Writing in an article DENNING LJ says: "Nowadays there are some grounds for suggesting that an act may be good consideration even though it is not a benefit to the promisor nor a detriment to the promisee. If a man promises a charitable institution that he will pay £ 100 into its funds if it procures nine other persons to do the same, justice requires that his promise should be held binding on him as soon as it has procured the nine others to pay £ 100 each; but the act done by the institution is not a benefit to him nor a detriment to the institution." A trend of this kind is observable in a decision of the Supreme Court.<sup>15</sup> On the death of their father, his two sons picked up a clash. Their mother intervened writing to the junior son that in case his elder brother did not pay the sum of rupees fifty lakhs which was due to him out of the family assets, she would pay the same. The brother paid a part of the amount. The mother supplemented the payment to a certain extent, but she had still to pay the balance amount and for that she claimed a reduction in the computation of her net wealth. The Court allowed the deduction. The contract was a part of the family arrangement. It was not hit by Section 25 as purchase of family peace in such circumstances is good consideration.

A loan given to the son at the instance of his father who executed all the essential documents was held to be enforceable against the father.<sup>16</sup>

#### *Promises of charitable nature*

The decision of the Calcutta High Court in the *Kedarnath* case was followed by the Madras High Court in two cases in both of which the court

14. Rt. Hon. Sir ALFRED DENNING, *Recent Developments in the Doctrine of Consideration*, (1952) 15 Modern Law Review, p. 1.

15. *CWT v Her Highness Vijayaba*, (1979) 2 SCC 213: AIR 1979 SC 982.

16. *Radhakrishna Joshi v Syndicate Bank*, (2006) 1 AIR Kant 692: (2006) 2 All LJ (NOC) 403 (Kant).

laid down that “a promise to pay a subscription becomes enforceable as soon as any definite steps have been taken in furtherance of the object and on the faith of the promised subscription”.<sup>17</sup> In one of these cases:

A sum of Rs 5000 was promised by the defendant as a personal contribution for the purpose of constructing a bridge. He was held liable to pay the amount on the completion of the bridge.<sup>18</sup>

In a subsequent case, *Doraswami Iyer v Arunachala Ayyar*<sup>19</sup>, the Madras High Court explained the principle of *Kedarnath Bhattacharji v Gorie Mahomed* on the footing that there was not a bare promise to subscribe, but also a request that the promisee should do an act (construction of the town hall in that case), and that where there is no such request for an act the promise will be a bare promise and without any consideration. The facts of the case were:

The repair of a temple was in progress. As the work proceeded, more money was required and to raise this money subscriptions were invited and a subscription list raised. The defendant put himself down on the list for Rs 125 and it was to recover this sum that the suit was filed.

But no recovery was allowed. C. J. NARROW proceeded like this: “The plaintiff found the consideration for the promise as follows: That plaintiffs relying on the promise of the subscriber incurred liabilities in repairing the temple. The question is, does this amount to consideration? The definition of consideration in the Contract Act is that where at the desire of the promisor the promisee has done or abstained from doing something, such act or abstinence is called consideration. Therefore, the definition postulates that the promisee must have acted on something amounting to more than a bare promise. There must be some bargain between them in respect of which consideration has been given.... There must have been some request by the promisor to the promisee to do something in consideration of the promised subscription.”

The learned judge found support in the English case of *Hudson, re*<sup>20</sup> where the promise was to contribute a large sum of money for the payment

17. *Perumal Mudaliar v Sendanatha Mudaliar*, AIR 1918 Mad 311.

18. *District Board of Ramnad v D.K. Mahomed Ibrahim Sahib*, AIR 1933 Mad 524. There are some English authorities to the same effect. See, for example, *Soames, re*, (1837) 13 TLR 439. In this case S promised to leave the plaintiffs £ 3000 by will for opening of a school and its maintenance. The plaintiffs immediately established the school, which it was clear they would not have done but for Miss Soame's influence. But her will contained no such bequest. It was held that the plaintiffs were entitled to be paid £ 3000 from the estate by way of damages for breach of contract. Another case to the same effect is *Mountgarret, re*, (1913) 29 TLR 325. A testator promised to defray the cost of certain alterations in a Chapel in which he was interested, provided the total expense did not exceed a certain amount. Estimates were obtained and submitted to the testator, and thereafter the Provost of the Chapel entered into a formal contract for the work. The testator died after some of the work had been executed, but before a contract for the remainder had been entered into. Held, that the testator's estate was liable for the cost of so much only of the work in respect of which a contract had been entered into before the testator's death.

19. AIR 1936 Mad 135.

20. (1885) 54 LJ Ch 811.



of Chapel debts, the promisor having died after paying a large instalment, the balance could not be recovered from his executors. The claim was considered to be unsustainable in as much as the promisee had not undertaken any liability as part of the bargain with the promisor. Applying these principles to the present case, the learned judge said that there was no evidence of any request by the subscriber to the plaintiff to do the temple repairs.

### *Unilateral promises*

A unilateral promise is a promise from one side only and is intended to induce some action by the other party. “A unilateral contract refers to a gratuitous promise where only one party makes a promise without any return promise.”<sup>21</sup> The promisee is not bound to act, for he gives no promise from his side. But if he carries out the act desired by the promisor, he can hold the promisor to his promise. His act is at the same time an acceptance of and a consideration for the promise. “An act done at the request of the offeror in response to his promise is consideration, and consideration in its essence is nothing else but response to such a request.”<sup>22</sup>

It should be noted that in all the above cases where liability arose it arose only when the promisee had by doing some act, on the faith of the promise, altered his position. It follows, therefore, that where the promisee has done nothing, there is no consideration. Accordingly, in *Abdul Aziz v Masum Ali*,<sup>23</sup> the defendant promised Rs 500 to a fund started to rebuild a mosque but nothing had been done to carry out the repairs and reconstruction. The subscriber was, therefore, held not liable. Similarly, it has been pointed out in other cases that a mere promise to subscribe to a charitable institution cannot be sued upon.<sup>24</sup> Thus where the defendant had agreed to pay from time to time, out of his own pocket certain sums proportionate to the value of the goods imported by him, to a charitable society, the promise was held to be not enforceable, being without consideration.<sup>25</sup>



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21. *Aloka Bose v Parmatma Devi*, (2009) 2 SCC 582: AIR 2009 SC 1527. The court added that the observation in *Mohd Mohar Ali* case, AIR 1998 Gau 92 that an agreement of sale is a unilateral contract is not correct. Every sale presupposes somebody to sell and some other to buy.
  22. C.J. Hamson, *The Reform of Consideration*, (1938) 54 LQR 233, 234.
  23. AIR 1914 All 22: ILR (1914) 36 All 268.
  24. See, *Gopal v Trimbaik*, AIR 1953 Nag 195; *Doraswami Iyer v Arunachala Ayyar*, AIR 1936 Mad 135; *Jiban Krishna Mullick v Nirupama Gupta*, ILR (1926) 53 Cal 922; *CIT v Kameshwar Singh*, AIR 1953 Pat 231. In this case an assessee purchased Government securities and had agreed that the amount of interest on them would be paid to the Viceroy's War Purposes Fund for the duration of war—held, the agreement was not legally enforceable. Prejudice to rights is essential for the representation to be actionable under this rule. *Societe Italo—Belge Pour Le Commerce et l'Industrie v Palm & Veg Oils (Malaysia) Sdn Dhd*, (1982) 1 All ER 19.
  25. *Jamuna Das v Ram Kumar*, AIR 1937 Pat 358: 169 IC 396.

### *Revocation of unilateral promises*

There is yet another problem concerning such unilateral contracts. It is no doubt true that a promise which is given in return for an act is revocable before the promisee begins to alter his position by acting upon the promise. But may it be revoked after the promisee has commenced performance? If, for example, the promise is to pay a sum of money if the promisee walks from Lucknow to Kanpur, can it be revoked after the promisee has embarked upon the journey? The decision in *Kedarnath Bhattacharji v Gorie Mahomed*<sup>26</sup> suggests, though not in so many words, that such a revocation is impossible. The defendant, in that case, was held liable as soon as the contract for the construction of the hall was entered into.

The same appears from the decision of DENNING LJ in *Errington v Errington and Woods*.<sup>27</sup> The owner of a house had mortgaged it. The house was in the occupation of his son and daughter-in-law. He told them that the house would become their property if they paid off the mortgage debt in instalments and they commenced payment. In these circumstances, the court felt that it would be unjust if the promisor could revoke this promise at his pleasure. His Lordship said: "The father's promise was a unilateral contract... a promise of the house in return for their act of paying the instalments. It could not be revoked by him once the couple entered on performance of the act, but it would cease to bind him if they left it incomplete and unperformed."

Either way there is some difficulty. If the promisor is at liberty to revoke, he can frustrate the promisee at his pleasure. On the other hand, if he has no such liberty, he will be bound even though the promisee may stop performance at his sweet will. The House of Lords, therefore, suggested in *Morrison Steamship Co Ltd v Crown*<sup>28</sup> that the mere commencement of performance does not convert the offer into a contract in the sense that the promisor is bound to stay with his promise, but that if he revokes it, he may be sued for damages or on a *quantum meruit*.<sup>29</sup>

### *Promissory estoppel and Government agencies*

The position of the doctrine of promissory estoppel as against the Government and its agencies is thus summarised by RM SAHAI J of the Supreme Court in *Amrit Banaspati Co Ltd v State of Punjab*:<sup>30</sup>

26. ILR (1886) 14 Cal 64.

27. (1952) 1 KB 290 at p. 295 (CA).

28. (1924) 20 Ll LR 283.

29. For further reading see J.C. Smith, *Unilateral Contracts and Consideration*, (1953) 69 LQR 99 and 106. The Supreme Court has also held in *Lakshmanaswami Mudaliar v LIC*, AIR 1963 SC 1185, 1190: 1963 Supp (2) SCR 887, 888, that the mere acceptance or retention of donated money does not amount to consideration so as to prevent the donor from recovering back his donation. *Subbash Chandra v Nagar Mahapalika*, AIR 1984 All 228, where the donee promised to spend Rs 100 on the maintenance of the gifted property, held, no consideration; it was only a gift.

30. (1992) 2 SCC 411: AIR 1992 SC 1075, 1077.

Law of promissory estoppel which found its most eloquent exposition in *Union of India v Indo Afghan Agencies Ltd.*<sup>31</sup> crystallised in *Motilal Padampat Sugar Mills v State of U.P.*<sup>32</sup> as furnishing cause of action to a citizen, enforceable in a court of law, against the Government if it or its officials in the course of their authority extended any promise which created or was capable of creating legal relationship, and it was acted upon by the promisee, irrespective of any prejudice. It was reiterated in *Union of India v Godfrey Philips India Ltd*<sup>33</sup> and was taken further when it was held that no duty of excise was assessable on cigarettes manufactured by the assessee by including the cost of corrugated fibre board containers when it was clearly represented by the Central Board of Excise and Customs in response to the submission made by the Cigarette Manufacturers' Association and the representation was approved and accepted by the Central Government that the cost of containers would not be included in the value of cigarettes for the purpose of assessment of excise duty. In *Delhi Cloth and General Mills Ltd v Union of India*<sup>34</sup> it was held: 'All that is now required is that the party asserting the estoppel must have acted upon the assurance given to him. Must have relied upon the representation made to him. It means that the party has changed or altered his position by relying on the assurance or representation. The alteration of his position by the party is the only indispensable requirement of the doctrine. It is not necessary to prove further any damage, detriment or prejudice to the party asserting the estoppel.'

In *Pournami Oil Mills v State of Kerala*<sup>35</sup> the Government was not permitted to go back on its earlier promise of wider exemption from sales tax in pursuance of which certain industries were set up. A subsequent notification curtailing the exemption was held to be applicable to industries established after the notification. A promise which is against public policy or in violation of a statutory prohibition cannot be the foundation of an estoppel.<sup>36</sup>

#### *Estoppel of licensee*

The party who was granted a liquor licence was held to be estopped from saying afterwards that some of the restrictions imposed upon his trade freedom, particularly the one under which the Government reserved with it

31. AIR 1968 SC 718: (1968) 2 SCR 366.

32. (1979) 2 SCC 409: AIR 1979 SC 621: (1979) 2 SCR 641.

33. (1985) 4 SCC 369, 370: AIR 1986 SC 806.

34. (1988) 1 SCC 86: AIR 1987 SC 2414, 2419: (1988) 1 SCR 383.

35. 1986 Supp SCC 728: AIR 1987 SC 590 writ jurisdiction is available when promissory estoppel is involved but not otherwise for enforcing a Government contract. *Chamundi Roller Flour Mills v FCI*, (1992) 1 Kant LJ 579; *Prakash v Union of India*, (1994) 2 Bom CR 53, even in matters of contract, the Government must act fairly (Government lessee in this case), writ petition lies against unfairness.

36. *Amrit Banaspati Co Ltd v State of Punjab*, (1992) 2 SCC 411: AIR 1992 SC 1075, promise to refund sales tax amounts already paid was held to be not capable of creating an estoppel.

the power to vary issue prices, were unreasonable. Unreasonableness has to be considered in the totality of the circumstances including public interest. Liquor consumption has to be reduced and, therefore, free trade of such an item cannot be encouraged. The power to vary issue prices is a method of exercising control of this trade. The courts will only prevent a crushing use of this power. Such power does not also offend Section 29 of the Contract Act because there is no uncertainty about the nature of the price variation clause. Its unreasonable use can always be prevented under writ jurisdiction.<sup>37</sup>

A person, who had acquired title to the land of a Council by adverse possession, agreed subsequently to hold the same under a term licence from the Council. On the expiry of the term the Council told him to hand over possession. He tried to assert his title by adverse possession. He was not allowed to do so. Whatever rights he had acquired became substituted under the new arrangement which he voluntarily accepted. The new arrangement constituted a promissory estoppel against him.<sup>38</sup>

## PRIVITY OF CONTRACT AND OF CONSIDERATION

### “Promisee or any other person”

The second notable feature of the definition of consideration in Section 2(d) is that the act which is to constitute a consideration may be done by “the promisee or any other person”. It means; therefore, that as long as there is a consideration for a promise, it is immaterial who has furnished it. It may move from the promisee, or, if the promisor has no objection, from any other person. This principle had its genesis in the English common law, having been adopted by the Court of King’s Bench as early as 1677 in *Dutton v Poole*:<sup>39</sup>

A person had a daughter to marry and in order to provide her a marriage portion he intended to sell a wood of which he was possessed at the time. His son (the defendant) promised that if ‘the father would forbear to sell at his request he would pay the daughter £1000’. The father accordingly forbore but the defendant did not pay. The daughter and her husband sued the defendant for the amount.

It is clear that the defendant gave this promise to his father and it was the father alone who, by abstaining from selling the wood, had furnished consideration for the promise. The plaintiff was neither privy to the contract nor interested in the consideration. But it is equally clear that the whole object of the agreement was to provide a portion to the plaintiff. It would have been highly inequitable to allow the son to keep the wood and yet to deprive his sister of her portion. He was accordingly held liable.

37. *Lekh Raj v State of Rajasthan*, (1987) 1 Raj LR 661.

38. *Colchester Borough Council v Smith*, (1991) 2 WLR 540.

39. Court of King’s Bench, (1677) 2 Levins 210: 83 ER 523.

*Position of beneficiary who is not party*

Nearly two hundred years later in 1861 in *Tweddle v Atkinson*<sup>40</sup> the Court of Queen's Bench refused to follow this principle.

The plaintiff was to be married to the daughter of one G and in consideration of this intended marriage G and the plaintiff's father entered into a written agreement by which it was agreed that each would pay the plaintiff a sum of the money. G failed to do so and the plaintiff sued his executors. WHITMAN J considered it to be an established principle 'that no stranger to the consideration can take advantage of a contract, although made for his benefit'.

Thus, although the sole object of the contract was to secure a benefit to the plaintiff, he was not allowed to sue as the contract was made with his father and not with him.

The case laid the foundation of what subsequently came to be known as the doctrine of "privity of contract", which means that a contract is a contract between the parties only and no third person can sue upon it even if it is avowedly made for his benefit.<sup>41</sup> Referring to this in *Drive Yourself Hire Co (London) Ltd v Strutt*<sup>42</sup> DENNING LJ suggested that the doctrine never arose until 1861 and then observed:

For the last two hundred years before 1861 it was settled law that, if a promise in a simple contract was made expressly for the benefit of a third person in such circumstances that it was intended to be enforceable by him, then the common law would enforce the promise at his instance, although he was not a party to the contract.<sup>43</sup>

The principle was affirmed by the House of Lords in *Dunlop Pneumatic Tyre Co v Selfridge & Co Ltd*.<sup>44</sup>

Plaintiffs (Dunlop & Co) sold certain goods to one Dew & Co and secured an agreement from them not to sell the goods below the list price and that if they sold the goods to another trader they would obtain from him a similar undertaking to maintain the price list. Dew & Co sold the motor tyres to the defendants (Selfridge & Co) who agreed not to sell the tyres to any private customer at less than the list prices. The plaintiffs sued the defendants for breach of this contract.

It was held that assuming that the plaintiffs were undisclosed principals, no consideration moved from them to the defendants and that the contract was unenforceable by them. Lord Viscount HALDANE most emphatically declared that:

40. 123 ER 762: 1 B&S 23, 393: 30 LJ QB 218: 4 LT 468.

41. *Kanta Devi Berllia v Mohit Jhunjhunwala*, (2006) 2 CHN 161, nor can such a person be sued on the contract.

42. (1954) 1 QB 250 at p. 272: (1953) 3 WLR 1111.

43. See a note by E.J.P. on *Privity of Contract*, (1954) 70 LQR 467.

44. 1915 AC 847.

In the law of England certain principles are fundamental. One is that only a person who is a party to a contract can sue on it. Our law knows nothing of a *jus quaesitum tertio* arising by way of contract. Such a right may be conferred by way of property, as, for example under a trust, but it cannot be conferred on a stranger to a contract as a right to enforce the contract *in personam*. A second principle is that if a person with whom a contract not under seal has been made is to be able to enforce it, consideration must have been given by him.

### *Fundamental propositions of English Law*

Stated in other words the two fundamental propositions of English law referred to by his Lordship are:

(1) Consideration must move from the promisee and the promisee only. If it be furnished by any other person, the promisee becomes a stranger to the consideration and, therefore, cannot enforce the promise.<sup>45</sup>

(2) A contract cannot be enforced by a person who is not a party to it even though it is made for his benefit. He is a stranger to the contract and can claim no rights under it.<sup>46</sup>

### Privity of consideration

The former of these two propositions is not at all applicable in India. Here, in view of the clear language used in defining consideration in Section 2(d), it is not necessary that consideration should be furnished by the promisee. A promise is enforceable if there is some consideration for it and it is quite immaterial whether it moves from the promisee or any other person. The leading authority is the decision of the Madras High Court in *Chinnaya v Ramayya*:<sup>47</sup>

An old lady, by deed of gift, made over certain landed property to the defendant, her daughter. By the terms of the deed, which was registered, it was stipulated that an annuity of Rs 653 should be paid every year to the plaintiff, who was the sister of the old woman. The defendant on the same day executed in plaintiff's favour an *Iqrarnama* (agreement) promising to give effect to the stipulation. The annuity was, however, not paid and the plaintiff sued to recover it.

It was clear that the only consideration for the defendant's promise to pay the annuity was the gift of certain lands by the old woman to the defendant.

45. See Anson, PRINCIPLES OF THE ENGLISH LAW OF CONTRACT (23rd Edn by A.G. Guest, 1971) 89; Cheshire and Fifoot, LAW OF CONTRACT (8th Edn, 1972) 64.

46. See Anson, *ibid* at p. 370; Cheshire and Fifoot, *ibid* at pp. 380–82; Arthur L. Corbin, *Contracts for the Benefit of Third Persons*, (1930) 46 LQR 12. In this article the learned writer maintains that the doctrine is not after all as dogmatic as the leading authors on the English Law of Contract assert.

47. ILR (1876–82) 4 Mad 137. Another illustration: *Samuel Pillai v Ananthanatha Pillai*, (1883) 6 Mad 351.

The defendant, therefore, tried to defend herself on the ground that the promisee (the plaintiff) had furnished no consideration. Briefly, the whole situation was this: the defendant's promise was given to the plaintiff, but consideration was furnished by the plaintiff's sister. The court could have easily allowed the plaintiff to recover the annuity, as consideration given by "any other person" is equally effective. The court reached the same result but on a somewhat different ground. INNES J tried to equate the situation with the facts of *Dutton v Poole*. In that case the defendant's sister would have got her marriage portion but for the defendant's promise. In the present case also it appeared that the plaintiff was already receiving from her sister an annuity of like amount out of the estate and when the estate was handed over to the defendant it was stipulated that the payment to the plaintiff should be continued and she promised accordingly. That means that the failure to keep the promise would have deprived the plaintiff of an amount which she was already receiving and it is a legal commonplace that if a promise causes some loss to the promisee, that is sufficient consideration for the promise. Thus the plaintiff had given consideration.

Justice KINDERSLEY also came to the same conclusion, but on a different ground. According to him the deed of gift and the defendant's promise to pay the annuity were executed simultaneously and, therefore, they should be regarded as one transaction and there was sufficient consideration for that transaction.

American judicial opinion is in favour of this rule. In the words of the great American writer Williston: "The rule that consideration must move from the promisee is somewhat technical, and in a developed system of contract law there seems no good reason that why A should not be able for a consideration received from B to make an effective promise to C. Unquestionably he may in the form of a promissory note, and the same result is generally reached in this country in the case of an ordinary simple contract."<sup>48</sup>

### Privity of contract

The rule of "privity of contract" which means that a stranger to contract cannot sue has taken firm roots in the English Common Law. But the principle has been generally criticised.<sup>49</sup> In 1937, the Law Revision Committee, under the chairmanship of Lord Wright, also criticised the doctrine and recommended its abolition. In its Sixth Interim Report the Committee stated:

Where a contract by its express terms purports to confer a benefit directly on a third party, the third party shall be entitled to enforce the provision in his own name, provided that the promisor shall be entitled

48. Samuel Williston, *Contracts for the Benefit of a Third Person*, (1901–02) 15 Harv L Rev 767.

49. Professor Corbin, *Contract for the Benefit of Third Person*, (1930) 46 LQR 12. Andrew Tettenborn, *Third Party Contracts—Pragmatism from the Law Commission*, 1996 JBL 602; Peter Kincaid, *Privity Reform in England*, (2000) 116 LQR 43; M.H. Ogilvie, *Privity of Contract in the Supreme Court of Canada: Fare Thee Well or Welcome Back*, 2002 JBL 163.

to raise against the third party any defence that would have been valid against the promisor ....

Lord Justice DENNING has also criticised the rule in a number of cases,<sup>50</sup> in one of which his Lordship observed:<sup>51</sup>

It (the privity principle) has never been able entirely to supplant another principle whose roots go much deeper. I mean the principle that a man who makes a deliberate promise which is intended to be binding, that is to say, under seal or for good consideration, must keep his promise; and the Court will hold him to it, not only at the suit of the party who gave the consideration, but also at the suit of one who was not a party to the contract, provided that it was made for his benefit and that he has a sufficient interest to entitle him to enforce it, subject always, of course, to any defences that may be open on the writs.

In the subsequent case of *Beswick v Beswick*<sup>52</sup> the Court of Appeal adopted the same approach. In that case:

*B* was a coal merchant. The defendant was assisting him in his business. *B* entered into an agreement with the defendant by which the business was to be transferred to the defendant. *B* was to be employed in it as a consultant for his life and after his death the defendant was to pay to his widow an annuity of £5 per week, which was to come out of the business. After *B*'s death, the defendant paid *B*'s widow only one sum of £5. The widow brought an action to recover the arrears of the annuity and also to get specific performance of the agreement.

It was held that she was entitled to enforce the agreement. Thus the plaintiff was allowed to enforce the agreement in her personal capacity, although she was not a party to it and it was considered not necessary to infer a trust in favour of the plaintiff. Lord DENNING MR concluded with the words:

Where a contract is made for the benefit of a third person who has a legitimate interest to enforce it, it can be enforced by the third person in the name of the contracting party or jointly with him or, if he refuses to join, by adding him as a defendant. In that sense, and it is a very real sense, the third person has a right arising by way of contract. He has an interest which will be protected by law. The observations to the contrary ... are

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50. See *Smith & Snipes Hall Farm Ltd v River Douglas Catchment Board*, (1949) 2 KB 500 (CA); *Drive Yourself Hire Co (London) Ltd v Strutt*, (1954) 1 QB 250; (1953) 3 WLR 1111.
  51. In first of the above-stated cases, at pp. 514–15. Catherine Mac Millan, *A Birthday Present for Lord Denning; The Contracts (Rights of Third Parties) Act, 1999*, (2000) 63 MLR 721 at pp. 726, 730–31. This New Zealand Act permits a person who is not a party to a contract to enforce a term of the contract in two situations: (1) where the contract expressly so provides and (2) where the term purports to confer a benefit except where on proper construction, it appears that the parties to the contract did not intend that the term should be enforceable by the third party. S. M. Waddams, *Privity of Contract in the Supreme Court of Canada*, (1993) 109 LQR 349.
  52. 1968 AC 58; (1967) 3 WLR 932.

in my opinion erroneous. It is different when a third person has no legitimate interest, as when he is seeking to enforce the maintenance of prices to the public disadvantage, as in *Dunlop Pneumatic Tyre v Selfridge & Co Ltd*<sup>53</sup> or when he is seeking to rely not on any right given to him by the contract, but on an exemption clause, seeking to exempt himself from his just liability.

The case shows that a reform, as was recommended by the Law Revision Committee in 1937, is long overdue and if Parliament takes any step in this respect that would hardly be revolutionary.

Another such observation is to be seen through the words of STEYN LJ in *Darlington Borough Council v Wiltshire Northern Ltd*.<sup>54</sup>

“The case for recognising a contract for the benefit of a third party is simple and straightforward. The autonomy of the will of the parties should be respected. The law of contract should give effect to the reasonable expectations of contracting parties. Principle certainly requires that a burden should not be imposed on a third party without his consent. But there is no doctrinal, logical or policy reason why the law should deny effectiveness to a contract for the benefit of a third party where that is the expressed intention of the parties. Moreover, often the parties, and particularly third parties, organise their affairs on the faith of the contract. They rely on the contract. It is therefore unjust to deny effectiveness to such a contract. I will not struggle further with the point since nobody seriously asserts the contrary....”

But the House of Lords did not approve the approach adopted by Lord DENNING MR and found for the plaintiff on a different ground.<sup>55</sup> Lord REID said that the plaintiff “in her personal capacity has no right to sue, but she has a right as administratrix of her husband’s estate to require the appellant to perform this obligation under the agreement”. Lord PEARCE put it like this: “The estate (though not the widow personally) can enforce it.”<sup>56</sup>

In some earlier cases also the House of Lords showed no preference for Lord DENNING’s approach. For example, in *Scrutons Ltd v Midland Silicones Ltd*<sup>57</sup> referring to the argument that the orthodox view which crystallised a century ago in *Tweddle v Atkinson* (1861) and finally established in *Dunlop v Selfridge* (1915) should be rejected, Viscount SIMOND said that “certain statements which appear to support it in recent cases such as *Smith v River Douglas Catchment Board*<sup>58</sup> and *White v John Warwick & Co Ltd*<sup>59</sup> must be rejected. If the principle of *jus quae situm tertio* is to be introduced

53. 1915 AC 847.

54. (1995) 1 WLR 68 at p. 903–04 (CA).

55. *Beswick v Beswick*, 1968 AC 58; (1967) 3 WLR 932.

56. As stated in Anson, THE LAW OF CONTRACT (23rd Edn by A.G. Guest, 1971) 388.

57. 1962 AC 446; (1962) 2 WLR 186 (HL).

58. (1949) 2 KB 500; (1949) 2 All ER 179.

59. (1953) 1 WLR 1285 (CA).

into our law, it must be done by Parliament after a due consideration of its merit and demerits". His Lordship emphasised that "the law is developed by the application of old principles to new circumstances. Therein lies its genesis. Its reform by the abrogation of those principles is the task not of the courts of law but of Parliament".

### *Position in India: Decisions following English Law*

In India also there has been a great divergence of opinion in the courts as to how far a stranger to a contract can enforce it. There are many decided cases which declare that a contract cannot be enforced by a person who is not a party to it and that the rule in *Tweddle v Atkinson*<sup>60</sup> is as much applicable in India as it is in England. But there is no provision in the Contract Act either for or against the rule. The Privy Council extended the rule to India in its decision in *Jamna Das v Pandit Ram Autar Pande*.<sup>61</sup>

A borrowed Rs 40,000 by executing a mortgage of her zamindari in favour of B. Subsequently she sold the property to C for Rs 44,000 and allowed C, the purchaser, to retain Rs 40,000 of the price in order to redeem the mortgage if he thought fit. B sued C for the recovery of the mortgage money, but he could not succeed because he was no party to the agreement between A and B.

Lord MACNAUGHTAN, in his very short judgment, said that the undertaking to pay back the mortgagee was given by the defendant to his vendor. "The mortgagee has no right to avail himself of that. He was no party to the sale. The purchaser entered into no contract with him, and the purchaser is not personally bound to pay this mortgage debt."<sup>62</sup>

Thus, where all that appears is that a person transfers property to another and stipulates for the payment of money to a third person, a suit to enforce that stipulation by the third party will not lie.<sup>63</sup> But the party making the contract may sue for specific performance for the benefit of the third party.<sup>64</sup> Similarly, where on a lease of certain *muafi* land, the lessees undertook, as between themselves and their lessor, to be responsible for the payment to the zamindar of certain sums which the *muafid* was primarily bound to pay, it was held that the zamindar could not enforce this covenant by a

60. 123 ER 762: 1 B&S 23, 393: 30 LJ QB 218: 4 LT 468.

61. (1911-12) 39 IA 7: ILR (1911-12) 34 All 63. *Babu Ram Budhu Mal v Dhan Singh Bishan Singh*, AIR 1957 Punj 169, the first mortgagee was not allowed to recover the money retained by the second mortgagee under the agreement between the owner and second mortgagee.

62. At p. 9. *Tham Saw Fong v Teh Teng Seng Realty*, (1990) 2 Curr LJ 860 (Malaysia), High Court, Ipoh, where the directors of a company were not permitted to sue a person who purported to sell land to their company and about whom they alleged that he defaulted in giving vacant possession.

63. *Subbu Chetti v Arunachalam Chettiar*, ILR (1930) 53 Mad 270: AIR 1930 Mad 382.

64. *K. Gopalasamy Chetty v Selliamman Koil Coop Housing Society Ltd*, (2003) 1 ICC 184 (Mad).

suit against the lessees.<sup>65</sup> In still another case<sup>66</sup>, the plaintiff could not get a decree against the appellant for his salary on the basis of an agreement entered into by the plaintiff with another person.<sup>67</sup>

In the opinion of RANKIN CJ this seems to be the effect of the Contract Act itself. In *Krishna Lal Sadhu v Promila Bala Dasi*<sup>68</sup> he observed: Not only, however, is there nothing in Section 2 to encourage the idea that contracts can be enforced by a person who is not a party to the contract, but this notion is rigidly excluded by the definition of "promisor" and "promisee" .... In my judgment, it is erroneous ... to suppose that in India persons who are not parties to a contract can be permitted to sue thereupon ....

Consequently, a Hindu assured's wife's action to recover the money due under her deceased husband's policy was rejected because she, though a nominee under the policy, was not a party to the contract between the deceased and the insurance company and no interest passed to her merely because she was named in the policy.<sup>69</sup>

#### *Decisions not following English Law*



CASE PILOT

There is, however, another line of thinking also which is mainly based upon an observation of the Privy Council in *Nawab Khwaja Muhammad Khan v Nawab Hussaini Begum*.<sup>70</sup> Their Lordships observed:

In India and among communities circumstanced as the Mahomedans, among whom marriages are contracted for minors by parents and guardians it might occasion serious injustice if the common law doctrine was applied to agreements or arrangements entered into in connection with such contracts.

This statement has been taken by some High Courts as laying down the rule that Indian courts are not bound by the rule in *Tweddle v Atkinson*.<sup>71</sup> Accordingly, it has been observed by the Madras High Court:<sup>72</sup>

65. *Mangal Sen v Mohd Husain*, ILR (1915) 37 All 115.

66. *State of Bihar v Charanjitlal Chadha*, AIR 1960 Pat 139.

67. This line of thinking has been followed in insurance cases also. See, for example, *Shankar Vishvanath v Umabai*, ILR (1913) 37 Bom 471, where the beneficiary of an insurance policy could claim no right under the contract between the assured and the insurance company because there was nothing to show that the plaintiff was either the promisor or the promisee and, therefore, a party to the agreement. See also *Oriental Govt Security Life Assurance Ltd v Venteedu Ammiraju*, ILR (1912) 35 Mad 162, where it was held that the contract between the company and the assured gives no right of action to the beneficiary named.

68. AIR 1928 Cal 518; ILR (1928) 55 Cal 1315.

69. Other examples of the rule are: *Protapmull Rameswar v State of W.B.*, (1956) 61 CWN 78; *Chhangamal Harpaldas v Dominion of India*, AIR 1957 Bom 276. In the last-mentioned case the court held that a bare consignee, who is not a party to the contract of consignment, and who is not the owner of the goods, cannot maintain a suit for compensation for loss of or damage to the goods.

70. (1909-10) 37 IA 152.

71. 123 ER 762; 1 B&S 23, 393; 30 LJ QB 218; 4 LT 468.

72. *Munisami Naicker v Vedachala Naicken*, AIR 1928 Mad 23.

There is ample authority for the proposition that in this country, and indeed in a certain class of cases in England where a contract is made between 'A' and 'B' for the benefit of 'C', 'C' is entitled to sue the defaulting party. It is unnecessary to cite authorities, but the principle is firmly established for this country by the decision of the Privy Council in *Nawab Khwaja Muhammad Khan v Nawab Hussaini Begum*.<sup>73</sup>

Similarly, the Calcutta High Court observed:<sup>74</sup> Nor is there anything in the Indian Contract Act, which prevents the recognition of a right in a third party to enforce a contract made by others, which contains a provision for his benefit.

Again, JENKINS CJ said in another important case:<sup>75</sup> We now have ample authority for saying that the administration of justice in British India is not to be in any way hampered by the doctrine laid down in *Tweddle v Atkinson*.<sup>76</sup> That I take to be the result of the decision of the Privy Council in *Nawab Khwaja Muhammad Khan v Nawab Hussaini Begum*.<sup>77</sup>

#### *Supreme Court upholds privity*

The Supreme Court of India has expressed itself in favour of the rule in *Tweddle v Atkinson*. In *M.C. Chacko v State Bank of Travancore*,<sup>78</sup> SHAH Ag. CJ (afterwards CJ) endorsed the statement of RANKIN CJ in *Krishna Lal Sadhu v Promila Bala Dasi*<sup>79</sup> and after referring to the observation of Lord HALDANE in *Dunlop v Selfridge*, said:

The Judicial Committee applied that rule in *Nawab Khwaja Muhammad Khan v Nawab Hussaini Begum*.<sup>80</sup> In a later case, *Jamna*

73. (1909–10) 37 IA 152.

74. *Kshirodebihari Dutta v Mangobinda Panda*, ILR (1934) 61 Cal 841: AIR 1934 Cal 682, *Per* Lord WILLIAMS J at p. 857. *Raymond Woollen Mills Ltd v Coal India Ltd*, (1998) 1 CHN 53, where the court said that the doctrine of privity of contract has undergone a change in recent years and, therefore, a principal can initiate a legal action against a third party although the principal was only one of the beneficiaries under the contract. The court cited the decision of the High Court of Australia in *Trident General Insurance v McNiece Bros P Ltd*, (1988) 165 CLR 107: 1989 Comm LR 1 where the court observed: "The long-established rule that a contract could be enforced only by the parties to that contract had caused considerable injustice and inconvenience in the context of contracts of liability insurance. The existence of the privity rule had provoked criticism by judges, academics and law reform agencies alike and in some jurisdictions statutory abrogation of the rule had occurred. It would be unjust in the present case to apply the rule and preclude the respondent from enforcing the policy of insurance." The court also cited *Indian Mutual General Insurance Society Ltd v Himalaya Finance and Construction Co*, AIR 1974 Del 114, where the ratio of the decision was that the owners of a vehicle who really have legal interest in the property could very easily come within the definition of beneficiary, though not party to the policy because the same was taken out by the hirer.

75. *Debarayan Datt v Chunilal Ghose*, ILR (1914) 41 Cal 137.

76. 123 ER 762: 1 B&S 23, 393: 30 LJ QB 218: 4 LT 468.

77. (1909–10) 37 IA 152.

78. (1969) 2 SCC 343: AIR 1970 SC 504.

79. AIR 1928 Cal 518: ILR (1928) 55 Cal 1315.

80. (1909–10) 37 IA 152.

*Das v Pandit Ram Autar Pande*,<sup>81</sup> the Judicial Committee pointed out that the purchaser's contract to pay off a mortgage could not be enforced by the mortgagee who was not a party to the contract. It must therefore be taken as well-settled that except in the case of a beneficiary under a trust or in the case of a family arrangement, no right may be enforced by a person who is not a party to contract.<sup>82</sup>

The facts of the case were as follows:

The Highland Bank was indebted to the State Bank of Travancore under an overdraft. One M was the manager of the Highland Bank and his father K had guaranteed the repayment of the overdraft. K gifted his properties to the members of his family. The gift deed provided that the liability, if any, under the guarantee should be met by M either from the bank or from the share of property gifted to him. The State Bank attempted to hold M liable under this provision of the deed.

But he was held not liable. "The State Bank not being a party to the deed was not bound by the covenants in the deed, nor could it enforce the covenants. It is settled law that a person not a party to a contract cannot enforce the terms of the contract."

The representatives who held the properties of K would have been liable to pay out of the property if the action against them had not been time barred.

### Exceptions to privity rule

In the course of time, the courts have introduced a number of exceptions in which the rule of privity of contract does not prevent a person from enforcing a contract which has been made for his benefit but without his being a party to it. Many of the exceptions are connected with the special branches of the law of contract, such as negotiable instruments, agency, bill of lading, railway receipts, transfer of property, etc. Some of the most commonly known exceptions may be considered here.

#### 1. Beneficiaries under trust or charge or other arrangements

A person in whose favour a charge or other interest in some specific property has been created may enforce it though he is not a party to the contract. The decision of the Privy Council in *Nawab Khwaja Muhammad Khan v Nawab Hussaini Begum*<sup>83</sup> is illustrative of this principle. The facts were:

81. (1911-12) 39 IA 7; ILR (1911-12) 34 All 63.

82. See, *M.C. Chacko v State Bank of Travancore*, (1969) 2 SCC 343; AIR 1970 SC 504 at pp. 347-48. Reaffirmed by the Supreme Court in *P.R. Subramania Iyer v Lakshmi Ammal Lakshmi Ammal*, (1973) 2 SCC 54; *Fatehchand Murlidhar v Maharashtra SEB*, AIR 1985 Bom 71, where it was held that where the supply of electricity was granted to the occupier of a premises, its owner could not be sued for dues, there being no privity.

83. (1909-10) 37 IA 152.

The appellant executed an agreement with the respondent's father that in consideration of the respondent's marriage with his son (both being minors at the time) he would pay to the respondent Rs 500 a month in perpetuity for the betel-leaf expenses and charged certain properties with the payment, with power to the respondent to enforce it. The husband and wife separated on account of a quarrel and the suit was brought by the plaintiff-respondent for the recovery of the arrears of this annuity.

It was held that the respondent, although no party to the agreement, was clearly entitled to proceed in equity to enforce her claim. "Here the agreement executed by the defendant (appellant) specifically charges immovable property for the allowance which he binds himself to pay to the plaintiff (respondent); she is the only person beneficially entitled under it." An example of a trust in favour of a third party is to be found in the facts of another Privy Council decision, namely, *Rana Uma Nath Bakhsh Singh v Jang Bahadur*:<sup>84</sup> *U* was appointed by his father as his successor and was put in possession of his entire estate. In consideration thereof *U* agreed with his father to pay a certain sum of money and to give a village to *J*, the illegitimate son of his father, on his attaining majority. It was held that in the circumstances mentioned above a trust was created in favour of *J* for the specified amount and the village. Hence he was entitled to maintain the suit.<sup>85</sup>

In England also there is a line of cases in which "trust" has been used as a device for holding the promisor to his promise. One such case is *Gregory & Parker v Williams*:<sup>86</sup>

Parker was indebted to both Williams and Gregory. Parker assigned all his property to Williams in satisfaction of the debt and Williams promised to pay Parker's debt to Gregory. Williams failed to pay. But he was held liable to pay Gregory in terms of his promise with Parker.

Another illustration is *Touche v Metropolitan Rly Warehousing Co.*:<sup>87</sup>

The plaintiff rendered services to the promoters of the defendant-company and they promised that he should receive £2000 from the company. Later, when the company was formed, its articles of association provided that £2000 should be paid to Walker, one of the promoters, for the benefit of the plaintiff.

The plaintiff sued the company in his own name. It was held that the defendant-company's promise was for the benefit of the plaintiff and that the plaintiff had the right to obtain the benefit of the arrangement entered into between the promoter and the company.

84. AIR 1938 PC 245.

85. In *Kshirodebihari Dutta v Mangobinda Panda*, ILR (1934) 61 Cal 841: AIR 1934 Cal 682.

86. (1817) 3 Mer 582: 36 ER 224.

87. (1871) 6 Ch App 671.

Trust may be actual or constructive. But in general the courts are slow to infer a constructive trust. Explaining the judicial approach in *Ramchand v Thakur Janki Ballabhji Maharaj*<sup>88</sup> SHAH, AG CJ (afterwards CJ) said:

For creating a charge on immovable property no particular form of words is needed; ... But in order that a charge may be created, there must be evidence of intention disclosed by the deed that a specified property or fund was intended to be made liable to satisfy the debt. The recitals in the deed (in the present case) do not evidence any intention of the donor to create a charge in favour of the State Bank; they merely set out an arrangement between the donor and the members of his family that the liability under the guarantee will be satisfied by M.C. Chacko out of the property allotted to him under the deed.

Constructive trust is created in favour of an addressee of insured articles and he can claim compensation from the Central Government on non-delivery of such articles.<sup>89</sup>

An airline company made an arrangement with a hotel for accommodating its passengers. One of the passengers so accommodated was injured because of negligent maintenance of the hotel premises. His action directly against the hotel-keeper was allowed. The court said the doctrine of privity of contract is subject to many exceptions, one of them being that a beneficiary can sue on a contract which is meant only to provide some benefits to him.<sup>90</sup>

## 2. Marriage settlement, partition or other family arrangements

Where an agreement is made in connection with marriage, partition or other family arrangement and a provision is made for the benefit of a person, he may take advantage of that agreement although he is no party to it. For example, in *Rose Fernandez v Joseph Gonsalves*,<sup>91</sup> a girl's father entered into an agreement for her marriage with the defendant, it was held that the girl after attaining majority could sue the defendant for damages for breach of the promise of marriage and the defendant could not take the plea that she was not a party to the agreement. Similarly, where two brothers,

88. (1969) 2 SCC 313.

89. *Chaudhri Amir Ullah v Central Govt*, (1959) 57 All LJ 271; *Postmaster General v Ram Kripal Sahu*, AIR 1955 Pat 442. *Punjab National Bank v Khazan Singh*, AIR 2004 P&H 282, financier of vehicle is the beneficiary of the insurance policy on the vehicle, entitled to be impleaded in a proceeding under an accident claim.

90. *Klaus Mittelbacher v East India Hotels Ltd*, AIR 1997 Del 201 at p. 230. In *Greene v Chelsea Borough Council*, (1954) 2 QB 127: (1954) 3 WLR 12, the husband had taken premises on licence from the defendant. A ceiling fell on his wife injuring her. She was allowed to sue the owner in her own right as a beneficiary under the contract. *Prithvi Singh v Banshi Lal*, AIR 2004 Raj 100, landlord gave a piece of land to his tenant in lieu of the latter permitting passage to a person who had purchased a part of the property. Denial of such passage to the purchaser on the ground that there was no privity between him and the tenant was held to be improper.

91. ILR (1924) 48 Bom 673: AIR 1925 Bom 97.

on a partition of joint properties, agreed to invest in equal shares a certain sum of money for the maintenance of their mother she was held entitled to require them to make the investment.<sup>92</sup> Also, where a daughter along with her husband agreed that she will maintain her mother if the property of the father is conveyed to them, the mother was held entitled to maintain a suit for specific performance although the agreement was between the father, daughter and the daughter's husband only and the mother was not a party to it.<sup>93</sup> Another interesting case is *Daropti v Jaspat Rai*.<sup>94</sup> The defendant's wife left him because of his cruelty. He then executed an agreement with her father, promising to treat her properly, and if he failed to do so, to pay her monthly maintenance and to provide her with a dwelling. Subsequently she was again ill-treated by the defendant and also driven out. She was held entitled to enforce the promise made by the defendant to her father.

### 3. Acknowledgment or estoppel

Where by the terms of a contract a party is required to make a payment to a third person and he acknowledges it to that third person, a binding obligation is thereby incurred towards him. Acknowledgment may be express or implied. This exception covers cases where the promisor by his conduct, acknowledgment, or otherwise, constitutes himself an agent of the third party. The case of *N. Devaraja Urs v Ramakrishniah*<sup>95</sup> is a good example: A sold his house to B under a registered sale deed and left a part of the sale price in his hands desiring him to pay this amount to C, his creditor. Subsequently B made part-payments to C informing him that they were out of the sale price left with him and that the balance would be remitted immediately. B, however, failed to remit the balance and C sued him for the same. The suit was held to be maintainable. "Though originally there was no privity of contract between B and C, B having subsequently acknowledged his liability, C was entitled to sue him for recovery of the amount."

An illustration of acknowledgment by conduct is *Kshirodebihari Datta v Mangobinda Panda*:<sup>96</sup> The tenant and the sub-tenant of a piece of land agreed between themselves that the sub-tenant would pay the tenant's rent direct to the landlord. The agreement was acted upon by all the parties interested.

Under these circumstances the landlord was allowed to obtain a decree for his rent direct against the sub-tenant. In other words, the sub-tenant was estopped from denying his liability to pay the tenant's rent on the ground that there was no such contract between him and the landlord.

In a tripartite building contract the builder contracting with his employer simultaneously agreed to be directly responsible to the owner of the building.

92. *Shappu Ammal v Subramaniyam*, ILR (1910) 33 Mad 238.

93. *Veeramma v Appayya*, AIR 1957 AP 965.

94. (1905) (Punj Rec) 171.

95. AIR 1952 Mys 109.

96. ILR (1934) 61 Cal 841; AIR 1934 Cal 682.

It was held that the employer had no right to sue the builder for any loss caused to the owner by any deficiency in works. Such liability was incurred directly to the owner.<sup>97</sup>

#### 4. Covenants running with land

The rule of privity may also be modified by the principles relating to transfer of immovable property. The principle of the famous case of *Tulk v Moxhay*<sup>98</sup> is that a person who purchases a land with notice that the owner of the land is bound by certain duties created by an agreement or covenant affecting the land, shall be bound by them although he was not a party to the agreement.

An illustration of the principle is *Smith & Snipes Hall Farm Ltd v River Douglas Catchment Board*:<sup>99</sup> The defendants (the Board) agreed with certain landowners adjoining a stream to improve the banks of the stream and to maintain them in good condition. The landlords on their part paid proportionate costs. Subsequently one of the landlords sold his land to the first plaintiff and he to the second plaintiff. There was negligence on the part of the Board in maintaining the banks, which burst and the land was flooded.

Both the plaintiffs were strangers to the agreement with the Board, but even so the Court of Appeal allowed them to sue the Board for breach of the contract, for the whole arrangement was for the benefit of the landowners whoever they might be and not merely the parties to the agreement.

Where the Central Government assigned a piece of land to its own corporate undertaking with all the rights, interests and privileges, it was held that privileges or rights to exemption from payment of land revenue which had accrued to the Central Government in respect of that land would also be available to the undertaking as a successor in interest to the Central Government.<sup>100</sup>

#### “... HAS DONE OR ABSTAINED FROM DOING ...”

These words mean that consideration is an act or abstinence which has already been done at the desire of the promisor, or is in progress or is promised to be done in future. An act which has already been done in response to the promise is referred to as an executed consideration.

#### Past consideration

It is an age-old principle of English law that consideration should be contemporaneous with the promise. Consideration, being the price for the

97. *McAlpine (Alfred) Construction Ltd v Panatown Ltd*, (2001) 1 AC 518: (2000) 3 WLR 946 (HL).

98. (1919) 88 LJKB 861 (HL).

99. (1949) 2 KB 500 (CA). See Andrew Tettenborn, *Covenants, Privity of Contract and the Purchase of Personal Property*, (1982) Camb LJ 59.

100. *SAIL v State of M.P.*, (1999) 4 SCC 76: AIR 1999 SC 1630.

promise, should be given in response to and as an inducement for the promise. If the act has been done before any promise is made, it is called past consideration and a past consideration is no consideration. If, for example: A has lost his purse and B, a finder, delivers it to him. A, in recognition of this service, promises to pay B, a sum of money. This promise is given for an act which was done before any promise existed, and, therefore, cannot be said to have been done as a price for the promise. The promise is to pay for a wholly past act and is, therefore, no more than an expression of gratitude. The past act may explain why the promise was given and may, thus, be a motive for the promise, but it furnishes no legal consideration.<sup>101</sup> “The consideration and the promise ought to go together.”<sup>102</sup> An example is *McArdle, re*:<sup>103</sup> A effected certain improvements to property. The ultimate beneficiaries of the property signed a document declaring that: “In consideration of your carrying out certain alterations and improvements, we the beneficiaries shall repay to you the sum of £488 in settlement of the amount spent on such improvements.” An action to enforce this promise was rejected.

JENKINS LJ said: “But the true position was that, as the work had in fact all been done and nothing remained to be done by the promisee at all, the consideration was wholly past consideration, and, therefore, the beneficiaries’ agreement for the repayment to her out of the estate was *nudum pactum*, a promise with no consideration to support it.”<sup>104</sup>

The rule involves inconvenience and hardship. If a person promises to pay for a past act, he means to recognise the past consideration and, therefore, should not be permitted to break his voluntary promise. The (English) Law Reform Committee has, therefore, recommended the abolition of the rule.<sup>105</sup>

#### *Past act at request good consideration*

However, an important exception is almost as old as the rule itself. It was established as early as 1616 in *Lamplleigh v Brathwait*<sup>106</sup> that a past act done at request will be good consideration for a subsequent promise. The facts were:

The defendant, having committed a murder, requested the plaintiff to labour and to do his endeavour to obtain pardon from the King. The plaintiff did his best to obtain the King’s pardon, riding and journeying at his own expense. Afterwards the defendant promised the plaintiff to give him £100 and then refused to pay. He was, however, held liable.

101. See *Roscor v Thomas*, (1842) 3 QB 234: 11 LJ QB 214, where a horse having been sold, a subsequent warranty for its soundness was held to be based upon past consideration.

102. Street, FOUNDATIONS OF LEGAL LIABILITY, 281.

103. 1951 Ch 669 (CA).

104. See also *Savage v Uwechia*, (1961) 1 WLR 455 (PC).

105. 6th Interim Report, para 32.

106. Hob 106: 80 ER 255.

The court observed: “A mere voluntary courtesy will not have consideration to uphold as assumpsit.<sup>107</sup> But if the courtesy were moved by a request of the party that gives the promise, it will bind, for the promise, though it follows, yet it is not naked, but it couples itself with the suit before.”

The modern version of this rule is that in such cases it is ordinarily in the contemplation of the parties that the service rendered at request would be ultimately paid for and that subsequent promise is nothing but a fixation of reasonable compensation for the service.

Besides this, two more exceptions have been admitted. A promise to pay a time-barred debt and a negotiable instrument issued for a past consideration are both valid.

### Position in India

It is not necessary for the courts in India to follow the English rule as to past consideration.<sup>108</sup> A past consideration may arise in two ways. It may consist of services rendered at request but without any promise at the time or it may consist of voluntary services.

#### 1. Past voluntary service

A past voluntary service is adequately covered by the provision in Section 25(2). A voluntary service means a service rendered without any request or promise and there is a subsequent promise to pay for the same. For example, to borrow an illustration from Anson:

“If A saves B from drowning and B later promises A a reward.”

Then in English law “A cannot rely on his action as consideration for B’s promise for it is past in point of time”.<sup>109</sup> But in India the promise would be enforceable by virtue of Section 25(2) which provides that “a promise to compensate, wholly or in part, a person who has already voluntarily done something for the promisor” is enforceable. The Act gives the following two illustrations to explain this:

“A finds B’s purse and gives it to him. B promises to give A Rs 50. This is a contract.”

“A supports B’s infant son. B promises to pay A’s expenses in so doing. This is a contract.”

#### 2. Past service at request

The only area of uncertainty should be about requested services, because this is not adequately covered either by Section 2(d) or by Section 25(b).

107. *Assumpsit* was the name of a form of action (now abolished) from which the law of contract originated.

108. *Devukutty Amma v Madhusudanan Nair*, (1995) 2 KLT 118, where it was observed that past consideration is good consideration under the Indian Contract Act and that it is a deviation from the English common law.

109. Anson’s PRINCIPLES OF THE ENGLISH LAW OF CONTRACT (23rd Edn, 1972) 86.

Section 2(d) requires that the act should be done at the promisor's desire. This presupposes the existence of a promise to pay for the act and even when construed literally the provision cannot apply to an act done at request but without any promise to pay. But the provision can be construed to include an act which has been done at request and for which a promise to pay is given subsequently. Even if no subsequent promise is given the courts can, following the principle laid down in *Upton-on-Severn RDC v Powell*,<sup>110</sup> infer an implied promise. Every request for an act carries an inbuilt promise to pay. In the words of BOWEN LJ in *Casey's Patents, re, Stewart v Casey*:<sup>111</sup>

The fact of a past service raises an implication that at the time it was rendered it was to be paid for, and if it was a service which was to be paid for, when you get in the subsequent document a promise to pay, that promise may be treated as an admission which evidences or as a positive bargain which fixes the amount of that reasonable remuneration on the faith of which the service was originally rendered.

In that case, J and T, the joint owners of a patent, wrote a letter to their manager saying: “We now have pleasure in stating that in consideration of your services as the practical manager in working both our patents, we hereby agree to give you one-third share of the patents”. The court held that “here for past services there is ample justification for the promise to give the third share”.

Pollock and Mulla have been heavily in favour of this interpretation of Section 2(d). The learned editor, Mr J.L. Kapur expressed his preference in these words:<sup>112</sup>

They (the words ‘has done or abstained from doing’) declare the law to be that an act done by A at B's request, without any contemporaneous promise from B, may be a consideration for a subsequent promise from B to A.... The use of the perfect tense in the clause embodies in the law of India the exception to the general rule which is supposed to have been made by the seventeenth century case of *Lampleigh v Brathwait*.<sup>113</sup>

The Bombay High Court in *Sindha Shri Ganpat Singhji v Abraham*<sup>114</sup> laid down that services rendered to a minor at his request and which were continued after majority at the same request, were good consideration for his promise to pay.

### Past and executed consideration

A *past* consideration should, however, be distinguished from *executed* consideration. Past consideration always consists of an act done without any promise. But executed consideration means an act which has been done in

110. (1942) 1 All ER 220 (CA). See “Proposal” or “Offer” in the first chapter.

111. (1892) 1 Ch 104 (CA).

112. (9th Edn, 1972) 41–42.

113. Hob 106; 80 ER 255.

114. ILR (1896) 20 Bom 755.

response to a positive promise. Where, for example, a reward is offered for finding a lost article, the offer can be accepted only by producing the article to the offeror and that is also a consideration for the promise. It is, thus, an example of a consideration which has already been executed. Explaining this in *Union of India v Chaman Lal Loona & Co*<sup>115</sup> S.K. DAS J of the Supreme Court said: “An executed consideration consists of an act for a promise. It is the act which forms the consideration. No contract is formed unless and until the act is performed, e.g., the payment for a railway ticket, but the act stipulated for exhausts the consideration, so that any subsequent promise, without further consideration, is merely a *nudum pactum*. In an executed consideration the liability is outstanding on one side only; it is a present as opposed to a future consideration.”

“In an executory consideration the liability is outstanding on both sides. It is in fact a promise for a promise; one promise is bought by the other. The contract is concluded as soon as promises are exchanged. In mercantile contracts this is by far the most common variety.”<sup>116</sup>

### Executory consideration

Thus consideration may consist of an act which has already been, or is in the process of being done. It may also consist of an act which is only promised to be done at some future time. There may be a simple exchange of promises and each promise is a consideration for the other. For example: A agrees to sell and B to buy a quantity of goods at a stated price. In other words, A has promised to sell and B has promised to pay. Until the goods are actually delivered to B under the contract, the consideration is executory. To put it in a few words, consideration may, under Section 2(d), consist of a past, present or a future act.<sup>117</sup>

### “SUCH ACT, ABSTINENCE OR PROMISE IS CALLED CONSIDERATION”

### Consideration must be of some value

Consideration, as defined in the Act, means some act, abstinence or promise on the part of the promisee or any other person which has been done at the desire of the promisor.<sup>118</sup> Does it, therefore, mean that even a worthless act will suffice to make a good consideration if it is only done at

115. AIR 1957 SC 652: 1957 SCR 1039.

116. *Union of India v Chaman Lal Loona & Co*, AIR 1957 SC 652: 1957 SCR 1039.

117. *Pankaj Bhargava v Mohinder Nath*, (1991) 1 SCC 556 where the court in reference to Ss. 5 and 51 said that mere reciprocal promises are sufficient to constitute a contract. *Union of India v Chaman Lal Loona & Co*, AIR 1957 SC 652, promise of one party to the other and by the other to the one, each promise is a consideration for each other. S. 2(e) provides that every promise and set of promises forming the consideration for each other, is an agreement. *Sultana Safiana Tahsin v Manoj Jajodia*, (2006) 4 CLT 122 (Gau), mutual promises recognised as consideration.

118. See *Manna Lal v Bank of Bengal*, ILR (1875–80) 1 All.309, 311.

the promisor's desire. For example: *A* promises to give his new Rolls-Royce car to *B*, provided *B* will fetch it from the garage.<sup>119</sup> The act of fetching the car cannot by any stretch of imagination be called a consideration for the promise. Yet it is the only act the promisor desired the promisee to do. Such an act no doubt satisfies the words of the definition, but it does not catch its spirit. It is for this reason that the English common law has always insisted that “consideration must be of some value in the eyes of the law.”<sup>120</sup> *White v Bluett*<sup>121</sup> may be cited as an illustration in point.

The defendant owed a sum of money under a promissory note to his father. The defendant perpetually, day and night, complained to his father that he had not been treated equally with other children in the distribution of his property. Thereupon the father promised to discharge him from all liability in respect of the loan and the note, provided he would stop complaining, which the defendant accordingly did. The question was whether the defendant's promise to cease his complaints was a sufficient consideration to sustain his father's promise.

POLLOCK CB said: “It would be ridiculous to suppose that such promises could be binding. In reality there was no consideration whatever.” In a later case a judge said that “a contract founded upon such an illusory consideration appears to be as invalid as a promise by a father made in consideration that his son would not bore him”.<sup>122</sup>

In India also it has been laid down by SUBBA RAO J (afterwards CJ) of the Supreme Court in a case<sup>123</sup> that consideration “shall be ‘something’ which not only the parties regard but the law can also regard as having some value”. Similarly, it has been observed by the Madras High Court:<sup>124</sup>

Though the Indian Contract Act does not in terms provide that consideration must be good or valuable to sustain a contract it has always been understood that consideration means something which is of some value in the eyes of law. It must be real and not illusory, whether adequate or not.... So long as the consideration is not unreal it is sufficient if it be of slight value only.

But the courts have been very liberal in this respect and have always tried to find value in something to which parties attach value. Thus, a transfer of property “in consideration that the transferee shall accept the responsibility

119. This problem is posed in Smith and Thomas, A CASEBOOK ON CONTRACT (2nd Edn, 1961) 144.

120. See Anson, PRINCIPLE OF THE ENGLISH LAW OF CONTRACT (22nd Edn by A.G. Guest, 1964) 91.

121. (1853) 23 LJ Ex 36.

122. HOOD J in *Dunton v Dunton*, (1892) 18 VLR 114 (SC of Victoria).

123. *Chidambara Iyer v P.S. Renga Iyer*, AIR 1966 SC 193, 197: (1966) 1 SCR 168.

124. *Kulasekharaperumal v Pathakutty Thalavanar*, AIR 1961 Mad 405: (1916) 74 LW 16 (Mad).

See also *Sonia Bhatia v State of U.P.*, (1981) 2 SCC 585, where the court explained the meaning of adequate consideration and held that it does not include love, affection or spiritual benefit as involved in a gift.

and discharge those recurrent religious services and ceremonies”,<sup>125</sup> and a promise by a wife to pay off her husband’s debts and to maintain his mother made in consideration of enjoying certain properties, were held to be for valuable consideration.<sup>126</sup>

### Value need not be adequate (adequacy of consideration)

It is not, however, necessary that consideration should be adequate to the promise. The courts can hardly assume the job of settling what should be the appropriate consideration for a promise. It is entirely for the parties. If a party gets what he has contracted for and if it is of some value, which may be great or small, the courts “will not enquire whether it was equivalent to the promise which he gave in return”.<sup>127</sup> “The adequacy of the consideration is for the parties to consider at the time of making the agreement, not for the court when it is sought to be enforced”.<sup>128</sup> This is the English rule and is applicable in India also, for Explanation 2 attached to Section 25 lays it down so clearly that “an agreement to which the consent of the promisor is freely given is not void merely because the consideration is inadequate”. This is further fortified by illustration (f) which is as follows: A agrees to sell a horse worth Rs 1000 for Rs 10. A’s consent to the agreement was freely given. The agreement is a contract notwithstanding the inadequacy of the consideration.

The best known English authority is *De La Bere v Pearson Ltd.*<sup>129</sup>

The defendants, who were newspaper proprietors, offered to answer inquiries from readers of the paper desiring financial advice. The plaintiff wrote to them asking for a safe investment and also for the name of a good stock broker. The editor recommended a person who, unknown to him, was, in fact, an undischarged bankrupt. The plaintiff, in reliance on the recommendation, sent sums for investment and they were immediately misappropriated. In an action against the defendants, the question was whether there was sufficient consideration for the offer of the advice.

Holding that there was, VAUGHAN WILLIAM J said: “Such publication might obviously have a tendency to increase the sale of the defendant’s

125. *Ramacharya v Shiv Nivascharya*, (1918) 20 Bom LR 441: 46 IC 19.

126. *Kulasekharaperumal v Pathakutty Thalavanar*, AIR 1961 Mad 405.

127. Anson, PRINCIPLES OF THE LAW OF CONTRACT (22nd Edn, by Guest, 1964) 91. *Desigowda v Karnataka Industrial Area Development Board*, AIR 1996 Kant 197, land acquisition, landholders agreed to receive compensation under S. 29(2) of the Karnataka Industrial Area Development Act, 1966, such agreement could not by itself be regarded as unconscionable or unreasonable, the court could not also examine inadequacy of agreed amount of compensation. *Vijaya Minerals (P) Ltd v Bikash Chandra Deb*, AIR 1996 Cal 67, parties bargaining power equal for settling their terms, it is unbelievable that there would be inadequacy of consideration in such a situation and even if it is there the contract cannot be rendered nugatory on that ground.

128. BLACKBURN J in *Bolton v Madden*, 1873 LR 9 QB 55, 57.

129. (1908) 1 KB 280 (CA). See also *A. Lakshmanaswami Mudaliar v LIC*, 1963 Supp (2) SCR 887: AIR 1963 SC 1185, where the Supreme Court discusses the concept of inadequacy.

paper. I think that this offer, when accepted, resulted in a contract for good consideration.”

The principle has been followed in this country also. The transfer of the goodwill and the whole of the assets of a business for a bare Rs 1000 has been upheld.<sup>130</sup>

### Inadequacy as evidence of imposition

However, the Act provides in Explanation 2 to Section 25 that “inadequacy of consideration may be taken into account by the court in determining the question whether the consent of promisor was freely given”. Illustration (g) explains this: A agrees to sell a horse worth Rs 1000 for Rs 10. A denies that his consent to the agreement was freely given. The inadequacy of the consideration is a fact which the court should take into account in considering whether or not A’s consent was freely given.

“A party seeking to set aside a transaction on the ground of inadequacy of consideration, must show such inadequacy as will involve the conclusion that he either did not understand what he was about, or was the victim of some imposition.”<sup>131</sup> For “once a court is satisfied that a person has entered into an agreement freely and with knowledge of its purport and effect”, the agreement will be valid notwithstanding the inadequacy of consideration. Even where a transaction is avoided under this principle, it is not because of the inadequacy of consideration, but because of fraud or some other vitiating element. For “inadequacy of consideration may in circumstances suggest fraud, coercion, mistake and such like”.<sup>132</sup> The same result would follow where the consideration is so markedly inadequate as to be unconscionable and there is a serious inequality of bargaining power between the parties. A lady was injured as a result of the defendant’s negligent driving. Soon thereafter she confronted an insurance adjuster and signed up a release agreement of all her claims for just \$ 331. Subsequently she sued the defendant in tort and her damages were assessed at \$ 21,000. She was held to be not bound by the agreement. She was still suffering from her injuries; she received no independent advice and was, therefore, in a much weaker position as compared with a professional claim adjuster.<sup>133</sup>

### Forbearance to sue

Forbearance to sue has always been regarded as valuable consideration. It is, indeed, a kind of abstinence, which is so very clearly recognised as

130. *Devji Shivji v Karsandas Ramji*, AIR 1954 Pat 280.

131. Per Lord WESTBURY in *Tennent v Tennents*, LR 2 Scot 6, cited in *Administrator General of Bengal v Juggeswar Roy*, ILR (1877) 3 Cal 192, 196 (PC): 1 CLR 107.

132. See HARRISS CJ in *Rai Bahadur H.P. Banerji v CIT*, ILR (1940) 20 Pat 202, 214: AIR 1941 Pat 59. See also *Banda Ali v Banspat Singh*, ILR (1882) 4 All 352: 1882 AWN 66 where the Allahabad High Court set aside a bond executed for inadequate consideration as the circumstances revealed duress; *Bhimbha v Yeshwantrao*, ILR (1900) 25 Bom 126.

133. *Pridmore v Calvert*, (1975) 54 DLR (3d) 133 (BCSC).

good consideration in the definition itself. “Forbearance to sue” means that the plaintiff has a certain right of action against the defendant or any other person and on a promise by the defendant he refrains from bringing the action. The Patna High Court observed in a case that:<sup>134</sup> Where a wife who is ready to sue her husband for maintenance allowance has forborence to sue on husband's agreeing to pay her monthly allowance by way of maintenance, the contract is supported by consideration as wife's forbearance to sue amounts to consideration for husband's agreement for payment of maintenance allowance.

Another easy illustration is in a decision of the Kerala High Court:<sup>135</sup>

Three depositors of a bank refrained from demanding payment of their deposits, although they had matured and become payable, as the director of the bank had given them a written agreement undertaking personal liability to return the amount with interest at 6 per cent within 12 months.

This forbearance to withdraw the amount or press for its repayment was held to be sufficient consideration for the agreement within the meaning of Section 2(d).<sup>136</sup>

An act or forbearance on the part of the creditor, though it may not be for a definite period, is a good consideration. The compromise of doubtful rights has also been regarded as sufficient consideration for an agreement.<sup>137</sup> But there must be a *bona fide* claim and not merely one which is set up frivolously or vexatiously. “If there is in fact a serious claim honestly made, the abandonment of the claim is good consideration for a contract.”<sup>138</sup> “If a person believes that he has a *bona fide* claim to enforce, his forbearance from trying to put that claim in a court and to have it decided will be a good consideration for a contract, however the claim, if brought, may be decided.”<sup>139</sup> A claim set up on the basis of a false or forged “will” cannot sustain an agreement. Rejecting a claim of this kind in *Krishna Chandra Dutta Roy v Hemaja Sankar Nandi*<sup>140</sup> the Calcutta High Court cited the following statement of Lord BLACKBURN: Of course, forbearance of a non-existing claim would not be forbearance at all.<sup>141</sup>

Again there can be no real forbearance unless the claim is immediately due. In *Manna Lal v Bank of Bengal*:<sup>142</sup>

134. *Debi Radha Rani v Ram Dass*, AIR 1941 Pat 282. Also see *Kastoori Devi v Chiranjit Lal*, AIR 1960 All 446, where the withdrawal of a pending suit by a wife against her husband was held to be a good consideration for his promise to pay her maintenance.

135. *M. Ramiah Pillai v P. A. Sankaranarayana Iyer*, AIR 1958 Ker 246: 1958 KLJ 253.

136. See also *Dadabhoy Dajibhoy v Pestonji*, ILR (1893) 17 Bom 457, where forbearance of the right to rescind a contract was held to be good consideration for an agreement.

137. *Rameshwar Prasad Singh v Lachmi Prasad Singh*, ILR (1904) 31 Cal 111.

138. COTTON LJ in *Miles v New Zealand Alford Estate Co*, (1886) 32 Ch D 266 (CA) cited in *Krishna Chandra Dutta Roy v Hemaja Sankar Nandi*, (1917-18) 22 CWN 463.

139. *Gulab Chand v Kamal Singh*, AIR 1922 All 260.

140. (1917-18) 22 CWN 463.

141. *Cook v Wright*, (1861) 1 B&S 559.

142. ILR (1875-80) 1 All 309.

A *hundi* debt had not yet matured when the acceptor of the *hundies* pledged his own house and shops as security for due payment in the event of their dishonour on maturity.

The court quite obviously came to the conclusion that there was no consideration for the pledge.

### Compromise good irrespective of merits

Compromise of a pending suit is a good consideration for the agreement of compromise. But here also it is essential that the dispute should be *bona fide*, although the Patna High Court has held in a case that a compromise is binding even if the “suit was based on a false claim”.<sup>143</sup> However, a compromise is a good consideration “irrespective of merits of the claim of either side”, and even “where there is some doubt in the minds of the parties as to their respective rights”.<sup>144</sup>

An agreement to accept a new mortgage in substitution and in consideration of not enforcing the earlier mortgage, although the original was executed only by one person and the substitute by four persons<sup>145</sup> and an agreement to release a debtor and to accept a new debtor in his place have been sustained.<sup>146</sup> “An agreement to avoid further litigation is not an agreement void of consideration.”<sup>147</sup> Similarly, it has been held that “where an agreement has been arrived at between certain members of a family that is designed to promote grace and goodwill, this by itself is a good consideration to support the transaction.”<sup>148</sup> In a case before the Supreme Court<sup>149</sup> two brothers were quarrelling over the division of their late father’s property. Their mother persuaded the junior to give up the struggle on the promise that if the elder one did not provide him a sum of money she would subsidise him. The promise was held to be enforceable. It was given to purchase family peace and that was sufficient consideration.

## PERFORMANCE OF EXISTING DUTIES

### Performance of legal obligations

Consideration, it is generally said, must be something more than what the promisee is already bound to do. A person may be bound to do something

143. *Rameshar Mistri v Babulal Pandit*, AIR 1946 Pat 97; *M.M. Hussain v Laminated Package P Ltd*, (1999) 6 Andh LT 529, the surrender of a disputed title was recognised as good consideration. It is not necessary that consideration should always be in the shape of money.

144. *United Province Govt v Church Missionary Trust Assn Ltd*, ILR (1948) 22 Luck 93: AIR 1948 Oudh 54; *Kailash Narain v Mahila Manbhota*, AIR 1996 MP 194, compromise, allegation that it was induced by fraud not substantiated, the court entitled to pass decree in terms of compromise.

145. *Fanindra Narain Roy v Kachhemen Bibi*, AIR 1918 Cal 816: ILR (1917) 45 Cal 774.

146. *Mobesh Chandra Guha v Rajani Kanta Dutt*, (1915) 31 IC 29.

147. *Bhima v Nigappa*, (1868) 5 BHC 75 (Appeal Civil). See also *Chidambara Iyer v P.S. Renga Iyer*, AIR 1966 SC 193: (1966) 1 SCR 168, where a charitable institution gave up its rights for a transfer of a property to it, held, good consideration.

148. *Latif Jahan Begam v Mohd Nabi Khan*, AIR 1932 All 174.

149. *CWT v Her Highness Vijayaba*, (1979) 2 SCC 213: AIR 1979 SC 982.

by law or by contract. "Performance of a legal duty is no consideration for a promise." This principle of English law was adopted by the Madras High Court in *P. Sashannah Chetti v P. Ramasamy Chetti*<sup>150</sup> even before the Contract Act came into force, although the Act contains no provision on the point.

The facts of the case were that the plaintiff had been served with summons requiring him to give evidence before a court of law. The defendant, who was a party to the case, gave him a promissory note promising to pay a sum of money for his trouble. The note was held to be void for want of consideration.

The court observed: "It is quite clear that if a *sub poena* (summon) had been served, and the note had been given to compensate the plaintiff for his loss of time or other inconvenience, it would have been without consideration, because his attendance and the giving of evidence would have been merely the performance of a duty imposed upon him by law." *Collins v Godefroy*<sup>151</sup> is an English authority to the same effect. Similarly, a promise to pay a sum of money to a police officer for investigating a crime will be without consideration if he is already bound to do so by law. "But doing or agreeing to do more than one's official duty will serve as consideration." As was observed by Lord DENMAN CJ in *England v Davidson*:<sup>152</sup> "I think there may be services which the constable is not bound to render and which he may, therefore, make the ground of a contract." Following this principle the Court allowed in that case a police officer, who had given information leading to the conviction of a criminal, to recover the reward offered by the defendant for such information. But in all such cases the court must make sure that the service rendered is really beyond the scope of official duty and not a mere pretence for extracting money. An American Judge remarked in a case that:

If a constable for making extraordinary efforts to perform an ordinary official act, may not only receive, but may also collect by law a compensation beyond what the statute allows for the act, any other officer may do the same; and sheriffs, legislators and judges might, and soon would, put their extraordinary efforts in the market, to be had by the higher bidder. This is a sickening and revolting view of the subject:<sup>153</sup>

In an American case:

A fireman was allowed to receive a reward offered by a husband to anyone who would rescue his wife from a burning building, dead or alive, because at great peril to his life and health he accomplished the rescue of

150. (1868) 4 MHC 7.

151. (1831) 109 ER 1040: 9 LJ KB 158.

152. (1840) 9 LJ (QB) 287.

153. *Hogan v Stophelt*, (1899) 170 Ill 150.

her dead body and because the court found that as a fireman of the city he was not legally bound to risk his life in that rescue.<sup>154</sup>

The English case of *Glasbrook Bros Ltd v Glamorgan County Council*<sup>155</sup> is another illustration of services rendered outside the scope of official obligations:

On the occasion of a strike, a colliery manager applied for police protection for his colliery and insisted that it could only be efficiently protected by billeting a police force on the colliery premises. The police superintendent was prepared to provide what in his opinion was adequate protection by means of a mobile force, but refused to billet police officers at the colliery except on the terms of the manager agreeing to pay for the force so provided at a specified rate. It was held by a majority that there was nothing illegal in the agreement, nor was it void for want of consideration.

The court laid down that “although the police authority is bound to provide sufficient protection to life and property without payment, if in particular circumstances, at the request of an individual, they provide a special form of protection outside the scope of their public duty, they may demand payment for it”.

On the same principle, the mother of an illegitimate child, having been separated from the child's father, was allowed to enforce the father's promise to pay £1 per week for looking after the child, although she was herself under a statutory obligation to maintain the child.<sup>156</sup> Similarly, a married woman who had deserted her husband was allowed to enforce her husband's promise to pay her a weekly sum if she would maintain herself and lead a chaste life.<sup>157</sup> In the last-mentioned case DENNING LJ said: “A promise to perform an existing duty is, I think, sufficient consideration to support a promise, so long as there is nothing in the transaction which is contrary to the public interest.”

## Performance of contractual obligations

### A. Pre-existing contract with promisor

Secondly, compliance with legal obligation imposed by a contract with the promisor can be no consideration for a promise. An illustration is supplied by the facts of *Ramchandra Chintaman v Kalu Raju*.<sup>158</sup>

The plaintiff accepted a *Vakalatnama* from the defendant to act for him in a certain suit on receiving his usual fee. Subsequently the defendant agreed to pay him a certain sum as a special reward (inam), if the suit

154. Costigan, CASES ON CONTRACT (3rd Edn) 309.

155. 1925 AC 270 (HL).

156. *Ward v Byham*, (1956) 1 WLR 496 (CA).

157. *Williams v Williams*, (1957) 1 WLR 148 (CA).

158. ILR (1877) 2 Bom 362.

was decided in his favour. The suit was decided in favour of the defendant, who, however, did not pay the amount. The plaintiff, therefore, brought the present suit against him.

Rejecting the action, WESTROPPE CJ said: "The plaintiff, having accepted a *Vakalatnama* was already bound to render his best service as a pleader. There was no fresh consideration proceeding from the plaintiff when he obtained the agreement."

The better known illustration is the old English case of *Stilk v Meyrick*:<sup>159</sup>

In this case while a ship was on a voyage, two of the seamen deserted; and the captain, having in vain attempted to supply their places, entered into an agreement with the rest of the crew that if they work the ship home, they should have the wages of the two who had deserted equally divided among them.

Lord ELLENBOROUGH CJ held that the agreement was void for want of consideration in as much as it was the contractual duty of the mariners who remained with the ship to exert themselves utmost in any emergency of the voyage to bring the ship in safety to her destined port and the desertion of a part of the crew was definitely an emergency of the voyage.

But where, in another case, sailors refused to complete a voyage because of war risks, not originally contemplated, but remained on duty on the promise of extra pay, they were allowed to recover it.<sup>160</sup> The principle would seem to be that "where conditions have arisen under which a party is entitled to refuse to go ahead with his contract, a promise to pay him extra if he will not do so is valid".<sup>161</sup> Where the main contractor found that his sub-contractor was slow in progress and it was partly due to the low rates allowed to him. Partly for this reason and partly for the reason that the main contractor would fall under heavy penalties if the work was not completed in time, he promised more money to the sub-contractor for doing the same work which he had already undertaken and no additional work. He was held bound to pay the sub-contractor according to the increased rates.<sup>162</sup> It has been observed that the case provided an authority for the proposition that a promise to perform an existing obligation can amount to good consideration provided there are practical benefits to the promisee. This statement was not accepted to be a working principle in a subsequent case in which the payment of tax arrears was rescheduled to the acceptance of the Tax Collector, but the agreement was held to be not binding. An aggravating factor was that the taxpayer was not able to keep up the payment of

159. (1809) 2 Camp 317: 170 ER 1168.

160. *Liston v Owners Carpathian*, (1915) 2 KB 42. See also *Hartley v Ponsonby*, (1857) 119 ER 1471: 26 LJ QB 322: 29 LT 195, where the number of deserters was so great that only a few hands were left and, therefore, the captain's promise to pay them extra was held enforceable.

161. A.L. Goodhart, *Blackmail and Consideration in Contracts*, (1928) 44 LQR 436 and Samuel Williston, *Successive Promises of the same Performance*, (1894–95) 8 Har LR 27.

162. *Williams v Roffey Bros & Nicholls (Contractors) Ltd*, (1991) 1 QB 1: (1990) 2 WLR 1153 (CA).

instalments.<sup>163</sup> The court said: “When a creditor and a debtor who are at arm’s length reach agreement on the payment of the debt by instalments to accommodate the debtor, the creditor will no doubt always see a practical benefit to himself in so doing.”

The court continued to say that if there were no authority, like the decision in *John Weston Foakes v Julia Beer*,<sup>164</sup> there would have been much to be said for the enforceability of such a contract. The same result was reached in another case involving part payment, namely *C Re (A debtor)*.<sup>165</sup> A person was under a statutory demand of the Legal Aid Board for about £16,500. He mailed a cheque for the lesser amount of £14,000 with a request for the Board to return the cheque if it was not acceptable in full settlement. The Board accepted the cheque but only “on account”. Thus, it was not possible for the debtor to prove a promise by the Board to accept the lesser sum. These cases were distinguished from the decision in *Williams v Roffey Bros & Nicholls (Contractors) Ltd*.<sup>166</sup> Here money was promised to a contractor in excess of the amount for which he undertook to complete the project. The promise was intended to ensure the completion of the work in time. There was no evidence of any undue influence or exploitation by the contractor. The court overcame the effect of authorities by resorting to the doctrine of promissory estoppel. The best and simplest description of the doctrine and how it works is to be found in the following words of Lord DENNING:<sup>167</sup>

“When a man, by his words or conduct, has led another to believe that he may safely act on the faith of them—and the other does act on them—he will not be allowed to go back on what he has said or done when it would be unjust and inequitable to do so.”

In a Canadian case,<sup>168</sup> a contractor was carrying out construction work for the completion of which the plaintiff was to supply steel at a fixed price. The plaintiff then found that steel prices were rising and, therefore, asked the contractor for an upward revision of the price for future supplies. The contractor orally accepted the revision and also accepted deliveries against invoices reflecting the increased price. The contractor, however, did not pay and the supplier sued for the difference. It was held that the price revision being without consideration, the contractor was not bound. The fact that he continued to accept supplies without repudiating the invoices did not create any promissory estoppel against him.<sup>169</sup>

163. *Selectmov Ltd, re*, (1995) 1 WLR 474 (CA).

164. (1884) LR 9 AC 605.

165. May 11, 1994 (unreported). Noted in Norma J. Hird and Ann Blair, *Minding Your Own Business—Williams v Roffey Revisited: Consideration Re-considered*, 1996 JBL 254.

166. (1991) 1 QB 1: (1990) 2 WLR 1153 (CA).

167. THE DISCIPLINE OF LAW, 223. See for further study Adams and Brownsword, *Contract, Consideration and Critical Path*, (1995) Mod LR 536.

168. *Gilbert Steel Ltd v University Construction Ltd*, (1976) 12 OR (2d) 19 (CA).

169. See also *Syros Shipping Co SA v Elaghill Trading Co*, (1981) 3 All ER 189 where a consignee's promise to pay extra money to the carrier was not allowed to be enforced.

### *Promise to pay less than amount due*

On the same principle, a promise to pay less than what is due under a contract cannot be regarded as a consideration. This rule, having been laid down in an early case, was thus formulated in *Pinnel's case*.<sup>170</sup>

"Payment of a lesser sum on the day in satisfaction of a greater cannot be any satisfaction for the whole, because it appears to the judges that by no possibility can a lesser sum be a satisfaction to the plaintiff for a greater sum. But the gift of a horse, hawk or robe, etc., in satisfaction is good. For it shall be intended that a horse, hawk or robe, etc., might be more beneficial to the plaintiff than the money in respect of some circumstances; or otherwise, the plaintiff would not have accepted of it in satisfaction."

The rule was criticised by JESSEL MR in a case<sup>171</sup> where his Lordship said: "According to English Common Law a creditor might accept anything in satisfaction of his debt except a less amount of money. He might take a horse, or a canary, or a tomtit he chose, and that was accord and satisfaction but, by a most extraordinary peculiarity of the English Common Law, he cannot take 19s. 6d. in the pound."

Similarly, Earl of SELBORNE LC said in *Weston Foakes v Julia Beer*:<sup>172</sup> "It might be (and indeed I think it would be) an improvement in our law, if a release or acquittance of the whole debt, on payment of any sum which the creditor might be content to receive by way of accord and satisfaction (though less than the whole) where held to be, generally, binding,...."

Despite this criticism the rule was unanimously affirmed by the House of Lords in the above-cited case:

Dr Foakes was ordered by a judgment decree to pay £2000 to Mrs Beer. The doctor, not being able to pay up at once, made an agreement with her under which he paid £200 immediately and agreed to pay the balance by instalments and she in her turn agreed not to enforce the judgment. When the balance was fully paid, she sued the doctor to recover interest on the judgment-debt.

The House of Lords held that she was entitled to the payment of the judgment-debt and to interest to the date of final payment as she accepted less in satisfaction of the whole and there was no consideration for her promise to accept anything less than the sum to which she was entitled.

### **Exceptions to the rule in "Pinnel case"**

The Law Revision Committee in its report in 1937 recommended abolition of the rule.<sup>173</sup> The courts have tried to avoid the awkward results of the rule by admitting exceptions to it.

170. (1602) 5 Co Rep 117a.

171. *Couldery v Bartrum*, (1881) LR 19 Ch D 394, 399 (CA).

172. (1884) LR 9 AC 605.

173. 6th Interim Report, paras 35, 40.

### 1. *Part-payment by third party*

In the first place, part-payment by a third party may be a good consideration for the discharge of the whole of the debt.

The father of a debtor wrote to the creditor, offering an amount less than that of the debt in full settlement of the debt, and enclosing a draft for that amount, and the creditor cashed and retained the proceeds of the draft, and afterwards brought an action against the debtor for the balance of the debt. It was held that the creditor must be taken to have accepted the amount received by him on the terms upon which it was offered, and therefore, he could not maintain the action.<sup>174</sup>

A debtor's wife has not been regarded as a third person for this purpose.

The plaintiff had a claim of £ 480 against the defendant. To the knowledge of the defendant he was in desperate financial straits. Exploiting this knowledge they offered him only £ 300 in full satisfaction, which he accepted. The payment was made by the defendant's wife.

The plaintiff was allowed to recover the remaining £ 180 on two grounds, first, there was no consideration for the settlement and, second, there was no true accord because no person can insist upon a settlement procured by intimidation.<sup>175</sup>

### 2. *Composition*

Secondly, payment of a lesser sum is a good satisfaction for a larger sum where this is done in pursuance of an agreement of compromise entered into by the debtor with his creditors.

### 3. *Payment before time*

Thirdly, payment of a lesser sum before time, or in a different mode or at a different place than appointed in the original contract or "the gift of a horse, hawk or robe, etc., in satisfaction is good".<sup>176</sup>

### 4. *Promissory estoppel*

The following statement of BOWEN LJ is an instructive expression of the principle of promissory estoppel.<sup>177</sup>

If persons who have contractual rights against others induce by their conduct those against whom they have such rights to believe that such rights will either not be enforced or will be kept in suspense or abeyance

174. *Hirachand Punamchand v Temple*, (1911) 2 KB 330, 331 (CA).

175. *D.&C. Builders v Rees*, (1966) 2 QB 617 (CA).

176. See *Pinnel's case*. Also see JESSEL MR in *Couldery v Bartrum*, (1881) LR 19 Ch D 394, 399 (CA).

177. *Birmingham & District Land Co v London and North Western Rly Co*, (1888) 40 Ch D 268 (CA).

for some particular time, those persons will not be allowed by a Court of Enquiry to enforce the rights until such time has elapsed....

This principle is well-known in the United States<sup>178</sup> and seems to have been first applied in England in *Thomas Hughes v Metropolitan Railway Co.*<sup>179</sup>

A landlord had given notice to his tenant to repair the premises within six months, failing which the lease was to be forfeited. A month after this the landlord entered into negotiations for the sale of the land to the tenant and, consequently, during the period covered by the negotiations, the tenant carried out no repairs. The negotiations failed to materialise and shortly thereafter the period of six months expired and the landlord claimed the lease to have been forfeited.

But it was held that six months would run from the failure of the negotiations. The conduct of entering into negotiations was an implied promise on the part of the landlord to suspend the notice and the tenant had acted on it by not carrying out the repairs.

Another landmark in the development of this principle is the much debated case of *Central London Property Trust Ltd v High Trees House Ltd*<sup>180</sup> where DENNING J asserted "that a promise intended to be binding, intended to be acted on and in fact acted on, is binding so far as its terms properly apply".<sup>181</sup>

The plaintiffs gave to the defendants a tenancy of a block of flats at a ground rent of £2500 a year for a period of 10 years. As a result of the 2nd World War, the flats could not be fully let and, therefore, the plaintiffs agreed to reduce the rent by half the amount. In 1945, war conditions ceased to exist, and the flats became fully occupied, but the defendants continued to pay only the reduced rent. The plaintiffs' action to recover the full rent as reserved in the original lease from the middle of 1945 was successful, but not for the arrears.

One of the questions was what was the consideration for the agreement to reduce the rent. Apparently there was none. But in the opinion of DENNING

178. See for example, G.H.L. Fridman, *Promissory Estoppel*, (1957) 35 CBR 279.

179. (1877) LR 2 AC 439.

180. (1947) 1 KB 130.

181. *Ibid* at p. 136. This statement of His Lordship has been the subject of what seems to be an unending debate. See, for example, J.F. Wilson, *Recent Developments in Estoppel*, (1951) 67 LQR 330. Cheshire & Fifoot, *Central London Property Trust Ltd v High Trees House Ltd*, (1947) 1 KB 130; L.A. Sheridan, *Equitable Estoppel Today*, (1952) 15 Mod LR 325, 328; A.G. Guest, *The New Estoppel, An English Development*, (1956) 30 Australian LJ 187; Fridman, *Promissory Estoppel*, (1957) 35 Can B Rev 279. For further insight see John P. Dawson, *GIFTS AND PROMISES* and P.S. Atiyah, *PROMISES: MORALS AND LAW*. The doctrine of promissory estoppel has no place in formally concluded contracts. See *C.V. Enterprises v Braithwaite & Co Ltd*, AIR 1984 Cal 306. Where certain employees were induced to change their Department by holding out promises of better service conditions, the Supreme Court did not permit the Government to resile from its promise. *Bhim Singh v State of Haryana*, (1981) 2 SCC 673: AIR 1980 SC 768.

J there was no necessity of finding consideration in a case like this where the promise is not set up as cause of action, but only as a defence. The plaintiffs having deliberately agreed to forego the rent and the defendants having acted on that promise up to the time of action, the plaintiffs were estopped from alleging that here was no consideration for the promise.

Referring to the above principle in his judgment in *Combe v Combe*,<sup>182</sup> DENNING LJ said: "That principle does not create new cause of action where none existed before. It only prevents a party from insisting upon his strict legal rights, when it would be unjust to allow him to enforce them, having regard to the dealings which have taken place between the parties."

In this case a wife obtained a decree *nisi* against her husband for divorce. She received a letter from the husband in confirmation of her own, as exchanged through solicitors, that he would make her £100 allowance a year. The husband did not make the payments and ultimately the wife brought an action to enforce the promise.

The Court of Appeal held that neither there was any consideration for promise nor was there any promissory estoppel against the husband. The husband never made a request that she should not enforce her normal right to maintenance, nor was there any undertaking on her part not to do so. Her abstinence was not the result of any promise of the husband.

Though promissory estoppel may not sustain a new cause of action, it is not necessarily confined to cases where the parties are bound by a subsisting contract and one of them promises not to enforce his normal contractual rights. The decision of the Court of Appeal in *Evenden v Guildford City Assn Football Club Ltd*<sup>183</sup> marks a further extension of the boundaries of promissory estoppel. Lord DENNING MR stated that the doctrine of estoppel applies whenever a representation is made, whether of fact or law, present or future, which is intended to be binding, intended to induce a person to act on it and he does act on it. The facts were that the plaintiff had been working since 1955 as a groundsman in a supporters' club of a football club. In 1968 the football club itself acquired his services on the same terms and for the same work. In 1974 he was made redundant. He claimed redundancy benefit right from 1955 whereas the club proposed to pay him only from 1968. The principle of promissory estoppel was applied because there was a representation that his employment would be treated as continuous:

That representation was intended to be binding and intended to be acted on. He did act on it. He did not claim from the supporters' club the redundancy payment to which he would otherwise have been entitled from that club. Six months later his claim against the supporters' club was barred by lapse of time. It would be most unfair for the football club to

182. (1951) 2 KB 215 (CA). But see, M.P. Thompson, *From Representation to Expectation, Estoppel as a Cause of Action*, 1983 Camb LJ 257.

183. 1975 QB 917 (CA).

go back now on that representation. The employment must be treated as continuous for 19 years.

The House of Lords considered this line of cases in their decision in *Tool Metal Mfg Co Ltd v Tungsten Electric Co Ltd*,<sup>184</sup> and applied the principle of promissory estoppel to the facts of the case. Their Lordships held that where a party has suspended his normal rights under a contract, he can at any time by giving reasonable notice to the other resume them; and a counter-claim based on those rights which was raised in an earlier case was a sufficient notice of the intention to resume the original rights. The Tool Metal Company was entitled to a fixed rate of compensation depending upon the quantity of material consumed by the Electric Co. A new agreement being under preparation, the T.M. Co told the other company that they would not claim compensation in the meantime. The new agreement was not accepted by the Electric Co and, therefore, T.M. Co sought to restore its right to compensation and was allowed to do so for the future. The final shape of the principle of promissory estoppel as it has resulted from the line of cases has been stated by Lord HODSON while delivering the opinion of the Judicial Committee of the Privy Council in *Emmanuel Ayodeji Ajaji v R.T. Briscoe (Nigeria) Ltd*.<sup>185</sup>

The principle is that when one party to a contract in the absence of fresh consideration agrees not to enforce his rights an equity will be raised in favour of the other party. This equity is, however, subject to the qualifications: (1) that the other party has altered his position, (2) that the promisor can resile from his promise on giving reasonable notice, which need not be a formal notice, giving the promisee reasonable opportunity of resuming his position, (3) the promise only becomes final and irrevocable if the promisee cannot resume his position.

A promise to pay more than the sum due under an existing contract may be equally void. A recent illustration is provided by a Canadian case in which there was an agreement to supply steel at a stated price for completing a construction contract. On account of rising steel prices it was orally agreed between parties that increased price would be charged. Subsequent deliveries were made and accepted on increased prices, but not paid for. The contractor was held to be not bound to pay the extra price, the revision agreement being without any consideration.<sup>186</sup>

Where the party carrying out works to a vessel was told that he would be paid an additional amount by way of bonus, if he completed the works within a certain date, and a certificate was issued by an employee of the ship-owning company that the works had been satisfactorily completed within the given time, the shipowner was not allowed to resile from the promise

184. (1955) 1 WLR 761.

185. (1964) 1 WLR 1326 (PC).

186. *Gilbert Steel Ltd v University Construction Ltd*, (1976) 12 OR (2d) 19 (CA).

by saying subsequently that the work was not satisfactory. No objection was raised about the certificate for a considerable period of time and the shipowner had also benefited from the timely completion. It would not have been fair or just to allow the shipowner to deny the promised benefit to the other party.<sup>187</sup>

### *Position under Indian Contract Act different*

Luckily in India controversies of this kind are not likely to arise, for the Contract Act in Section 63 clearly provides that “every promisee may dispense with or remit, wholly or in part, the performance of the promise made to him, or may extend the time for such performance, or may accept instead of it any satisfaction which he thinks fit”. The section has the following illustrations:

- (b) *A owes B 5000 rupees. A pays to B and B accepts, in satisfaction of the whole debt, 2000 rupees paid at the time and place at which the 5000 rupees were payable. The whole debt is discharged.*
- (c) *A owes B 5000 rupees. C pays to B 1000 rupees, and B accepts them, in satisfaction of his claim on A. This payment is discharge of the whole claim.*
- (d) *A owes B under a contract, a sum of money, the amount of which has not been ascertained. A, without ascertaining the amount gives to B and B, in satisfaction thereof, accepts the sum of 2000 rupees. This is discharge of the whole debt whatever may be its amount.*
- (e) *A owes B 2000 rupees, and is also indebted to other creditors. A makes an arrangement with his creditors, including B to pay them a composition of eight annas in the rupee upon their respective demands. Payment to B of 1000 rupees is a discharge of B's demand.*

There was a development-agreement between an Improvement Trust and a land owner. A clause in the agreement provided that the owner is to transfer the plot earmarked for a primary school to the Trust free of cost. It was held to be not void for being without consideration or being opposed to public policy. The land owner had under the agreement derived huge benefit by getting his land freed from acquisition and also getting permission to develop the land and put it to commercial use.<sup>188</sup>

### *B. Pre-existing contract with third party*

Where a person has contracted to do an act, and a third person promises to pay him a sum of money if he would go ahead with the performance, is there a consideration for the promise? A situation like this arose in *Shadwell v Shadwell*.<sup>189</sup>

The plaintiff was already engaged to be married to a girl, named Ellen Nicholl. His uncle, the defendant, sent him the following letter: ‘I am glad to hear of your intended marriage with Ellen Nicholl; and, as I promised

187. *Aker Oil & Gas Technology UK Plc v Sovereign Corporate Ltd*, 2002 CLC 557 (QBD).

188. *Narayanrao Jagobaji Gowande Public Trust v State of Maharashtra*, AIR 2016 SC 823.

189. (1860) 9 CB (NS) 159: 142 ER 62: 127 RR 604.

to assist you at starting, I am happy to tell you that I will pay to you £150 yearly during my life, and until your annual income derived from your profession of a Chancery barrister shall amount to 600 guineas.'

The question was what was the consideration for the uncle's promise. The majority judgment was delivered by ERLE CJ who found sufficient consideration to sustain the promise. According to his Lordship the promise of the annuity might have been intended as an inducement to the marriage. "The plaintiff may have made the most material changes in his position... and have incurred pecuniary liabilities resulting in embarrassments, which could be in every sense a loss, if the income which had been promised should be withheld." His lordship also noted that there was some benefit to the promisor as the marriage of a near relative is always an object of interest.

BYLES J dissented. In his opinion the letter disclosed no consideration. "Marriage of the plaintiff at the testator's express request would be, no doubt, an ample consideration; but the marriage of the plaintiff without the testator's request is no consideration to the testator..., for the plaintiff before the letter had already bound himself to marry, by placing himself not only under a moral but under a legal obligation, to marry and the testator knew it."<sup>190</sup>

To the same effect is the decision in *Scotson v Pegg*:<sup>191</sup> The plaintiffs were carrying a cargo of coal aboard their ship and had contracted with the charterer to deliver it to his order. The charterer ordered the coal to be delivered to the defendant. The defendant promised to unload the ship at a specified rate if the shipowner would deliver the coal to him. This the shipowner agreed to do, but the defendant delayed unloading for a few days putting the plaintiffs to loss. In an action by the plaintiffs to recover the loss, the defendant contended that there was no consideration for his promise as the shipowner was already bound by his contract with the charterer to deliver the cargo to him. Nevertheless the court held for the plaintiff. WILDE B observed as follows: I accede to the proposition that if a person contracts with another to do a certain thing, he cannot make the performance of it a consideration for a new promise to the same individual. But there is no authority for the proposition that where there has been a promise to one person to do a certain thing, it is not possible to make a valid promise to another to do the same thing. Therefore, deciding this matter on principles it is plain to my mind that the delivery of the coals to the defendant was a good consideration for his promise, although the plaintiffs had made a previous contract to deliver them to the order of other persons.

The principle of these cases has been followed in India by the High Court of Madhya Pradesh in *Firm Gopal Co Ltd v Firm Hazarilal Co*:<sup>192</sup> The

190. Followed in India in *Indermal v Ram Prasad*, AIR 1970 MP 40, where a person who had agreed to execute a sale-deed did so only when a third person promised to give him a promissory note for Rs 30,000 held, that the promise was for consideration.

191. (1861) 6 H&N 295: 158 ER 121: 123 RR 516.

192. AIR 1963 MP 37.

plaintiff was under a contract to purchase some bales of cotton from a mill, but refused to fulfil a substantial part of his contract as the prices of cloth had fallen down. The defendants, who were the sole selling agents of the mill and who had guaranteed the performance of the contract, requested the plaintiff to take the whole of the quota of bales fixed for delivery in the first month and promised that they would buy from the plaintiff a part of such bales at the contract price or pay him Rs 25,000 at his option. The plaintiff complied with their request and elected to take Rs 25,000. The defendants contended that their promise was void for want of consideration as the plaintiff was already bound to take the cotton. The court reviewed English authorities and said: "From these decisions it appears that the second agreement brings into existence a new contract between different parties and therefore a promise to do a thing which the promisee is already bound to do under a contract with a third party can be good consideration to support a contract."

Here also the courts have to safeguard a party from being blackmailed into extra payment.

A vessel was chartered to carry a consignment of tractors to Yemen. The freight was prepaid by the consignees. The charterers, however, defaulted in their payment of hire to the shipowners, because there was congestion at the port of discharge and the ship had proceeded to other ports. During this period the shipowners negotiated an extra payment by the consignees for the discharge of cargo. The consignees agreed to pay, but, after the cargo was discharged, refused to make the payment.

It was held that the promise of extra payment did not create any estoppel against the consignees. There being no consideration for the promise, it was not enforceable.<sup>193</sup>

### Consideration and motive

Consideration should be distinguished from motive or a pious desire to fulfil an obligation. "Motive is not the same thing with consideration." This well-known phrase occurs in the judgment of PATTERSON J in *Thomas v Thomas*:<sup>194</sup> A testator, on the day of his death, had verbally said in front of witnesses that he was desirous that his wife should enjoy certain premises for her life. The executors, who were also the assignees, "in consideration of such desire and of the premises," agreed with the widow to convey the premises to her provided she would pay to the executors the sum of £1 yearly towards the ground rent and keep the said house in repair. On the question of consideration for the agreement between the executors and the widow the court pointed out that the motive for the agreement was, unquestionably, respect for the wishes of the testator. But that was no part of the

193. *Syros Shipping Co SA v Elagbill Trading Co*, (1981) 3 All ER 189.

194. (1842) 2 QB 851, 859.

legal consideration for the agreement. Motive should not be confounded with consideration. The agreement was, however, held to be binding as the undertaking to pay the ground rent was a sufficient consideration.<sup>195</sup>

### Absence of consideration

In a case where the promissory note was apparently genuine, neither forged, nor fabricated, the lender was allowed to recover the loan amount with interest. The court said that a bare denial of the passing of consideration does not make any defence. Something which is probable has to be brought on record so that the court may either believe that consideration did not exist or that its non-existence was so probable that a prudent man would, under the circumstances of the case, act on the belief that it did not exist.<sup>196</sup>

## EXCEPTIONS TO CONSIDERATION

### Contracts under seal in English Law

In English law a contract under seal is enforceable without consideration. In the words of Anson: "English law recognises only two kinds of contract, the contract made by deed that is under seal, which is called a deed or specialty, and the simple contract."<sup>197</sup> A contract under seal means a contract which is in writing and which is "signed, sealed and delivered".

### Exceptions under Section 25, Contract Act

Indian law, however, does not recognise any such exception. But Section 25 of the Contract Act lays down a few exceptions.

#### S. 25. An agreement made without consideration is void, unless.—

- (1) **it is in writing and registered.**—It is expressed in writing and registered under the law for the time being in force for registration of [documents], and is made on account of natural love and affection between parties standing in a near relation to each other; or unless
- (2) **or is a promise to compensate for something done.**—It is a promise to compensate, wholly or in part, a person who has already voluntarily done something for the promisor, or something which the promisor was legally compellable to do; unless
- (3) **or is a promise to pay a debt barred by limitation law.**—It is a promise, made in writing and signed by the person to be charged therewith, or by his agent generally or specially authorised in that behalf, to pay wholly or in part a debt of which the creditor might have enforced payment but for the law for the limitation of suits.

195. The distinction thus drawn between a moral obligation and consideration was approved by the Madhya Pradesh High Court in *Firm Gopal Co Ltd v Firm Hazarilal Co*, AIR 1963 MP 37 at p. 40.

196. *Atma Singh v Lachman Dass*, (2009) 4 SCC 668 P&H.

197. A.G. Guest, PRINCIPLES OF THE LAW OF CONTRACT (22nd Edn, 1964) 65.

In any of these cases, such an agreement is a contract.

*Explanation 1.*—Nothing in this section shall affect the validity, as between the donor and donee, of any gift actually made.

*Explanation 2.*—An agreement to which the consent of the promisor is freely given is not void merely because the consideration is inadequate; but the inadequacy of the consideration may be taken into account by the Court in determining the question whether the consent to the promisor was freely given.

#### *Illustrations*

- (a) A promises, for no consideration, to give to B Rs 1000. This is a void agreement.
- (b) A, for natural love and affection, promises to give his son, B, Rs 1000. A puts his promise to B into writing and registers it. This is a contract.
- (c) A finds B's purse and gives it to him. B promises to give A Rs 50. This is a contract.
- (d) A supports B's infant son. B promises to pay A's expenses in so doing. This is a contract.
- (e) A owes B Rs 1000, but the debt is barred by the Limitation Act. A signs a written promise to pay B Rs 500 on account of the debt. This is a contract.
- (f) A agrees to sell a horse worth Rs 1000 for Rs 10. A's consent to the agreement was freely given. The agreement is a contract notwithstanding the inadequacy of the consideration.
- (g) A agrees to sell a horse worth Rs 1000 for Rs 10. A denies that his consent to the agreement was freely given.

#### *1. Natural love and affection*

The essence of the first exception is that a written and registered agreement based on natural love and affection between near relatives is enforceable without consideration.<sup>198</sup> Who is a near relative? The Act provides no guidance, nor has the expression been judicially construed. The expression will without doubt include parties related by blood or marriage. Again, what is meant by natural love and affection? There is always some degree of instinctive love and affection between parties nearly related. But this instinct may sometimes be overruled by external circumstances. Thus, for example, in *Rajlukhy Dabee v Bhootnath Mookerjee*:<sup>199</sup>

The defendant promised to pay his wife a fixed sum of money every month for her separate residence and maintenance. The agreement was contained in a registered document which mentioned certain quarrels and disagreements between the two.

The Calcutta High Court refused to regard the agreement as one covered by the exception. The court could find no trace of love and affection between the parties whose quarrels had compelled them to separate.<sup>200</sup>

198. Love and affection has to be the basis of the promise because otherwise emotional expressions and human sentiments cannot take the place of consideration in the material sense of the word. See *Surendra Behari Lal v Jodonath*, 1984 All LJ 21 (NOC), transfer of a house allotted to a member to his brother-in-law, held void for want of consideration.

199. (1899–00) 4 CWN 488. Prize chits are not without consideration, not necessary to attract S. 25. *Sanchaita Investment v State of W.B.*, AIR 1981 Cal 157.

200. See also *Appa Pillai v Ranga Pillai*, ILR (1882) 6 Mad 71. In this case a member of an undivided Hindu family by a registered document renounced all rights in the family property in

With this should be contrasted the decision of the Bombay High Court in *Bhiwa v Shivaram*:<sup>201</sup>

A sued B, his brother, for a share in certain lands. But the suit was dismissed as B solemnly affirmed that the property was not ancestral; B then agreed by registered writing to give A one-half of the same property. The present suit was brought to obtain that share.

The plaintiff admitted that he and his brother had long been on bad terms. But in spite of the strained relations, the court held "that this is just the case to which Section 25(1) should be held to apply. The defendant had such natural love and affection for his brother that in order to be reconciled to him, he was willing to give him his property."<sup>202</sup>

A family settlement between a man and his wife was made for providing maintenance to wife. This was held to be enforceable because it was meant for deriving satisfaction and peace of mind from family harmony. So it could be interpreted either as a consideration or as love and affection.<sup>203</sup> The court followed the decision of the Supreme Court in *Ram Charan Das v Girja Nandini Devi*<sup>204</sup> where it was observed that "the courts give effect to a family settlement upon the broad and general ground that its object is to settle existing or future disputes regarding property among members of a family. The word 'family' in this context is not to be understood in the narrow sense of being a group of persons who are recognised in law as having the right of succession or having a claim to a share in the property in dispute .... The consideration for such a settlement, if one may put it that way, is the expectation that such a settlement will result in establishing or ensuring amity and goodwill among persons bearing relationship with one and another. That consideration having passed by each of the disputants, the settlement consisting of recognition of the right asserted by each other cannot be permitted to be impeached thereafter." The same view was again reiterated in *Maturi Pullaiah v Maturi Narasimham*.<sup>205</sup>

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favour of the other members who agreed to maintain him in the family. This promise was held to be void as the plaintiff did not seem to have been moved by love and affection in renouncing his share.

201. (1899) 1 Bom LR 495.

202. See also *Ram Dass v Kishan Dev*, AIR 1986 HP 9, a family settlement between cousins (brother and sister) to resolve disputes regarding family property on account of natural love and affection, held binding. The court recognised a cousin (brother) as a near relative.

203. *Manali Singhal v Ravi Singhal*, AIR 1999 Del 156.

204. AIR 1966 SC 323: (1965) 3 SCR 841.

205. AIR 1966 SC 1836; *Radhakrishna Joshi v Syndicate Bank*, (2006) 1 AIR Kant 692: (2006) 2 All LJ (NOC) 403 (Kant), loan advanced to defendant's son under self employment scheme, father executed documents undertaking and acknowledging to pay. He was held liable though he was not a guarantor. The case came within the exception because nature obliges parents to provide for children. There was also consideration because he purchased his family peace by saving the attachment of his sons estate. 6 per cent interest was allowed to the bank and not 14 per cent. *Ranganayakamma v K.S. Prakash*, (2005) AIR Kant 2654: 2005 AIHC 4410 (Kant), family partition, inadequacy of consideration without fraud, not sufficient, point not raised in pleadings and raised only after 21 years, not tenable.

A power of attorney was executed by a sister, relinquishing her right to share in joint family properties in favour of her brother on token of Re 1 but out of love and affection for the brother also authorising the brother to enter into partition agreement on her behalf. The document was in writing and registered. She was held to be bound by her promise, it being wholly covered by the exception.<sup>206</sup>

## 2. Past voluntary service

Secondly, a promise to compensate wholly or in part, a person who has already voluntarily done something for the promisor, is enforceable. In other words, a promise to pay for a past voluntary service is binding. It is necessary to attract this exception that the service should have been rendered voluntarily<sup>207</sup> and also for the promisor. Thus where services were rendered for a company not then in existence, a subsequent promise to pay for them could not be brought within the exception. But a promise made after attaining majority to pay for goods supplied to the promisor during minority has been held to be within the exception.<sup>208</sup> The court in that case said: "It is now settled law that a promise by an infant is in law a mere nullity and void, but we fail to see how an agreement made by a person of full age to compensate a promisee, who has already voluntarily done something for the promisor even at a time when the promisor was a minor does not fall within the purview of Section 25(2) of the Indian Contract Act. As at the time when the thing was done the minor was unable to contract, the person who did it for the minor must, in law, be taken to have done it voluntarily. But he has in fact *done something* for the minor, and if words mean anything at all, surely his case must be deemed to come within the scope of the Act."

Earlier the Bombay High Court had held in *Sindha Shri Ganpatsinghji v Abraham*<sup>209</sup> that "services rendered at the desire of the minor expressed during his minority and continued at the same request after his majority form a good consideration for a subsequent express promise by him in favour of the person who rendered the services".<sup>210</sup>

Another situation covered by the exception is where the promisee has done something for the promisor "which the promisor was legally compelled to do". A subsequent promise to pay for the act is enforceable.

206. *Ranganyakamma v K S Prakash*, (2008) 15 SCC 673.

207. See *T.V. Krishna Iyer v Official Liquidator of Cape Comorin General Traffic Co*, AIR 1952 TC 99, where it was held that the payment of bonus will not come under S. 25(2) as the employees render services in return for wages and not voluntarily. See also *Kalip Das v Durgadas Roy*, (1922–23) 27 CWN 769; *Raja of Venkatagiri v Rao Bahadur Krishnayya*, (1948) 61 LW 545: AIR 1948 PC 150.

208. *Karam Chand v Basant Kaur*, 1911 Punjab Rec No 31, p. 91.

209. ILR (1896) 20 Bom 755.

210. See also *Abdulla Darakhan v Purshottam Darakhan*, ILR 1947 Bom 807: AIR 1948 Bom 265, where it was pointed out that a promise given for any motive other than the desire to compensate the promisee would not be within the exception.

### 3. Time-barred debt

Lastly, a promise to pay a time-barred debt is enforceable.<sup>211</sup> The promise should be in writing. It should also be signed by the promisor or “by his agent generally or specially authorised in that behalf”.<sup>212</sup> The promise may be to pay the whole or any part of the debt. The debt must be such “of which the creditor might have enforced payment but for the law for the limitation of suits”.

Is it necessary that the promise should be given by the person who was liable for the original time-barred debt? The Bombay High Court has held that “a promise made by a person who is under no obligation to pay the debts of another ... does not fall within the clause.”<sup>213</sup> But in the opinion of the Madras High Court “the words ‘by the person to be charged therewith’ in Section 25(3) are wide enough to include the case of a person who agrees to become liable for the payment of a debt due by another and need not be limited to the person who was indebted from the beginning.”<sup>214</sup>

An admission by the legal heir of a deceased debtor in his deposition in the court to the effect that he was willing to pay the principal time-barred amount was held to be a promise to pay making him liable.<sup>215</sup>

“The promise referred to in Section 25(3) must be an express one and cannot be held to be sufficient if the intention to pay is unexpressed and has to be gathered from a number of circumstances. There must be a distinct promise to pay before the document can be said to fall within the provisions of the section.” Thus a debtor’s letter to his creditor “to come and receive” what was due to him, was held to disclose no express promise. A brief note by the promisor on the back of the promissory note written at the expiry of the period of limitation that he had taken the loan and unaccompanied by any words promising or undertaking to pay, was held to be not sufficient to attract Section 25.<sup>216</sup> In another case there was a demand by a landlord for rent including time-barred rent. The tenant replied that the rent may

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211. It is different from acknowledgment of liability because that has to be within the period of limitation, whereas under this exception the matter is ex hypothesi an already time-barred debt. Hence, the promisee gets new cause of action. *Umesh Chandra Chakravarty v Union Bank of India*, (1991) 1 Gau LR 223. A pronote executed for a time-barred debt was held to be enforceable, *Indian Bank v C.K. Syed Mohammed*, (1997) 2 KLJ 290.
212. *A.V. Murthy v B.S. Nagabasawanna*, (2002) 3 Bom CR 13 (SC), distinction between acknowledgment before expiry of limitation and promise to pay after expiry of limitation. *Rakesh Kumar Dinesh Kumar v UG Hotels & Resorts Ltd*, AIR 2006 HP 135, the buyer of goods defaulted in payment, he made an offer in writing to pay a certain amount in full and final settlement, the seller accepted part payment. The court said that a new contract as to payment arose, the plea of time bar was not available.
213. *Pestonji Manekji Mody v Bai Meherbai*, AIR 1928 Bom 539.
214. *Puliyath Govinda Nair v Parekalathil Achutan Nair*, AIR 1940 Mad 678.
215. *SBI v Dilip Chandra Singh Deo*, AIR 1998 Ori 129.
216. *Tulsi Ram v Same Singh*, AIR 1981 Del 165; *SBI v Dilip Chandra Singh Deo*, AIR 1998 Ori 129, no definite understanding was spelt out that the defendant would clear the dues of his late mother. He had made one payment towards the over-drawn account and undertook in writing to clear the dues. Such undertaking was distinguished from a promise. *Narendra V.*

be collected by cash or cheque, but mentioned no amount. This was not regarded by the court as a promise to pay a time-barred debt.<sup>217</sup> As against it, in another case, where an acknowledgment of a debt was coupled with an agreement to pay interest, it was held to be an agreement with a promise to pay within the meaning of Section 25(3).<sup>218</sup> Similarly, where a tenant in a letter to the landlord referred to the arrears of time-barred rent and said: "I shall send by the end of the Vysakh month", it was held that the document contained the ingredients required by Section 25(3).<sup>219</sup> Where, in a reply to a notice, the authorised advocate stated that on receiving payment from a third person the account with the plaintiff will be settled, it was held that this amounted to a promise to pay.<sup>220</sup>

The Bombay High Court has given a new turn to this exception by holding that a statement in the balance sheet of a firm signed by a partner showing that the firm was indebted to the plaintiff in respect of the stated sum became an implied promise to pay.<sup>221</sup> In reply to a winding-up petition, the company admitted its liability and also promised to pay by a letter to the creditor. The debt being time-barred at the time, the letter revived it.<sup>222</sup>

A cheque issued for a time-barred debt would still fall within the purview of Section 138, Negotiable Instruments Act in view of Sections 25(3).<sup>223</sup>

An acknowledgement of a debt is something different from a promise of this kind. An acknowledgement has to take place before expiry of the period of limitation only then the period of limitation becomes extended.<sup>224</sup> Section 25(3) requires a promise to pay a time-barred debt. It thereby becomes a new contract. It is not just merely the acknowledgement of an existing liability.<sup>225</sup>

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*Kanekar v Bardez Taluka Coop Housing Mortgage Society Ltd*, (2006) 6 Bom CR 874, issue of a cheque for a time-barred debt does not create liability under S. 138 of the Negotiable Instruments Act, that section requires an enforceable debt or liability:

217. *Daulat Ram v Som Nath*, AIR 1981 Del 354. It is not necessary that the new promise should expressly mention the time-barred debt. *Bishambhar Dayal v Vishwanath*, AIR 1985 All 12; *Canara Bank v Vijay Shamrao Ghatole*, (1996) 5 Bom CR 338, a mere admission of liability, not sufficient to attract the section. *Kadir Usman Malawar v Dattatraya Bhaskar Sinkar*, (2005) 4 Mah LJ 1076, signed promise in writing made with knowledge that it was for payment of past debt, binding.
218. *Debi Prasad v Bhagwati Prasad*, AIR 1943 All 63.
219. *Appa Rao v Suryaprakao Rao*, ILR (1899) 23 Mad 94.
220. *Panicker v Prabhakaran*, (1993) 2 KLJ 380; (1993) 2 KLT 417. The court followed *Noor Mohammad Rawther v Charu*, 1959 KLJ 168; *Puliyath Govinda Nair v Parekalathil Achutan Nair*, AIR 1940 Mad 678 where it was held that "a promise to pay a part of the barred debt cannot be taken to be a promise to pay the whole of the debt. If a person promised to pay a portion of a barred debt, he can only be sued for that portion alone and not for the whole debt."
221. *R. Sureshchandra & Co v Vadnere Chemical Works*, AIR 1991 Bom 44.
222. *Business Forms Ltd v Ashoka Agencies*, AIR 1996 Cal 153.
223. *Ramakrishnan v Gangadharan Nair*, AIR 2007 NOC 2033 (Ker); 2007 Cri LJ 1486.
224. *Madishetti Shekar v Puliyala Komurelli*, (2008) 1 APLJ 9 SN.
225. *MNS Charities v Pilla Ramaraao*, (2009) 2 APLJ 226; *Bank of Baroda v D Radha Krishna Reddy*, (2008) 1 ICC 633 AP, a banker can exercise its right of lien even in respect of a claim which is time-barred.

### **Gift actually made [S. 25 (Expln. I)]**

The provisions as to consideration do not affect, as between donor and donee, the validity of any gift which has actually been made. A gift of movables which has been completed by delivery and gift of immovables which has been perfected by registration cannot be questioned as to their validity only on the ground of lack of consideration. They may be questioned otherwise. Where a gift of property was made by registered deed and attested by two witnesses, it was not allowed to be questioned by the donor on the ground that she was the victim of fraud which she was not able to establish.<sup>226</sup>

### **Inadequacy of consideration [S. 25 (Expln. II)]**

For notes see under “Adequacy of Consideration” (*supra*).

The inadequacy of the consideration is a fact which the Court should take into account in considering whether or not A's consent was freely given.

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226. *Vasant Rajaram Narvekar v Ankusha Rajaram Narvekar*, (1995) 3 Bom CR 196; *K. Balakrishnan v K. Kamalam*, (2004) 1 SCC 581, gift by mother to her minor son under gift deed with the right to be in the property up to her life time. The son kept it with his father and did not repudiate on attaining majority. Thus, accepted and became irrevocable.

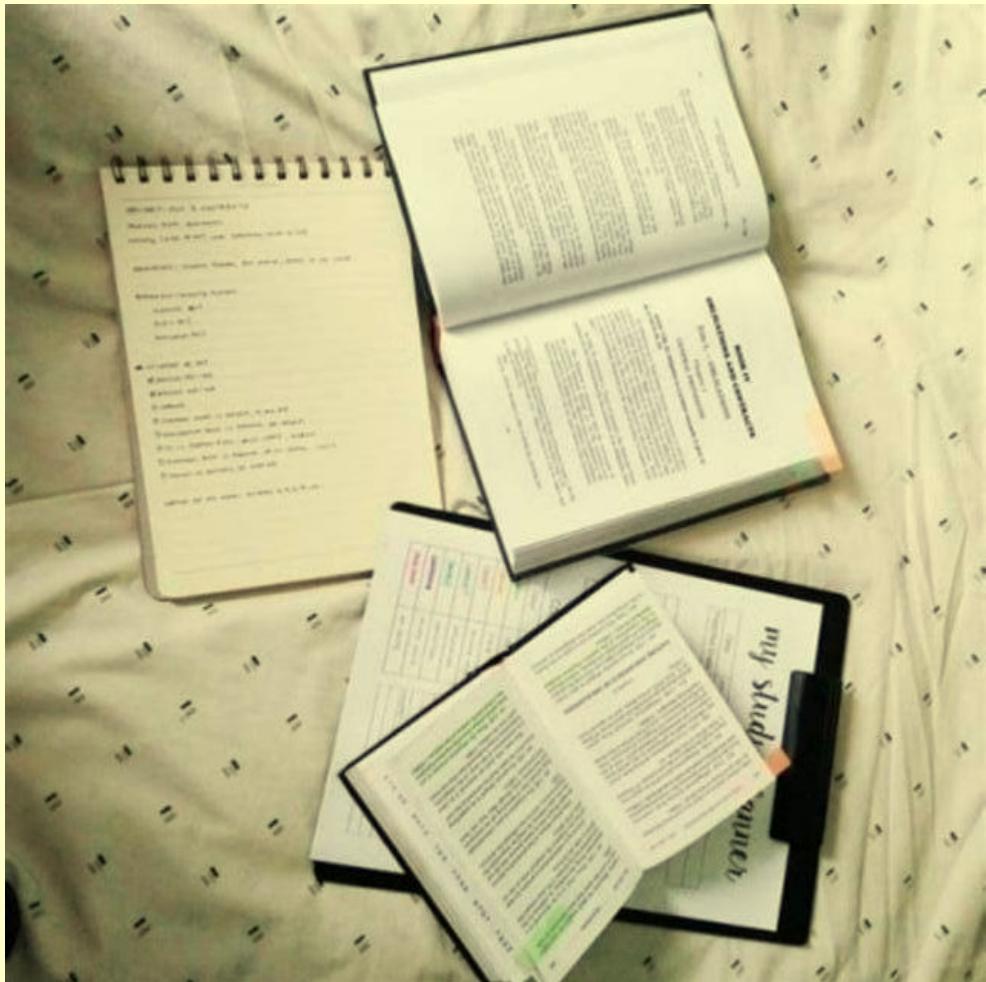
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- *Abdul Aziz v Masum Ali*, AIR 1914 All 22: ILR (1914) 36 All 268
- *Doraswami Iyer v Arunachala Ayyar*, AIR 1936 Mad 135
- *Kedarnath Bhattacharji v Gorie Mahomed*, ILR (1986) 14 Cal 64
- *Nawab Khwaja Muhammad Khan v Nawab Hussaini Begum*, (1909–10) 37 IA 152

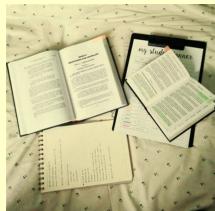




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## Capacity to Contract

Section 10 of the Contract Act requires that the parties must be competent to contract. Competence to contract is defined in Section 11:

**S. 11. Who are competent to contract.**—Every person is competent to contract who is of the age of majority according to law to which he is subject, and who is of sound mind, and is not disqualified from contracting by any law to which he is subject.

Thus, the section declares the following persons to be incompetent to contract—

- (1) minors,
- (2) persons of unsound mind, and
- (3) persons disqualified by law to which they are subject.<sup>1</sup>

### MINOR

#### Age of majority

The age of majority is generally eighteen, except when a guardian of a minor's person or property has been appointed by the court, in which case it is 21.<sup>2</sup> The age of majority of a person is to be determined "according to the law to which he is subject".<sup>3</sup>

In England the age of majority formerly was 21 years. But now under the Family Law Reform Act, 1969, "a minor is a person under the age of eighteen years". Formerly a minor was referred to as an "infant", but this Act has changed the term to "minor".

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1. *Ashok Kumar J. Pandya v Suyog Coop Housing Society Ltd*, AIR 2003 NOC 118 (Guj): 2002 AIHC 3401, a housing society agreed to sell land before it became a legal person by registration. Not enforceable.

2. The Indian Majority Act, 1875, S. 3, which reads:

"Every person domiciled in India shall be deemed to have attained his majority when he shall have completed his age of eighteen years, and not before. In the case, however, of a minor of whose person or property or both a guardian has been appointed by a court, or of whose property the superintendence is assumed by a court of wards, before the minor has attained the age of eighteen years, when he has completed the age of 21 years."

3. The section defines inherent competence to be a party to a contract, and not competence for being an agent or representative, etc. *Dharmeshwar Kalita v Union of India*, AIR 1955 Ass 86.

### Nature of minor's agreement

Section 10 requires that the parties to a contract must be competent and Section 11 declares that a minor is not competent. But neither section makes it clear whether, if a minor enters into an agreement, it would be voidable at his option or altogether void. These provisions had, therefore, quite naturally given rise to a controversy about the nature of a minor's agreement.<sup>4</sup> The controversy was only resolved in 1903 by the Judicial Committee of the Privy Council in their well-known pronouncement in *Mohori Bibee v Dhurniodas Ghose*.<sup>5</sup> Sir Lord NORTH observed: "Looking at Section 11 their Lordships are satisfied that the Act makes it essential that all contracting parties should be competent to contract and expressly provides that a person who by reason of infancy is incompetent to contract cannot make a contract within the meaning of the Act. The question whether a contract is void or voidable presupposes the existence of a contract within the meaning of the Act, and cannot arise in the case of an infant."

Ever since this decision it has not been doubted that a minor's agreement is absolutely void. In England also the Infants' Relief Act of 1874 declares the following categories of a minor's agreement to be "absolutely void".

- (1) contract for repayment of money lent or to be lent, or
- (2) contract for goods supplied or to be supplied (other than necessary), and
- (3) contract for accounts stated.<sup>6</sup>

Any other rule would have made the law asymmetrical leaving it to the whim of a child to pick and choose between agreements made by him which he will and which he will not enforce. A child may show poor judgment in making a particular contract, and it is a protection against his own ignorance and immaturity—not merely fraudulent manipulation by others—that the law affords. The general presumption that every man is the best judge of his own interests is suspended in the case of children.<sup>7</sup>

The ruling of the Privy Council in the *Mohori Bibee* case has been generally followed by the courts in India and applied both to the advantage and disadvantage of minors. Another decision of the Privy Council in line is *Mir Sarwarjan v Fakhruddin Mahomed Chowdhury*.<sup>8</sup> "A contract to purchase

4. There is no provision as to the effect of incompetency.

5. (1902–03) 30 IA 114: ILR (1903) 30 Cal 539 (PC); *Lakhwinder Singh v Paramjit Kaur*, AIR 2004 P&H 6: (2004) 1 ICC 151, sale deed of property of minor executed by the minor's power of attorney holder, held not binding, the buyer made no inquiries into the matter. *Ram Ashish Chaudhary v State of U.P.*, 2003 All LJ 330, appointment of persons below age as teachers held, void ab initio. *M.S. Madhusoodhanan v Kerala Kaumudi P Ltd*, (2004) 9 SCC 204, minor's share of property sold by legal guardian to his father who in turn transferred it further, valid.

6. Apart from these categories, the contract of an infant may be either valid or voidable at his option. Anson's PRINCIPLES OF THE ENGLISH LAW OF CONTRACT (1964) 178.

7. Anthony T. Kronman, *Paternalism and the Law of Contract*, (1988) 92 Yale LJ 763, 786.

8. (1911–12) 39 IA 1: (1912) 39 Cal 232 PC. Also followed in *Ma Hnit v Fatima Bibi*, (1926–27) 54 IA 145 (PC).

certain immovable property had been made by a guardian on behalf of a minor, and the minor sued the other party for a decree of specific performance to recover possession. His action was rejected.”

The court said that it was not within the competence either of the manager of the minor’s estate or of the guardian of the minor, to bind the minor or the minor’s estate by a contract for the purchase of immovable property; that as the minor was not bound by the contract, there was no mutuality; and that consequently the minor could not obtain specific performance of the contract.

In its subsequent pronouncement in *Sirkakulam Subramanyam v Kurra Subba Rao*<sup>9</sup> the Privy Council overruled earlier decisions and entertained no doubt that it was within the powers of the mother of a minor as guardian to enter into a contract of sale for the purpose of discharging his father’s debts. Following this decision the Orissa High Court held that endowment of property for religious purposes by guardians on behalf of minors, being within their competence, was specifically enforceable.<sup>10</sup> The other High Courts have also expressed the view that the doctrine of mutuality should not have been imported into the matter where the contract was within the competence of the guardian and that there is no scope for this doctrine under Section 20 of the Specific Relief Act, 1963.<sup>11</sup> If the contract is within the competence of the guardian and it is for the benefit of the minor it is specifically enforceable.<sup>12</sup>

In today’s society it does not seem to be possible, much less desirable, for law to adhere to the categorical declaration that a minor’s agreement is always “absolutely void”. Minors are appearing in public life today more frequently than even before. A minor has to travel, to get his dresses tailored, or cleaned, to visit cinema halls and deposit his cycle at a stand. He has to deal with educational institutions and purchase so many things for the facility of life and education. If, in any one of these cases, the other party to the contract could brush aside the minor on the ground that the engagement is void, the legal protection against contractual liability would be too dear to minors. The Privy Council had, therefore, to modify its earlier decisions. This trend is evidenced by the decision of their Lordships in *Srikakulam Subrahmanyam v Kurra Subba Rao*.<sup>13</sup> In order to pay off the debts of his father, which were promissory notes owing to the appellants and a mortgage to another, a minor son and his mother sold a piece of land to

9. (1947–48) 75 IA 115: AIR 1948 PC 25.

10. *Durga Thakurani Bije Nijigarb v Chintamoni Swain*, AIR 1982 Ori 158.

11. *Vadakattu Suryaprakasham v Ake Gangaraju*, AIR 1956 AP 33. For the power of the manager of a family to contract on behalf of the family including minor members, see *CIT v Hukumchand Mannalal & Co*, (1970) 2 SCC 352: AIR 1971 SC 383: (1971) 1 SCR 646. Properties belonging to certain minors were contracted to be sold to raise money for their marriages. Specific enforcement allowed.

12. *Gopalkrishna Govind v Tukaram Narayan*, AIR 1956 Bom 566; *CIT v Shah Mohandas Sadhuram*, AIR 1966 SC 15.

13. (1947–48) 75 IA 115: ILR 1949 Mad 141 PC.

the appellants in satisfaction of the notes, requiring that the appellants pay off the mortgage debt. The appellants, accordingly, paid off the mortgagee and took possession. Afterwards the minor brought an action to recover back the land. It was found as a fact that the transaction was for the benefit of the minor and the guardian had the capacity to contract on his behalf. Lord MORTON said that Section 11 and the *Mohori Bibi* case leave no doubt that a minor cannot contract and that if the guardian and the mother had taken no part in this transaction it would have been void. The contract being for the benefit of the minor and within the power of the guardian was held to be binding upon him.

### Effects of minor's agreement

A minor's agreement being void, ordinarily it should be wholly devoid of all effects.<sup>14</sup> If there is no contract, there should, indeed, be no contractual obligation on either side. Consequently, all the effects of a minor's agreement must be worked out independently of any contract.

#### 1. No estoppel against minor

Suppose that a minor by misrepresenting his age induces another to contract with him, will there be any estoppel against him, or, in other words, will he be precluded from disclosing his true age in a litigation resulting from the contract? Even this question had at one time created a controversy. But it is now settled by a preponderance of authority that there is no such estoppel against the minor.<sup>15</sup> The infant is not estopped from setting up the defence of infancy. The reason is very simple. There can be no estoppel against a statute. The policy of the law of contract is to protect persons below age from contractual liability and naturally the doctrine of estoppel cannot be used to defeat that policy. Thus, in a case before the Bombay High Court,<sup>16</sup> BEAUMONT CJ reviewed the earlier authorities and concluded by saying: "The court is of opinion that where an infant represents fraudulently or otherwise that he is of age and thereby induces another to enter into a contract with him then in an action founded on the contract the infant is not estopped from setting up infancy."

14. An agreement which confers benefits on a minor is not only not void, but is enforced at his instance. A minor's consent, being nullity, it cannot change matters, in this case, matters relating to validity of possession. See *Padma Vithoba Chakkayya v Mohd Multani*, AIR 1963 SC 70, 74; (1963) 3 SCR 229; minor releasing rights in a property, infructuous, see *Wali Singh v Sohan Singh*, AIR 1954 SC 263; family settlements are binding, but minor's position under it will depend upon the principle that a minor's agreement is void.

15. See, for example, *Jagar Nath Singh v Lalta Prasad*, ILR (1908–10) 21 All 21, where the courts said: "the law of estoppel cannot be invoked in aid to validate that which is void under the law". *Kanhayalal v Girdharilal*, (1912) 9 All LJ 103 pleading minority against a promissory note, allowed.

16. *Gadigeppa Bhimappa Meti v Balangowda Bhimangowda*, AIR 1931 Bom 561, where the court reviewed all authorities on this point.

## 2. No liability in contract or in tort arising out of contract

A minor's agreement is, of course, in principle devoid of all legal effects. "A minor is in law incapable of giving consent, and, there being no consent, there could be no change in the character" or status of the parties.<sup>17</sup> In England it was laid down as early as 1665 in *Johnson v Pye*<sup>18</sup> that "an infant who obtains a loan of money by falsely representing his age cannot be made to repay the amount of the loan in the form of damages for deceit". The court pointed out that if infants were held liable on their contracts by means of actions in tort, all the infants of England would be ruined. Hence a minor cannot be held responsible for anything which would be an indirect way of enforcing his agreement. "You cannot convert a contract into a tort to enable you to sue an infant."<sup>19</sup> This principle has been generally followed in India. The Calcutta High Court, for example, refused to hold a minor liable in tort for money lent on a bond.<sup>20</sup> The court said: "If the tort is directly connected with the contract and is the means of effecting it and is a parcel of the same transaction, the minor is not liable in tort."<sup>21</sup>

But where the tort is independent of the contract, the mere fact that a contract is also involved, will not absolve the infant from liability. Thus, where an infant borrowed a mare for riding only, he was held liable when he lent her to one of his friends who jumped and killed her.<sup>22</sup> Similarly, in another case, an infant was held liable for the tort of detenue for his failure to return certain instruments which he had hired and then passed on to a friend.<sup>23</sup>

ATKIN J's (as he then was) judgment in *Fawcett v Smethurst*<sup>24</sup> explains the earlier cases and also the test for ascertaining whether the tort in question is independent of the contract. "The principle of law applicable to this case is that which is referred to in *Leslie (R) Ltd v Sheill*<sup>25</sup> where KENNEDY LJ in his judgment cites with approval the following passage from POLLOCK ON CONTRACTS:<sup>26</sup> 'He (i.e., the infant) cannot be sued for a wrong when the cause of action in substance is *ex contractu*, or is so directly connected with the contract that the action would be an indirect way of enforcing the contract.... But if an infant's wrongful act, though concerned with the subject-matter of a contract, and such that but for the contract there would have been no opportunity of committing it, is nevertheless independent of

17. *Padma Vithoba Chakkayya v Mohd Multani*, AIR 1963 SC 70, 74: (1963) 3 SCR 229.

18. (1665) 1 Sid 258: 82 ER 1091.

19. *Jennings v Rundall*, (1799) 101 ER 1419: (1799) 8 TR 335; also cited in *Leslie (R) Ltd v Sheill*, (1914) 3 KB 607 (CA), 618.

20. *Harimohan v Dulu Miya*, ILR (1934) 61 Cal 1075.

21. For another illustration of the same principle see *Radhey Shiam v Biharilal*, ILR (1918) 40 All 558: (1918) 48 IC 478. An agreement by a minor to release his rights in a property is equally infructuous. *Wali Singh v Sohan Singh*, AIR 1954 SC 263, 265.

22. *Burnard v Haggis*, (1863) 4 CBN 45: 8 LT 328.

23. *Ballet v Mingay*, 1943 KB 281 (CA).

24. (1914) 84 LJKB 473: 112 LT 309.

25. (1914) 3 KB 607 (CA), 618.

26. (8th Edn) 78.

the contract in the sense of not being an act of the kind contemplated by it, then the infant is liable.' In the present case the car was hired for the purpose of going to Cairn Ryan and back, but was in fact driven further. In my opinion nothing that was done upon that further journey made the defendant an independent tortfeasor; and, if any damage was done to the car on that journey, the defendant would only be liable if he were liable under the contract made.... In *Burnard v Haggis*,<sup>27</sup> the defendant who was a Cambridge undergraduate and an infant, hired a horse for the purpose of going for a ride, expressly stating that he did not want a horse for jumping. The defendant let the horse to a friend, who used it for jumping, with the result that it fell and was injured. The defendant was liable on the ground that the act resulting in injury to the horse was one which was quite outside the contract, and could not be said to be an abuse of the contract. In *Jennings v Rundall*,<sup>28</sup> on the other hand, where the defendant, an infant, had hired a horse to be ridden for a short journey and took it on a much longer journey, with the result that it was injured, the court held the defendant not liable upon the ground that the action was founded in contract and that the plaintiff could not turn what was in substance a claim in contract to one in tort."

### 3. Doctrine of restitution

If an infant obtains property or goods by misrepresenting his age, he can be compelled to restore it, but only so long as the same is traceable in his possession. This is known as the equitable doctrine of restitution. Where the infant has sold the goods or converted them, he cannot be made to repay the value of the goods, because that would amount to enforcing a void contract.<sup>29</sup> Again, the doctrine of restitution is not applied where the infant has obtained cash instead of goods. The well-known authority is *Leslie (R) Ltd v Sheill*:<sup>30</sup>

An infant succeeded in deceiving some money-lenders by telling them a lie about his age, and so got them to lend him £400 on the faith of his being an adult.

Their attempt to recover the amount of principal and interest as damages for fraud failed for the reasons explained above. They then claimed the return of the principal moneys under a *quasi-contract* as "money had and received to the plaintiff's use". To this Lord SUMNER replied: "Further, under the statute<sup>31</sup> the principal, which at common law relieved an infant

27. (1863) 4 CBNS 45: 8 LT 328.

28. (1799) 8 TR 335: (1799) 101 ER 1419.

29. There has been, however, one case in England, namely, *Stocks v Wilson*, (1913) 2 KB 235, where an infant was held liable to account for the value of certain furniture and other articles which he had resold after obtaining them from the plaintiff by misrepresentation of age. The decision was criticised a year later by Lord SUMNER in *Leslie (R) Ltd v Sheill*, (1914) 3 KB 607 (CA), 618, and is not likely to be followed.

30. (1914) 3 KB 607 (CA), 618.

31. His Lordship was considering the effect of the Infants' Relief Act, 1874.

from liability for a tort directly connected with a voidable contract, namely, that it was impossible to enforce in a roundabout way an unenforceable contract, equally forbids the courts of law to allow, under the name of an implied contract or in the form of an action *quasi ex contractu*, a proceeding to enforce part of a contract, which the statute declares to be wholly void.”<sup>32</sup>

Finally, the money-lenders relied upon the doctrine of restitution, contending that the infant should be compellable in equity to restore the money. Rejecting this contention, Lord SUMNER said:

“I think that the whole current of decisions down to 1913 ... went to show that, when an infant obtained an advantage by falsely stating himself to be of full age, equity required him to restore his ill-gotten gains, or to release the party deceived from obligations or acts in law induced by the fraud, but scrupulously stopped short of enforcing against him a contractual obligation, entered into while he was an infant, even by means of a fraud .... Restitution stopped where repayment began.

... the money was paid over in order to be used as the defendant's own and he has so used it and, I suppose, spent it. There is no question of tracing it, no possibility of restoring the very thing got by the fraud, nothing but compulsion through a personal judgment to repay an equivalent sum out of his present and future resources .... I think this would be nothing but enforcing a void contract.”<sup>33</sup>

#### *Minor seeking relief, compellable to restore*

However, where an infant invokes the aid of the court for the cancellation of his contract, the court may grant the relief subject to the condition that he shall restore all benefits obtained by him under the contract, or make suitable compensation to the other party.<sup>34</sup>

This aspect of the doctrine of restitution found expression in Section 41 of the original Specific Relief Act of 1877.<sup>35</sup> The section authorised the courts to order any compensation that justice required to be paid by the party at whose instance a contract was cancelled. The first well-known case decided under the section is that of *Mohori Bibee v Dhurmodas Ghose*.<sup>36</sup>



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32. *Leslie (R) Ltd v Sheill*, (1914) 3 KB 607 (CA), 613.

33. *Ibid*, 618.

34. See, for example, *Jagar Nath Singh v Lalta Prasad*, ILR (1908–10) 21 All 21, where a minor was allowed to recover possession of property sold by him only subject to the condition that he restored the consideration. This principle was approved by the Privy Council in *Mahomed Syedol Ariffin v Yeoh Ooi Gark*, (1915–16) 43 IA 256: AIR 1916 PC 242. *Padinhare Veetil Madhavi v Pachikaran Veetil Balakrishnan*, AIR 2010 Ker 111, mother sold minor's share without court permission, suit for setting aside by minor on attaining majority, minor refused restoration of benefits obtained, no relief allowed.

35. The section ran as follows: “On adjudging the cancellation of an instrument, the Court may require the party to whom such relief is granted to make any compensation to the other party which justice may require.”

36. (1902–03) 30 IA 114: ILR (1903) 30 Cal 539 (PC).

The plaintiff, a minor, mortgaged his houses in favour of the defendant, a money lender, to secure a loan of Rs 20,000. A part of this amount was actually advanced to him. While considering the proposed advance, the attorney, who was acting for the money lender, received information that the plaintiff was still a minor. Subsequently the infant commenced this action stating that he was underage when he executed the mortgage and the same should, therefore, be cancelled.

The relief of cancellation had to be granted as the plaintiff was entitled to it under Section 39 of the Specific Relief Act, 1877 [S. 31 of 1963]. The money lender's only request was that the relief should be made subject to the condition of the minor repaying to him the sum of Rs 10,500 advanced as part of the consideration for the mortgage. He first relied upon Section 64 of the Contract Act. According to this section, a person who, having the right to do so, rescinds a voidable contract, he shall have to restore to the other party any benefit received by him under the contract. The Privy Council held that this section applies only to voidable contracts and cannot apply to the agreement of a minor, which is absolutely void. Similarly no relief was allowed under Section 65 of the Act. The essence of this section is that a party receiving any benefit under a contract shall have to restore it if the contract becomes void or is discovered to be void. Quite obviously the Privy Council said "that this section, like Section 64, starts from the basis of there being an agreement or contract between competent parties, and has no application to a case in which there never was, and never could have been, any contract."<sup>37</sup>

Finally, the money-lender relied upon Section 41 of the Specific Relief Act, 1877 [S. 33 of 1963], which was as follows: "On adjudging the cancellation of an instrument the court may require the party to whom such relief is granted to make any compensation to the other which justice may require." As to this their Lordships said: "This section no doubt gave a discretion to the court; but the court of first instance and subsequently the Appellate Court, in the exercise of such discretion, came to the conclusion that under circumstances of this case justice did not require them to order the return by the respondent of money advanced to him with full knowledge of his infancy, and their Lordships see no reason for interfering with the discretion so exercised."

There was alienation of a minor's property by a de facto guardian. The minor repudiated the sale on attaining majority. The purchaser was fully aware that the de facto guardian was incompetent to alienate. It was held that the minor was not liable to restore to the purchaser benefits obtained by him. Purchaser's remedy was to proceed against the de facto guardian.<sup>38</sup>

37. *Mohori Bibee v Dhurmadas Ghose*, (1902–03) 30 IA 114: ILR (1903) 30 Cal 539 (PC).

38. *Maniyan Nadar v Harikumar*, AIR 2015 Ker 183.

The second landmark decision in this line of cases on the extent of relief available against a fraudulent minor was the decision of the Lahore High Court in *Khan Gul v Lakha Singh*.<sup>39</sup>

The defendant, while still a minor, by fraudulently concealing his age, contracted to sell a plot of land to the plaintiff. He received the consideration of Rs 17,500 and then refused to perform his part of the bargain.

The plaintiff prayed for recovery of possession or refund of consideration. There could be no question of specific enforcement, the contract being wholly void. The only question, therefore, was: "Can a minor who has entered into a contract by false representation refuse to perform the contract and at the same time retain the benefit he may have received therefrom?" Section 41 of the Specific Relief Act, 1877, would not help the plaintiff as Sir SHADILAL CJ admitted that "the language of the section no doubt shows that the jurisdiction conferred thereby is to be exercised when the minor himself invokes the aid of the court." Nor would the principle of restitution as explained by Lord SUMNER in *Leslie (R) Ltd v Sheill*<sup>40</sup> be of any help unless it was extended in India to cover cases of money also. The learned Chief Justice found sufficient reason for this extension as he said: "There is no real difference between restoring the property and refunding the money, except that the property can be identified but cash cannot be traced.... It must be remembered that, while in India all contracts made by infants are void, there is no such general rule in England. There should therefore be a greater scope in India than in England for the application of the equitable doctrine of restitution."<sup>41</sup>

Referring to Sections 39 and 41 of the Specific Relief Act, 1877 [now Ss. 31 and 33 of Act 1963], His Lordship said: "The doctrine of restitution is not however confined to cases covered by those sections. The doctrine rests upon the salutary principle that an infant cannot be allowed by a court of equity to take advantage of his own fraud." Accordingly, the learned Chief Justice ordered refund of the consideration.<sup>42</sup>

This opinion was not followed by the Allahabad High Court in another landmark on the subject, namely, *Ajudhia Prasad v Chandan Lal*.<sup>43</sup>

A sum of money was borrowed by two minors under a mortgage deed. They were more than 18 but less than 21 years of age, but fraudulently concealed the fact that a guardian had been appointed for them. The question was whether the lender could get a decree for the principal money or sale of mortgaged property.

SULAIMAN CJ who delivered the judgment of the Full Bench, refused to follow the enlarged view of restitution as applied by Sir SHADILAL CJ in

39. ILR (1928) 9 Lah 701: AIR 1928 Lah 609.

40. (1914) 3 KB 607 (CA), 618.

41. *Khan Gul v Lakha Singh*, ILR (1928) 9 Lah 701, 715-19.

42. See also *Dattaram v Vinayak*, ILR (1903) 28 Bom 181.

43. AIR 1937 All 610 (FB).



*Khan Gul v Lakha Singh.*<sup>44</sup> His Lordship felt that the courts in India were probably bound by the principle of restitution as explained and restricted by Lord SUMNER in *Leslie (R) Ltd v Sheill*,<sup>45</sup> as it had already been approved by the Privy Council. In the opinion of his Lordship, any other “view would be contrary to the great preponderance of authority both in England and in India and would ignore the well-recognised distinction between the position of a minor when suing as a plaintiff and when he is being sued as a defendant.”<sup>46</sup> The learned Chief Justice added: “Where the property is not traceable and the only way to grant compensation would be by granting a money decree against the minor, decreeing the claim would be almost tantamount to enforcing the minor’s pecuniary liability under the contract which is void.... There is no rule of equity, justice and good conscience which entitles a court to enforce a void contract of a minor against him under the cloak of restitution.”

The Andhra Pradesh High Court had aligned itself with the Allahabad High Court.<sup>47</sup> After an extensive review of authorities, SUBBA RAO CJ said that the effect of the authorities is “that a person, who has parted with his goods can trace them into the hands of the quondam minor and recover them back in specie, for he has not lost his title to them. But he cannot seek to recover their price or damages, for, if allowed to do so, the court would be enforcing the contract of loan”.

In the matter of a mortgage in favour of a minor, it has been held by the Supreme Court that the minority of the mortgagee renders it *void ab initio*.<sup>48</sup>

### *Amended provisions in the Specific Relief Act, 1963*

The Law Commission of India preferred the view of Sir SHADILAL CJ and accordingly the controversy has now been set at rest by the new Specific Relief Act, 1963. The principle of restitution is contained in Section 33 of the new Act. The net result of the amendment may be stated in terms of the following two propositions:

- (1) Where a void or voidable contract has been cancelled at the instance of a party thereto, the court may require him to restore such benefits as he has received under the contract and to make any compensation to the other party which justice may require.
- (2) Where a defendant successfully resists any suit on the ground that the contract, by reason of his being incompetent, is void against him, he may be required to restore the benefits, if any, obtained by him under the contract, but only to the extent to which he or his estate has benefited thereby.

44. ILR (1928) 9 Lah 701; AIR 1928 Lah 609.

45. (1914) 3 KB 607 (CA), 618.

46. *Ajudhia Prasad v Chandan Lal*, AIR 1937 All 610, 617 (FB).

47. *Gokeda Latcharao v Viswariadham Bhimayya*, AIR 1956 AP 182.

48. *Mathai Mathai v Joseph Mary*, (2015) 5 SCC 622; AIR 2014 SC 2277.

Sub-section (1) of the above provision, as noted before, incorporates the principle that he who seeks equity must do equity. The courts have the discretion to require the minor-plaintiff to restore the advantages he has obtained under a void agreement. A good illustration of the circumstances in which this power is to be exercised is *Jagar Nath Singh v Lalta Prasad*,<sup>49</sup> where BANERJI J of the Allahabad High Court said: "Where persons who are in fact underage induce others to purchase property from them, they are liable in equity to make restitution to the purchasers for the benefit they have obtained before they can recover possession of the property sold."<sup>50</sup>

But the court will not compel any restitution by a minor even when he is a plaintiff, where the other party was aware of the infancy so that he was not deceived,<sup>51</sup> or where the other party has been unscrupulous in his dealings with the minor,<sup>52</sup> or where, though the minor had misrepresented his age, the other party was so zealous to enter into the transaction that the false representation exerted no influence on him,<sup>53</sup> or where the other party lays no material before the court for coming to the conclusion that justice requires return of the money paid to the minor.<sup>54</sup>

Section 33(1) of the Specific Relief Act, 1963 does not alter the earlier law. If the minor comes to the court as a plaintiff, he can be compelled to disgorge his gains under the agreement. Sub-section (2), however, makes this difference that if a minor is brought before the court as a defendant, he can be compelled to account for such portion of the money or anything else received by him as has gone to benefit him personally, such as education or training, or has resulted in an accretion to his estate.

### Beneficial contracts

The law declared by the Privy Council in the *Mohori Bibi* case<sup>55</sup> that a minor's agreement is "absolutely void" has been generally followed, but it has been growingly "confined to cases where a minor is charged with obligations and the other contracting party seeks to enforce those obligations against the minor."<sup>56</sup> It was observed by ABDUR RAHIM J of the Madras High Court that "what is meant by the proposition that an infant

49. ILR (1908–10) 21 All 21.

50. *Lalta Prasad v Jagar Nath Singh*, ILR 1909 All 21 at p. 27.

51. *Bhim Mandal v Mangaram Corain*, AIR 1961 Pat 21; *Shiamlal v Ram Piari*, ILR (1910) 32 All 25; *Radhey Shiam v Bihari Lal*, ILR (1918) 40 All 558; (1918) 48 IC 478; *Harimohan v Dulu Miya*, ILR (1934) 61 Cal 1075. In all these cases the minor had committed no fraud and, therefore, he was allowed to recover the property sold without restoring the consideration obtained by him.

52. *Mohd Said v Bishamber Nath*, AIR 1924 All 156.

53. *K. Maungll v Ma Hda On*, 1939 Rang 545.

54. *Kampa Prasad v Sheo Gopal Lal*, ILR (1904) 26 All 342; *T.S. Bellieraj v Vinodhini Krishnakumar*, (2004) 2 CTC 510, transfer of a minor's property by the guardian without obtaining an order of court was held to be violative of S. 8 of the Hindu Minority and Guardianship Act.

55. *Mohori Bibee v Dhurmodas Ghose*, (1902–03) 30 IA 114; ILR (1903) 30 Cal 539 (PC).

56. *A.T. Raghava Chariar v O.M. Srinivasa Raghava Chariar*, ILR (1916) 40 Mad 308.

is incompetent to contract or that his contract is void is that the law will not enforce any contractual obligation of an infant". Accordingly, a minor is allowed to enforce a contract which is of some benefit to him and under which he is required to bear no obligation. In *Raghava Chariar v Srinivasa*,<sup>57</sup> the following question was referred for the decision of a Full Bench of the Madras High Court: "Whether a mortgage executed in favour of a minor who has advanced the whole of the mortgage money is enforceable by him or by any other person on his behalf."

The unanimous opinion of the Full Bench was that the transaction was enforceable by or on behalf of the minor. WALLIS CJ said:

"The provision of law which renders minors incompetent to bind themselves by contract was enacted in their favour and for their protection, and it would be a strange consequence of this legislation if they are to take nothing under transfers in consideration of which they have parted with their money."<sup>58</sup>

The same opinion was expressed by BEAUMONT CJ of the Bombay High Court:<sup>59</sup> "The provisions of the law which make a contract by a minor not binding were no doubt intended to be for the benefit of the minors, and the courts in this country when faced with a contract which has been carried out by or on behalf of the minor, the performance of which by the other party is then resisted on the ground of minority, have struggled hard to avoid holding the contract wholly void to the detriment of the minor."

Accordingly, the learned Chief Justice rejected the defence of an insurance company that the person on whose behalf certain goods were insured was a minor and allowed the minor to recover the insurance money.<sup>60</sup>

On the same principle it has been held that "a minor is capable for purchasing immovable property and he may sue to recover the possession of the property purchased upon tender of the purchase money."<sup>61</sup> A transfer which has already been executed in favour of a minor can, of course, be much less impeached.<sup>62</sup>

57. *Ibid.*

58. *A.T. Raghava Chariar v O.A. Srinivasa Raghava Chariar*, (2011) 3 MWN (Civ) 1 (FB), nothing in the Contract Act prevents an infant from being promisee, where consideration passes from minor, he can enforce the promise of the adult promisor; if the consideration for the promise is transfer of property by minor, promise would be unenforceable. Minor is wholly incompetent to transfer property. Minor can seek cancellation of the transfer of property to him by returning the consideration to the other party.

59. *Great American Insurance Co Ltd v Mandanlal Sonulal*, ILR (1935) 59 Bom 656.

60. The decision achieves substantial justice, there is no fault with it. It would have been absurd to allow an insurer to escape responsibility having accepted the proposal with full knowledge of the plaintiff's minority. *Chekha Adinarayana v Oriental Fire & General Insurance Co Ltd*, AIR 2006 NOC 479 (AP), Marine Insurance Act, S. 3 insurance of boat, insured were minors at the time, this fact was not brought to the notice of the insurer, claim was rejected because the fact of accident was doubtful, rejection of the case by the trial court, insurance being void, was held to be proper.

61. *Thakar Das v Pulli*, AIR 1924 Lah 611.

62. *Ulfat Rai v Gauri Shankar*, ILR (1911) 33 All 657, where the court said that "there is nothing in the Transfer of Property Act which makes a minor incapable of being the transferee of

“A lease, however, is not like other transfers of property and a lease to a minor has been held to be void.”<sup>63</sup> A minor may enforce a promissory note executed in his favour.<sup>64</sup> “There is nothing in the Contract Act to prevent an infant from being the promisee.” “The law does not regard a minor as incapable of accepting a benefit.”<sup>65</sup> A gift of some property under a deed executed by the mother in favour of her minor child was held to be binding on the mother. The fact that the mother had reserved to herself the possession and enjoyment of the property did not destroy the effectiveness of the gift.<sup>66</sup>

All these cases proceed on the principle that the minor has already given the full consideration to be supplied by him and there is nothing that remains to be done by him under the contract. He is now a mere promisee and prays the court for recovering the benefit stipulated. But where the contract is still executory or the consideration is still to be supplied, the principle of the *Mohori Bibi* case<sup>67</sup> will thwart any action on the contract. In *Raj Rani v Prem Adib*:<sup>68</sup>

The plaintiff, a minor, was allotted by the defendant, a film producer, the role of an actress in a particular film. The agreement was made with her father. The defendant subsequently allotted that role to another artist and terminated the contract with the plaintiff's father.

The Bombay High Court held that neither she nor her father could have sued on the promise. If it was a contract with the plaintiff, she being a minor, it was nullity. If it was a contract with her father it was void for being without consideration. The promise of a minor girl to serve, being not enforceable against her, cannot furnish any consideration for the defendant's promise to pay her a salary.<sup>69</sup>

Where a minor has given consideration under a contract, but the consideration given to him has failed, he may have restitution. Thus, where a minor bought a zamindari property on payment of money, but he was ousted on a suit by a third party, it was held “that the minor was at any rate entitled to recover from the vendor the sum which he had paid as purchase money”.<sup>70</sup>

For this principle to apply there should be total failure of consideration. Where, for example, a minor purchased shares in a company and then repudiated them and also asked for refund of the partly paid purchase price, the court held that the price which he has already paid was not refundable,

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immovable property. He cannot transfer immovable property, it is true, but that is a different thing from recovering as transferee”.

63. *Jaykant Harkishandas Shah v Durgashankar Vilji Pandya*, AIR 1970 Guj 106.

64. *Sharfath Ali v Noor Mahomed*, AIR 1924 Rang 136.

65. Ibid; *Vijayakumar Motilal v New Zealand Insurance Co Ltd*, AIR 1954 Bom 347, right to recover under insurance.

66. *K. Balakrishnan v K. Kamalam*, (2004) 1 SCC 581: AIR 2004 SC 1257; *K. Balakrishnan v K. Kamalam*, (2004) 1 SCC 581: AIR 2004 SC 1257.

67. *Mohori Bibee v Dhurmadas Ghose*, (1902–03) 30 IA 114: ILR (1903) 30 Cal 539 (PC).

68. AIR 1949 Bom 215.

69. *Ibid* at p. 217, by DESAI J.

70. *Walidad Khan v Janak Singh*, AIR 1935 All 370.

because there was evidence that the shares were of some value. If the shares were totally worthless there would have been a total failure of consideration entitling the minor to refund. But he was not liable to pay further demands or calls for payment.<sup>71</sup>

“When an infant has paid for something and has consumed or used it, it is contrary to natural justice that he should recover back the money which he has paid.” This is the principle of the well-known case of *Valentini v Canali*:<sup>72</sup>

The plaintiff, a minor, agreed with the defendant to become a tenant of his house and to pay £100 for the furniture therein. He paid £68 in cash and gave a promissory note for the balance. The plaintiff occupied the premises and used the furniture for some months and then brought an action for the refund of the consideration paid by him.

The court ordered the cancellation of the promissory note, but refused to order refund of the sum paid. “The infant plaintiff had the quantity use of furniture for some months. He could not give back this benefit or replace the defendant in the position in which he was before the contract.... The legislature never intended, in making provisions for this purpose (for the protection of infants), to sanction a cruel justice.”<sup>73</sup>

### *Contracts of marriage*

A contract for the marriage of a minor is also *prima facie* for his or her benefit. “It is customary amongst most of the communities in India for parents to arrange marriages between their minor children and the law has to adapt itself to the habits and customs of the people.” It has, therefore, become well-established, almost without any controversy, “that while the contract of marriage could be enforced against the other contracting party at the instance of the minor it cannot be enforced against the minor”.<sup>74</sup> Where the agreement for marriage of a minor involves statutory violation, e.g. the Hindu Marriage Act, 1955, the age of the girl has to be 18 years, the agreement is likely to be avoided. In this case, on the date of engagement the girl was not of 18 years but on the date fixed for marriage she would have completed 18 years. The agreement was held to be valid. The other party ran away from the agreement. The court allowed her compensation of Rs 27,000

71. *Steinberg v Scala (Leeds) Ltd*, (1923) 2 Ch 452 (CA).

72. LORD COLERIDGE CJ in *Valentini v Canali*, (1889) 24 QBD 166: (1886–90) All ER Rep 883: 59 LJ QB 74.

73. BEAUMONT CJ, commenting on this case in *Khimji Kuveriji Shah v Lalji Karamsi Raghavji*, AIR 1941 Bom 129.

74. KANIA J (1941) Bom 211, 221. The Bombay High Court allowed such actions in the following cases: *Abdul Razak v Mohd Hussain*, ILR (1916) 42 Bom 499; *Rose Fernandez v Joseph Gonsalves*, ILR (1924) 48 Bom 673; *Janak Prasad v Gopi Krishna Lal*, AIR 1947 Pat 132. Those decisions are, however, subject to the provisions of applicable laws as to age of marriage.

for mental pain and suffering, lowering of esteem in society and amount spent on engagement ceremony.<sup>75</sup>

### *Marriage of Muslim minor girl*

Parties were governed by Shariat law. The medical report showed that the girl had not attained the age of majority. She had, therefore, no right to enter into the contract of marriage on her own free will. She could have been given in marriage only by her father or guardian. The *Kazi* who performed the ceremony of marriage was in know of things. The marriage was not valid. She could not have been forced to live with her husband against the mandate of *Quran Sharif*. The father was entitled to her custody.<sup>76</sup>

### *Contracts of apprenticeship*

Contracts of apprenticeship is another species of contracts which are for the benefit of minors. The Indian Apprentices Act, 1850 provides for contracts in the nature of contracts of service which are binding on minors. The Act was passed, as the preamble of the Act shows: "For better enabling children, and specially orphans and poor children brought up by public charity, to learn trades, crafts and employments, by which, when they come to full age, they may gain a livelihood."<sup>77</sup>

The Act requires the contract to be made by a guardian on behalf of the minor. [S. 9]

"In English law contracts of service and apprenticeship are put on the same footing and in the same category as contracts for necessaries." The well-known English case on the subject is *Roberts v Gray*.<sup>78</sup>

The defendant, an infant, agreed with the plaintiff, a noted billiards player, to join him in a billiards-playing tour of the world. The plaintiff spent time and money in making arrangements for billiards matches, but the defendant repudiated the contract. The plaintiff succeeded in recovering damages for the breach of the contract.

The contract was held to be one for necessaries as it was for the infant's "good teaching or instruction whereby he may profit afterwards". The most important part of the contract was the instruction that would be received

75. *Tulshiram v Roopchand*, (2006) 2 Mah LJ 647: AIR 2006 Bom 183; *Punjabrao Deorao v Sheshrao*, AIR 1962 Bom 175: 1960 Nag LJ 302, giving away a minor in marriage is opposed to public policy. In *Rajendra Bahadur Singh v Roshan Singh*, AIR 1950 All 592, the court held that betrothal itself was in the nature of a contract. *Ma Pua Kyue v Maung Hmat Gyi*, AIR 1939 Rang 86, a Buddhist girl sought to enforce a promise to marry made to her, when she was less than 18 years. The court held that she could not enforce such a promise. Here, the question was not of specific performance of promise to marry. The question was of getting damages for breach of promise. *Khimji Kuveriji Shah v Lalji Karamsi Raghavji*, AIR 1941 Bom 129, the court categorically ruled that a guardian can enter into a contract of betrothal on behalf of minor children and also can sue for breach.

76. *Kumari Shahnoor Md Tahseen v State of U.P.*, AIR 2007 NOC 437 (All).

77. See the judgement of DESAI J in *Raj Rani v Prem Adib*, AIR 1949 Bom 215, 218-19.

78. (1913) 1 KB 520 (CA).

by the defendant from playing constantly with the plaintiff under the conditions of a worldwide tour, a thing which a distinguished billiards player apparently contemplates as part of his career.<sup>79</sup>

It has been suggested by DESAI J of the Bombay High Court in *Raj Rani v Prem Adib*<sup>80</sup> that “though according to English Law the minor would be liable in the case of a contract of service where the contract was for his benefit, it is clear that under Section 11, the minor’s contract being void, the minor would not be held liable”.

#### *Trade contracts not included in beneficial contracts*

This category of beneficial contracts does not include ordinary trade contracts. In *Cowern v Nield*<sup>81</sup>, for example, a minor was carrying on business as a hay and straw merchant. He received a cheque from the plaintiff for the supply of clover and hay. He delivered the clover which was rejected as bad and failed to deliver hay. The plaintiff’s action for recovering back the amount of the cheque failed. PHILLIMORE J observed: “In a general sense contracts which can be brought within certain categories and are also for the benefit of the infant can be supported. A trading contract does not come within any of these categories. The only contracts of an infant which can be enforced are which relate to the infant’s person, as contracts by which he provides himself with clothes, food, or lodging or contracts of marriage, apprenticeship and service.”

#### *Option to retire from beneficial contracts on majority*

A minor will have the option of retiring from a contract of beneficial nature on attaining majority provided that he exercises the option within a reasonable time. Where a minor in pursuance of a marriage settled his after-acquired property and after attaining majority he received a large sum of money under the will of his father which came under the settlement, and, therefore, he attempted to repudiate the settlement, the House of Lords held that the repudiation coming five years after attaining majority was too late.<sup>82</sup>

#### **Ratification**

A person cannot on attaining majority ratify an agreement made by him during his minority.<sup>83</sup> Ratification relates back to the date of the making of the contract and, therefore, a contract which was then void cannot be made valid by subsequent ratification.<sup>84</sup> “It would be a contradiction in terms to say that a void contract can be ratified.”<sup>85</sup> If it is necessary, a fresh contract

79. To the same effect *Doyle v White City Stadium Ltd*, (1935) 1 KB 10.

80. AIR 1949 Bom 215.

81. (1912) 2 KB 419.

82. *John Edwards and Henry Isaacs v Robert Brudenell Carter*, 1893 AC 360 (HL).

83. *Nazir Ahmad v Jiwan Das*, AIR 1938 Lah 159.

84. *Tukaram Ramji Shendre v Madhorao Manaji Bhange*, AIR 1948 Nag 293.

85. *Bhola Ram Harbans Lal v Bhagat Ram*, AIR 1927 Lah 24.

should be made on attaining majority. And a new contract will also require a fresh consideration. “The consideration which passed under the earlier contract cannot be implied into the contract into which the minor enters on attaining majority.”<sup>86</sup> In a case before the Full Bench of the Allahabad High Court the facts were:<sup>87</sup>

A minor borrowed a sum of money, executing a simple bond for it, and after attaining majority executed a second bond in respect of the original loan plus interest. It was held by a majority of two as against one that the suit upon the second bond was not maintainable, as that bond was without consideration and did not come under Section 25(2) of the Contract Act. SULAIMAN CJ said: “Section 25, sub-clause (2), applies when there is a promise to *compensate* wholly or in part a person who has already *voluntarily done something for the promisor*. The word ‘compensate’ has been used advisedly and does not connote the same idea as a loan. The word ‘voluntarily’ also indicates to my mind that something has been done without any promise of compensation.... Similarly the expression ‘done something for’ does not mean ‘advance money to another person’. Doing something for a person is not paying money to him.”<sup>88</sup>

Where, however, a person, after attaining majority has not only ratified but also paid the debt incurred by him during minority, he cannot afterwards recover it back. In the view of the Allahabad High Court such a debt is only void and not unlawful.<sup>89</sup>

Where, in addition to the consideration already given during minority, a further advance is made or a fresh consideration given after majority, a promise to pay the whole of the amount, in the opinion of the Calcutta<sup>90</sup> and Allahabad<sup>91</sup> High Courts, becomes binding. “There is no question of ratification in such cases.”<sup>92</sup> A person can always make a fresh promise after attaining majority in terms of the promise made during minority. All that is necessary is that there should be some fresh consideration for it.<sup>93</sup>

Some wind of change is reflected by the following decision. The defendant was minor at the time when he executed a deed about his interest in the estate. The suit was filed at a time when he had attained majority. He did not repudiate the agreement on attaining majority. He rather admitted it. The contract became enforceable to the extent of the minor’s interest in the estate.<sup>94</sup>

86. *Nazir Ahmad v Jiwan Das*, AIR 1938 Lah 159.

87. *Suraj Narain v Sukhu Abir*, ILR (1928) 51 All 164.

88. Overruling its earlier decision in *Narain Singh v Chiranjilal*, AIR 1924 All 730: ILR (1924) 46 All 568.

89. *Anant Rai v Bhagwan Rai*, AIR 1940 All 12; *Magantal Kishordas Shah v Ramanlal Hiralal Shah*, 1942 SCC OnLine Bom 151: AIR 1943 Bom 362, ratification of partnership.

90. *Kundan Bibi v Shree Narayan*, (1906) 11 CWN 135.

91. *Narain Singh v Chiranjilal*, AIR 1924 All 730: ILR (1924) 46 All 568.

92. SULAIMAN CJ in *Suraj Narain v Sukhu Abir*, ILR (1928) 51 All 164, 166.

93. *Anant Rai v Bhagwan Rai*, AIR 1940 All 12, payment of mortgage debt after attaining majority.

94. *MC Nagalakshmi v MA Farook*, AIR 2007 Kant 105.

### Liability for necessities [S. 68]

Section 68 of the Contract Act provides for the liability for necessities supplied to persons incompetent to contract.

**S. 68. Claim for necessities supplied to person incapable of contracting, or on his account.**—If a person incapable of entering into a contract, or anyone whom he is legally bound to support, is supplied by another person with necessities suited to his condition in life, the person who has furnished such supplies is entitled to be reimbursed from the property of such incapable person.

#### *Illustrations*

- (a) A supplies B, a lunatic, with necessities suitable to his life. A is entitled to be reimbursed from B's property.
- (b) A supplies the wife and children of B, a lunatic, with necessities suitable to their condition in life. A is entitled to be reimbursed from B's property.

#### *Meaning of "necessaries"*

The liability is only for necessities, but there is no definition of the term "necessaries" in the Act. We may consequently turn to judicial decisions to determine its precise import.<sup>95</sup> An illustrative statement of the meaning of the term is to be found in the judgment of ALDERSON B in *Chapple v Cooper*:<sup>96</sup>

"Things necessary are those without which an individual cannot reasonably exist. In the first place, food, raiment, lodging and the like. About these there is no doubt. Again, as the proper cultivation of the mind is as expedient as the support of the body, instruction in art or trade, or intellectual, moral and religious education may be necessary also .... Then the classes being established, the subject and extent of the contract may vary according to the state and condition of the infant himself. His clothes may be fine or coarse according to his rank; his education may vary according to the station he is to fill; and the medicines will depend on the illness with which he is afflicted, and the extent of his probable means when of full age .... But in all these cases it must first be made out that the class itself is one in which the things furnished are essential to the existence and of reasonable advantage and comfort of the infant contractor. Thus articles of *mere* luxury are always excluded, though luxurious articles of utility are in some cases allowed."

Thus, "what is necessary" is a relative fact to be determined with reference to the fortune and circumstances of the particular minor; articles, therefore, that to one person might be mere conveniences or matters of taste may, in the case of another, be considered necessities, where the usage of society renders them proper for a person in the rank of life in which the

95. *Jagon Ram Marwari v Mahadeo Prosad Sahu*, ILR (1909–10) 36 Cal 768, 776.

96. (1844) 13 M&W 252, 258: 153 ER 105.

infant moves. The infant's need of things may also sometimes depend upon the peculiar circumstances under which they are purchased and the uses to which they are put.<sup>97</sup> For instance, articles purchased by an infant for his wedding may be deemed necessary, while under ordinary circumstances the same articles may not be so considered. "... Wedding presents for the bride of the infant may be necessaries."<sup>98</sup> But where such marriage is forbidden by law, the position will be different. Where "the funds are supplied to a minor for the marriage of a minor female in the family the lender may be able to get himself reimbursed from the property of the minor."<sup>99</sup> "The debt incurred for performing the funeral obsequies of the father of a minor" is a necessary.<sup>100</sup> Where a minor is involved in a litigation threatening his property<sup>101</sup> or liberty,<sup>102</sup> expenses reasonably incurred on his defence may be recovered from his estate.

"In *Peters v Fleming*<sup>103</sup> the court took judicial notice that it was *prima facie* not unreasonable that an undergraduate at a college should have a watch and consequently a watch chain; and that therefore it was a question of fact whether the watch chain supplied on credit was such as was necessary to support himself properly in his degree. PARKE B says: 'All such articles as are purely ornamental are to be rejected, as they cannot be requisite for anyone.' Possibly there may be exceptional cases in which things purely ornamental may be necessary."<sup>104</sup> The burden lies upon the supplier to prove that the ornamental thing is specially necessary for the minor. Thus, where a minor was supplied a pair of jewelled solitaires and an antique goblet and though he moved in high society, he was held not liable as the plaintiff could not prove that the articles were specially necessary for the minor.<sup>105</sup>

To render an infant's estate liable for necessaries "two conditions must be satisfied, namely: (1) the contract must be for goods reasonably necessary for his support in his station in life, and (2) he must not have already a sufficient supply of these necessaries".<sup>106</sup> The supplier has to prove, "not only that the goods supplied were suitable to the condition in life of the infant, but that he was not sufficiently supplied with the goods of that class". This is the principle of *Nash v Inman*<sup>107</sup> where an undergraduate in the Cambridge

97. *Kunwär Singh v Surajmal Makhanlal*, AIR 1963 MP 58, educational needs, house provided.

98. *Jagon Ram Marwari v Mahadeo Prosad Sahu*, ILR (1909–10) 36 Cal 768, 777.

99. *Tikki Lal Jaithu Teli v Komalchand*, AIR 1940 Nag 327: ILR 1940 Nag 632.

100. *Bechu Singh v Baldeo Prasad*, AIR 1933 Oudh 132.

101. Thus in *Kedar Nath v Ajudhia Prasad*, 1883 Punj Rec 165 at p. 522, money advanced to save a minor's estate from execution sale was held to be necessary.

102. *Shyam Charan Mal v Choudhary Deby Singh Pahraj*, ILR (1894) 21 Cal 872, where a minor was facing a criminal prosecution for dacoity, the court said: "The liberty of the minor being at stake, the money advanced must be taken to have been borrowed for necessities."

103. (1840) 6 M&W 42: 151 ER 314.

104. WILLES J in *Ryder v Woombwell*, (1868) 38 LJ Ex 8.

105. *Ibid.*

106. BUCKLEY LJ in *Nash v Inman*, (1908) 2 KB 1, 12.

107. *Ibid.*

University, who was amply supplied with proper clothes according to his position, was supplied by the plaintiff with a number of dresses, including eleven fancy waistcoats, the price was held to be irrecoverable.

### Nature of liability

There are two theories relating to the liability of a minor's estate for necessaries. According to one of the theories the liability does not depend upon the minor's consent. It arises because the necessities have been supplied to him and is, therefore, *quasi*-contractual in nature. The best statement of this theory is that of FLETCHER MOULTON LJ in *Nash v Inman*.<sup>108</sup>

"An infant, like a lunatic, is incapable of making a contract of purchase in strict sense of the word; but if a man satisfies the needs of the infant or lunatic by supplying to him necessities the law will imply an obligation to repay him for the services so rendered, and will enforce that obligation against the estate of the infant or lunatic. The consequence is that basis of the action is hardly contract. The real foundation is an obligation which the law imposes on the infant to make a fair payment in respect of needs satisfied. In other words, the obligation arises *re* and not *consensu*."

In India the subject has been dealt with in the chapter on "Certain Relations Resembling Those Created by Contract". The chapter provides for obligations of *quasi*-contractual nature. Further, the liability is not personal, but is only that of the minor's estate. Thus it has a very little contractual element.

The other view of the liability in England is that it is contractual. An infant is not absolutely destitute of contractual capacity. A contract for necessities is just one of those categories of contracts which an infant is permitted to make.<sup>109</sup>

## PERSONS OF UNSOUND MIND

### English Law

In English law a person of unsound mind is competent to contract, although he may avoid his contract if he satisfies the court that he was incapable of understanding the contract and the other party knew it. The contract is voidable at his option. It becomes binding on him only if he affirms it.<sup>110</sup> In this case Lord ESHER said that a lunatic (now such a person is known as mentally disordered) can only set aside a contract entered into with a person of sound mind in the following circumstances:

"When a person enters into a contract and afterwards alleges that he was so insane at the time that he did not know what he was doing, and proves the allegation, the contract is as binding on him in every respect,

108. *Ibid* at p. 8.

109. *Ibid* at p. 12.

110. *Imperial Loan Co v Stone*, (1892) 1 QB 599 (CA). See the judgment of Lord ESHER MR at p. 601.

whether it is executory or executed, as if he had been sane when he made it, unless he can prove further that the person with whom he contracted knew him to be so insane as not to be capable of understanding what it was about."

The position of a drunken person is also the same. If he makes a contract while drunk, he may, when sober, elect to avoid the contract or to affirm it.<sup>111</sup>

As regards the general effect of mental incapacity on the contractual competence of a person, HALSBURY'S LAWS OF ENGLAND states the following:<sup>112</sup> "There must be a free and full consent to bind persons in contract. Consent is an act of reason and of volition or choice, and it is on the ground that there is a want of rational and deliberate consent that the contracts of mentally disordered persons may be invalidated. A valid contract cannot be made by a person suffering from such incapacity of mind as not to understand the nature of what he is doing....

A fair contract with a person who was apparently of sound mind, but who in fact was suffering at the time of the contract from such mental disorder as rendered him incapable of entering into the contract, is voidable but not void. If the contract is not to be enforced against him, the person mentally disordered must prove that the other party either knew that he was of unsound mind or knew of such facts as would justify the Court in inferring such knowledge."<sup>113</sup>

In *Campbell v Hooper*,<sup>114</sup> where a mortgagee sought a decree directing repayment and foreclosure in default of such repayment and where there was evidence that at the time the mortgage was executed the mortgagor was a lunatic, STUART VC said:

"I do not understand that the simple fact of lunacy, if established, would deprive the mortgagee of all rights to equitable relief. I am not aware of any case in which it has been so held....

Even at law the contract of a lunatic is not necessarily void. Even at law the plaintiff in an action at law, seeking to recover under the contract of a person whose lunacy is established, has been held to be entitled to relief....

Mr Justice PATTESON, in *Dane v Viscountess Kirkwall*<sup>115</sup> in directing the jury laid down the law thus: 'It is not sufficient that Lady Kirkwall was of unsound mind, but you must be satisfied that the plaintiff knew it, and took advantage of it.' It would be a strange thing if a Court of Equity in dealing with contracts were to deal on any different principle."

111. *Mabews v Baxter*, (1873) LR 8 Exch 132. See the judgement of MARTIN B at p. 134.

112. Paras 1005–06, Vol 30 (4th Edn).

113. Quoted in *Che Som Binte Yip v Maha P Ltd*, (1989) 2 CLJ 802 High Court, Singapore. It is opined in this case that the word "fair" in the above statement may have to be deleted in view of the decision of the Privy Council in *Hart v O'Connor*, 1985 AC 1000, on appeal from New Zealand. In the *Maha P Ltd* case the mortgage executed by a person who was mentally unsound was enforced because it was not proved that the mortgagee bank had knowledge of his mental disorder.

114. (1855) 3 Sm&G 153.

115. (1838) 8 C&P 679.

### Position in India

In India, on the other hand, the agreement of a person of unsound mind is, like that of minor, absolutely void.<sup>116</sup> According to Section 12 “a person is said to be of sound mind for the purpose of making a contract if, at the time when he makes it, he is capable of understanding it and of forming a rational judgment as to its effects upon his interest.”<sup>117</sup> However, a person who is usually of unsound mind may make a contract when he is of sound mind. But a person who is usually of sound mind may not make a contract when he is of unsound mind.

**S. 12. What is a sound mind for the purposes of contracting.** — A person is said to be of sound mind for the purpose of making a contract if, at the time when he makes it, he is capable of understanding it and of forming a rational judgment as to its effect upon his interests.

A person who is usually of unsound mind, but occasionally of sound mind, may make a contract when he is of sound mind.

A person who is usually of sound mind, but occasionally of unsound mind, may not make a contract when he is of unsound mind.

#### Illustrations

- (a) A patient in a lunatic asylum, who is at intervals of sound mind, may contract during those intervals.
- (b) A sane man, who is delirious from fever, or who is so drunk that he cannot understand the terms of a contract, or form a rational judgment as to its effect on his interests, cannot contract whilst such delirium or drunkenness lasts.

### Disability at the time of agreement

For the purpose of declaring an agreement to be void what is relevant is that the person in question was suffering from the disability on the date of execution of the agreement, the report of medical unfitness of the year 1989 being much later in point of time was held to have no bearing on the agreements entered into in the years 1985 and 1987 respectively.<sup>118</sup>

An illustration is the decision of the Patna High Court in *Inder Singh v Parmeshwardhari Singh*.<sup>119</sup> A property worth about Rs 25,000 was agreed

116. *Machaiman v Usman Beari*, (1907) 17 MLJ 78; *Amina Bibi v Saiyid Yusuf*, ILR (1922) 44 All 748, a case of lease which was held to be void.

117. He can be favoured with benefits. *Sheoratan v Kali Charan*, 79 IC 955, Oudh, mortgage in favour of a person suffering from mental disorder.

118. *Nilima Ghosh v Harjeet Kaur*, AIR 2011 Del 104.

119. AIR 1957 Pat 491. See also *Jyotindra Bhattacharjee v Sona Bala Bora*, AIR 1994 Gau 99, the person in question filed cases against family members, remained away from house for long periods, transferred family properties to the extent of making the family homeless, the court said that all this was sufficient to indicate that the vendor was not normal and was not mentally sound at the time of sale. The purchaser adduced no evidence that the vendor was of sound mind. *Kimtu v Lachhi Devi*, 1999 AIHC 2533 (HP), selling the property of an insane by wife whose power of attorney was not valid, the purchaser also did not take care to verify facts, he resold it, the property was recovered back without having to pay anything for improvements, etc.

to be sold by a person for Rs 7000 only. His mother proved that he was a congenital idiot, incapable of understanding the transaction and that he mostly wandered about. Holding the sale to be void, SINHA J explained the effect of Section 12 in the following passage: "According to this section, therefore, the person entering into the contract must be a person who understands what he is doing and is able to form a rational judgment as to whether what he is about to do is to his interest or not. The crucial point, therefore, is to find out whether he is entering into the contract after he has understood it and has decided to enter into that contract after forming a rational judgment in regard to his interest.... It does not necessarily mean that a man must be suffering from lunacy to disable him from entering into a contract. A person may to all appearances behave in a normal fashion, but, at the same time, he may be incapable of forming a judgment of his own, as to whether the act he is about to do is to his interest or not. In the present case (he) was incapable of exercising his own judgment."

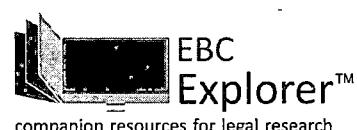
Illustration (b) appended to Section 12 shows that a drunken person is in the same category as a person of unsound mind. A sale deed of property was executed at a time when the transferor was suffering from alcoholic psychosis which was proved by medical certificate. A very valuable land was sold for a paltry amount. The sale deed was ordered by the Supreme Court to be set aside. The court said that unsoundness of mind is a finding of fact. There could be no interference in second appeal.<sup>120</sup>

A marriage between a Hindu girl and Muslim man was declared to be no marriage at all when the evidence showed that the girl was under intoxication at the material time and was not conscious of ongoing conversion and *nikah* ceremony. She also proved that she had not lived with the man even for a single day. Registration of the marriage under the Hindu Marriage Act, 1955 was also illegal. The Family Court was held to be competent to declare the status of the parties and declare the marriage to be void.<sup>121</sup>

120. *Chacko v Mahadevan*, (2007) 7 SCC 363.

121. *Asfaq Qureshi v Aysha Qureshi (Nivedita Yadav)*, AIR 2010 Chh 58 (DB).

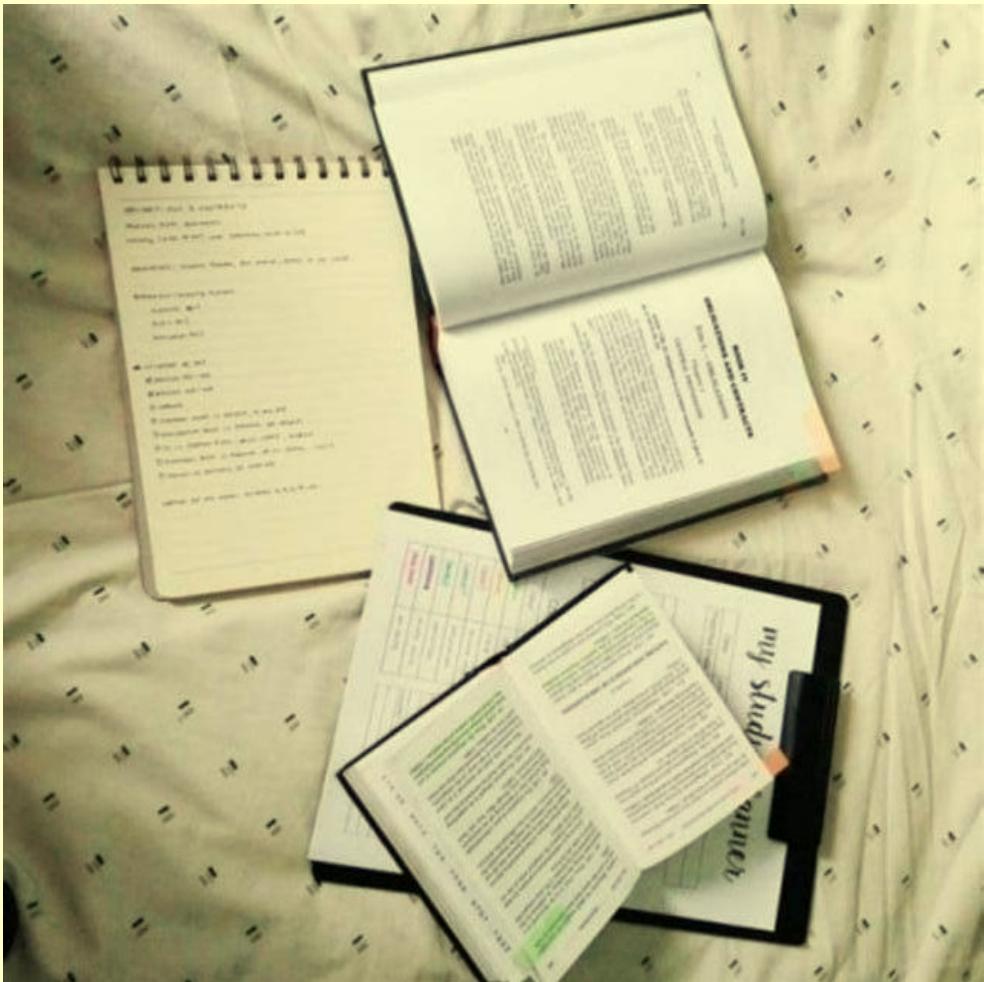
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The following cases from this chapter are available through EBC Explorer™:

- *Khan Gul v Lakha Singh*, ILR (1928) 9 Lah 701: AIR 1928 Lah 609
- *Mohori Bibee v Dhurmadas Ghose*, (1902–03) 30 IA 114: ILR (1903) 30 Cal 539 (PC)

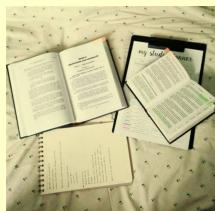




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## Free Consent

### DEFINITION OF FREE CONSENT [S. 14]

According to Section 10 free consent is an essential requirement of a contract. Section 14 defines “free consent”.

**S. 14. “Free consent” defined.**—Consent is said to be free when it is not caused by:

- (1) coercion, as defined in Section 15, or
- (2) undue influence, as defined in Section 16, or
- (3) fraud, as defined in Section 17, or
- (4) misrepresentation, as defined in Section 18, or
- (5) mistake, subject to the provisions of Sections 20, 21 and 22.

Consent is said to be so caused when it would not have been given but for the existence of such coercion, undue influence, fraud, misrepresentation or mistake.

### Vitiating factors and their effect

Where consent to an agreement is caused by coercion, undue influence, fraud or misrepresentation, the agreement is a contract voidable at the option of the party whose consent was so caused.<sup>1</sup> If, for example, a person is induced to sign an agreement by fraud, he may, on discovering the truth, either uphold the contract or reject it. If he confirms it, the contract becomes binding on both the parties. It is a contract which is enforceable at the option of only one of the parties, namely, the party whose consent was not free. Giving the meaning of a voidable contract, Section 2(i) says that “an agreement which is enforceable by law at the option of one or more of the parties thereto, but not at the option of the other or others, is a voidable contract.”<sup>2</sup>

1. Ss. 19 and 19-A. For an example of compulsory consent under a statute see *Mangaldas Raghavji Ruparel v State of Maharashtra*, AIR 1966 SC 128: (1965) 2 SCR 894, 906. *Krishna Prasad v Shyam Narayan Prasad*, AIR 2006 Sikk 25, in a deed of exchange, the stand taken by one of the executants was that only the business was included and not RCC building. Oral evidence also supported such a stand. The court said that RCC building could not be said to have been included on the basis of the recital in the deed alone.

2. See *Nokhia v State of H.P.*, AIR 1985 HP 88, where it was observed that consent to an acquisition cannot be described as a real consent. In the absence of these vitiating factors the contract binds and no one can get rid of it by unilateral action. Thus a site allotted and

Where consent is caused by mistake, the agreement is void. [Ss. 20–22]  
A void agreement is not enforceable at the option of either party. [S. 2(g)]

## COERCION

### Definition [S. 15]

An agreement the consent to which is caused by coercion is voidable at the option of the party whose consent was so caused. “Coercion” is defined in Section 15.

**S. 15. “Coercion” defined.**—“Coercion” is the committing, or threatening to commit, any act forbidden by the Indian Penal Code (XLV of 1860), or the unlawful detaining, or threatening to detain, any property, to the prejudice of any person whatever, with the intention of causing any person to enter into an agreement.

*Explanation.*—It is immaterial whether the Indian Penal Code (XLV of 1860), is or is not in force in the place where the coercion is employed.

### Illustrations

*A*, on board an English ship on the high seas, causes *B* to enter into an agreement by an act amounting to criminal intimidation under the Indian Penal Code (XLV of 1860).

*A* afterwards sues *B* for breach of contract at Calcutta.

*A* has employed coercion, although his act is not an offence by the law of England, and although Section 506 of the Indian Penal Code (XLV of 1860), was not in force at the time when or place where the act was done.

### Techniques of causing coercion

Consent is said to be caused by coercion when it is obtained by pressure exerted by either of the following techniques:

- (1) committing or threatening to commit any act forbidden by the Indian Penal Code; or
- (2) unlawfully detaining or threatening to detain any property.

### Acts forbidden by IPC

It is clear that coercion as thus defined implies a committing or threatening to commit some act which is contrary to law. The section has given rise to few decisions. The Privy Council observed in *Askari Mirza v Bibi*

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accepted by the allottee by performance of all the requirements for the purpose of establishing a nursing-home was not allowed to be cancelled by the allotting authority, *Kailash Chandra Kotia v Rajasthan State Industrial Development & Investment Corpn*, (1991) 1 Raj LR 174 Jodhpur Bench. *Sheo Ratan Prasad Gupta v Prema Devi*, (1997) 1 BLJR 695, a compromise agreement signed by the parties and their counsels, the court decided the suit by relying on it, not allowed to be questioned on the ground of lack of free consent unless there was proof of that fact available. *Hasina Bano v Alam Noor*, AIR 2007 Raj 49. The right of *mehr* can be relinquished by the wife conditionally provided that it is done voluntarily and with free consent. Facts disclosed that she had relinquished her claim. She could not claim it on being divorced under the Muslim Women (Protection of Rights on Divorce) Act, 1986.

*Jai Kishori*<sup>3</sup> that “cases brought under this particular branch of Section 15 of the Contract Act must be of rare occurrence”. A clear illustration would be consent obtained at the point of pistol, or by threatening to cause hurt, or by intimidation or by threatening to burn a man’s house or slashing his valuable picture. An intriguing question in this connection was before the Madras High Court in *Chikham Amiraju v Chikham Seshamma*:<sup>4</sup>

By threat of suicide, a Hindu induced his wife and son to execute a release in favour of his brother in respect of certain properties which they claimed as their own.

It was held by a majority “that the threat of suicide amounted to coercion within Section 15 and the release deed was, therefore, voidable”. The difference of opinion related to whether suicide is an act forbidden by the Indian Penal Code. An attempt to commit suicide is punishable under the Code, but there is no punishment provided for suicide.<sup>5</sup> The majority consisting of WALLIS CJ and SESAGIRI J believed that the man who commits suicide goes unpunished, not because the act is not forbidden, but because there is nobody left to be punished. OLDFIELD J dissented on the ground that unless an act is made punishable it cannot be said to be forbidden.

“When a criminal prosecution is instituted against a person and such person fearing the result of the prosecution enters into an agreement in favour of the complainant in consideration of his abandoning the prosecution, it cannot be held simply upon these facts that the consent of such person was caused by coercion.”<sup>6</sup> “To threaten a criminal prosecution is not *per se* an act forbidden by the Indian Penal Code. Such an act could only be one forbidden by the Indian Penal Code if it amounted to a threat to file a false charge.” This was pointed out by the Privy Council in *Askari Mirza v Bibi Jai Kishori*:<sup>7</sup>

A minor, having borrowed on two mortgage deeds, agreed to a compromise decree although the mortgages were void. Subsequently he pleaded that he entered into the compromise because he was threatened with prosecution for falsely misrepresenting his age and that this amounted to coercion. Their Lordships observed: “The law as contained in Section 15 is much wider than anything to be found in the English authorities and in India it is not correct to say that a contract is vitiated merely by proof of a threat to bring a criminal charge. Of course, if the charge of cheating

3. (1912) 16 IC 344.

4. ILR (1918) 41 Mad 33, 36.

5. S. 309, Indian Penal Code.

6. *Masjidi v Ayisha*, 1880 Punj Rec No 135, p. 398.

7. (1912) 16 IC 344. *Manapragada Krishna Murthy v Savani Transport (P) Ltd*, AIR 2006 AP 78, the defendant (cashier) misappropriated money, admitted it and made a promissory note in payment, not allowed to get rid of his liability to repay by saying that he was the victim of coercion. *Gangadeep Pratisthan (P) Ltd v Mechano*, (2005) 11 SCC 273: AIR 2005 SC 1958, no coercion found behind a consent decree.

was a true one, there is an end to the plaintiff's case, for a threat to bring such a charge would not be an act forbidden by the Indian Penal Code.”<sup>8</sup>

As the court below recorded no finding as to the truth or falsity of the charge, the case was referred back for re-trial.

The plea was that the plaintiff was dispossessed of promises forcibly under threat that he would be arrested and detained under the Maintenance of Internal Security Act. The court said that such threats would fall within the mischief of Section 15.<sup>9</sup>

### *Detention of property*

An illustration of detention of property is provided by an early case. The plaintiff had pledged his plate with the defendant for £20. When he went to redeem it the pledgee insisted that an additional £10 interest was also owed. The plaintiff paid this to redeem his plate and then sued to recover it back. The court allowed it. He was in immediate need of his article and the defendant extracted from him an extra amount by refusing to deliver it.<sup>10</sup> Refusal by a Government department to release the payment of a contractor unless he gave up his claim for extra rates amounted to coercion under the category of detention of property.<sup>11</sup> A company entered into a contract with a Government company (GAIL), for purchase of gas. The buyer company constructed the pipeline for carriage of gas and was also responsible for its maintenance. Even then GAIL demanded from the company transportation charges. The demand was also found to be against the price structure fixed by the Government. It was held that GAIL was acting dehors the Government pricing order and, being an agency of the Government, it should not have done so. It should not have acted in a commercial and arbitrary manner. GAIL had incurred no cost in transportation.<sup>12</sup>

### **Comparison with English Law**

The following comparison has been attempted by the Madras High Court:<sup>13</sup>

“What the Indian Law calls ‘coercion’ is called in English Law ‘Duress or Menace’. Duress is said to consist in actual or threatened violence or

8. Compulsory sales prescribed by an Act, for example, that the grower will sell all his product only to a particular mill, there is no coercion in it. For a subsequent decision see *Salar Jung Sugar Mills v State of Mysore*, (1972) 1 SCC 23: AIR 1972 SC 87.

9. *Kishan Lal Kalra v NDMC*, AIR 2001 Del 402: (2001) 92 DLT 67.

10. *Astley v Reynolds*, (1731) 2 STR 915: 93 ER 939.

11. *Irrigation Dep'tt v Progressive Engg Co*, (1997) 4 ALD 489 (AP); *U.P. Coop Cane Unions Federations v West U.P. Sugar Mills Assn*, (2004) 5 SCC 430: AIR 2004 SC 3697, fixation of sugar prices in the exercise of statutory power, no coercion.

12. *Essar Steel Ltd v Union of India*, (2006) 1 GLH 609: (2006) 1 Guj LR 436, thus the demand was of coercive nature and was, therefore, set aside. *State of Kerala v M.A. Mathai*, (2007) 10 SCC 195: AIR 2007 SC 1537, a claim of damages under supplemental work, contention that the supplemental agreement was the result of coercion, award of damages without considering the fact of coercion was held to be not proper.

13. *Karuppayee Ammal v Karuppiyah Pillai*, (1987) 2 MLJ 138.

imprisonment of the contracting party or his wife, parent or child, by the other party or by anyone acting with his knowledge and for his advantage. But coercion as defined in Section 15 is much wider and includes the unlawful detention of property also. Further, coercion may be committed by any person, not necessarily a party to the contract. Again, it need not be directed against the contracting party, or his parent, wife or child. It may be directed against any person, even if he is a stranger. While in English Law, duress must be such as will cause immediate violence and also unnerve a person of ordinary firmness of mind, these requisites are not necessary in Indian Law.”

### UNDUE INFLUENCE

#### Definition [S. 16]

**S. 16. “Undue influence” defined.**—(1) A contract is said to be induced by “undue influence” where the relations subsisting between the parties are such that one of the parties is in a position to dominate the will of the other and uses that position to obtain an unfair advantage over the other.

(2) In particular and without prejudice to the generality of the foregoing principle, a person is deemed to be in a position to dominate the will of another—

- (a) where he holds a real or apparent authority over the other or where he stands in a fiduciary relation to the other; or
- (b) where he makes a contract with a person whose mental capacity is temporarily or permanently affected by reason of age, illness, or mental or bodily distress.

(3) Where a person who is in a position to dominate the will of another, enters into a contract with him, and the transaction appears, on the face of it or on evidence adduced, to be unconscionable, the burden of proving that such contract was not induced by undue influence shall lie upon the person in a position to dominate the will of the other.

Nothing in this sub-section shall affect the provision of Section 111 of the Indian Evidence Act, 1872 (1 of 1872).

#### *Illustrations*

- (a) A, having advanced money to his son, B, during his minority, upon B's coming of age obtains, by misuse of parental influence, a bond from B for a greater amount than the sum due in respect of the advance. A employs undue influence.
- (b) A, a man enfeebled by disease or age, is induced, by B's influence over him as his medical attendant, to agree to pay B an unreasonable sum for his professional services. B employs undue influence.
- (c) A, being in debt to B, the moneylender of his village, contracts a fresh loan on terms which appear to be unconscionable. It lies on B to prove that the contract was not induced by undue influence.
- (d) A applies to a banker for a loan at a time when there is stringency in the money market. The banker declines to make the loan except at an unusually high rate of interest. A accepts the loan on these terms. This is a transaction in the ordinary course of business, and the contract is not induced by undue influence.

## Ability to dominate will of other

Sometimes the parties to an agreement are so related to each other that one of them is able to dominate the will of the other. The person who occupies the superior position may prevail upon the other to obtain his consent to an agreement to which he, but for the influence so exerted, would not have consented. The relationship between the parties so as to enable one of them to dominate the will of the other is a *sina qua non* for undue influence to come into play.<sup>14</sup> A spiritual adviser (guru), for example, in a case before the Allahabad High Court,<sup>15</sup> induced the plaintiff, his devotee, to gift to him the whole of his property to secure benefits to his soul in the next world. Such a consent is said to be obtained by undue influence. "Would any reasonable man," the court said, "in full possession of his senses and not under unusual influence of some kind or the other do such a thing?"

## Consent under pressure

In a mediclaim insurance policy, the insured was forced and pressurised to consent to exclusion of cover for cardiac ailments. It was held that the consent being not lawful, it had no binding effect.<sup>16</sup>

## Subtle species of fraud

"Undue influence is said to be a subtle species of fraud whereby mastery is obtained over the mind of the victim, by insidious approaches and seductive artifices. Sometimes the result is brought about by fear, coercion, importunity or other domination, calculated to prevent expression of the victim's true mind. It is a constraint undermining free agency, overcoming the powers of resistance, bringing about a submission of the other."<sup>17</sup> The following statement bears out the distinction between coercion and undue influence:

"The law draws a distinction between duress and undue influence. Duress (coercion) in the execution of a contract or deed occurs when there is a physical compulsion of the person, which must be very rare, or when there is a threat to the person's life or limb, or threat of a physical beating or of imprisonment. It may also take into account threats of a wrongful imprisonment or prosecution of the person and possibly of the person's near relative.

In contrast to duress, undue influence may exist without violence or threats of violence against the victim. It depends upon the existence of a relationship between two parties which, while it continues, causes one to place a confidence in the other which produces a natural influence over the one which that other abuses to his own advantage."<sup>18</sup>

14. *Bellachi v Pakeeran*, (2009) 12 SCC 95; (2009) 4 SCC (Civ) 640.

15. *Mannu Singh v Umadat Pande*, ILR (1888-90) 12 All 523.

16. *Akshoy Kumar Patil v New India Assurance Co*, AIR 2007 Del 136.

17. *Mahboob Khan v Hakim Abdul Rabim*, AIR 1964 Raj 250.

18. *Saxon v Saxon*, (1976) 4 WWR 300, 305, 306 (BC SC).

### Relations which involve domination

When can it be said that one party is able to dominate the will of the other? The answer is, in all cases where there is active trust and confidence between the parties or the parties are not on equal footing.<sup>19</sup> The principle applies to every case where influence is acquired and abused, where confidence is reposed and betrayed. It applies “to all variety of relation in which domination may be exercised by one person over another.”<sup>20</sup> “The relationships which may develop a dominating influence of one over another are infinitely various. There is no precisely defined law setting limits to the equitable jurisdiction of a court to relieve against undue influence. This is a world doctrine, not of neat and tidy rules. The courts of equity have developed a body of learning enabling relief to be granted where the law has to treat the transaction as unimpeachable unless it can be held to have been procured by undue influence. It is the unimpeachability at law of a disadvantageous transaction which is the starting-point from which the court advances to consider whether the transaction is the product merely of one's own folly or of the undue influence exercised by another. A court in the exercise of this equitable jurisdiction is a court of conscience. Definition is a poor instrument when used to determine whether a transaction is or is not unconscionable: this is a question which depends upon the particular facts of the case.”<sup>21</sup> For example, in *Williams v Bayley*:<sup>22</sup>

A son forged his father's signature on several promissory notes and paid them into his banking account. When the truth came to light, the manager of the bank threatened prosecution of the son and “transportation” if a satisfactory solution were not found. To avert this threat, the father agreed to give an equitable mortgage to the bank on his property in return for the promissory notes. Subsequently the father sought to have this agreement cancelled on the ground that he was influenced by the threat.

The House of Lords held the agreement to be voidable. Lord CHELMSFORD expressed the opinion that the negotiation proceeded upon an understanding that the agreement to give security for the promissory notes would relieve the son from the consequences of his criminal act; and the fears of the father were stimulated and operated on to an extent to deprive him of free agency, and to extort an agreement from him for the benefit of the bankers. There

19. The ordinary trade buyers and sellers are on equal footing and not related in fiduciary capacity. See *Devki Nandan v Gokli Bai*, (1886) 90 PLR 325 (P&H).

20. Sir SAMUEL ROMILLY in *Huguenin v Basely*, (1807) 14 Ves 273: 9 RR 283; *Krishnamoorthy v Sivakumar*, (2009) 3 CTC 446, an election candidate cannot be regarded as being in a position to influence the will of voter, nor in that process they are making any agreement. Any such agreement, if at all, would be contrary to law and public policy.

21. Lord SCARMAN in *National Westminster Bank P&C v Morgan*, (1985) 2 WLR 588 (HL).

22. (1866) LR 1 HL 200. It has been observed by the Supreme Court that S. 16 is based on English law of undue influence. *Subhas Chandra Das Mushib v Ganga Prasad Das Mushib*, AIR 1967 SC 878: (1967) 1 SCR 331.

was inequality between the parties and one of them took unfair advantage of the situation of the other and used undue influence to force an agreement from him.

In particular, however, and without prejudice to the generality of the principle, the Act lays down, in sub-section (2) of Section 16 that a person is deemed to be in a position to dominate the will of another in the following cases—

- (a) where he holds a real or apparent authority over the other, or where he stands in fiduciary relation to the other; or
- (b) where he makes a contract with a person whose mental capacity is temporarily or permanently affected by reason of age, illness, or mental or bodily distress.

#### *Real or apparent authority*

A person in authority is definitely able to dominate the will of the person over whom the authority is held. The authority may be real or apparent. Persons in authority would include an Income Tax Officer in relation to an assessee; a magistrate or police officer in relation to an accused person and the like. The expression “apparent authority” would include cases in which a person has no real authority, but is able to approach the other with a show or colour of authority.

#### *Fiduciary relation*

Fiduciary relations are of several kinds. Indeed every relationship of trust and confidence is a fiduciary relation.<sup>23</sup> And confidence is at the base of innumerable transactions of mankind. This category is, therefore, a very wide one. It includes the relationship of solicitor and client,<sup>24</sup> trustee and *cestui que trust*,<sup>25</sup> spiritual adviser and his devotee,<sup>26</sup> doctor and patient,<sup>27</sup> woman and her confidential managing agent,<sup>28</sup> parent or guardian and child,<sup>29</sup> and

23. See *Subhas Chandra Das Mushib v Ganga Prasad Das Mushib*, AIR 1967 SC 878: (1967) 1 SCR 331.

24. *Pushong v Mania Halwani*, 1868 BLR AC 95, where a poor woman agreed to give one-half of the property which she might recover with the assistance of her *Mookhtaar*. See, for example, *Moody v Cox*, (1917) 2 Ch 71, where a solicitor sold a trust property to one of his clients who subsequently sought rescission on the ground that the property was considerably overvalued. The Court of Appeal held that when undue influence is alleged against a solicitor he has to prove that he disclosed all the material facts and that the transaction was of advantage to the client.

25. *Raghunath v Varjivandas*, (1906) 30 Bom 578.

26. *Mannu Singh v Umadat Pande*, ILR (1888–90) 12 All 523.

27. *Mitchell v Homfray*, (1881) LR 8 QBD 587 (CA).

28. *Wajid Khan v Raja Ewaz Ali Khan*, (1890–91) 18 IA 144; *Subbamma v Mohd Abdul Hafiz*, AIR 1950 Hyd 55.

29. *Lakshmi Doss v Roop Laul*, ILR (1906–08) 30 Mad 169; *Suguna v Vinod G. Nehemiah*, (2008) 2 CTC 433, for twenty long years the daughter was taking care of her aged father, the latter settled his property upon her. The court felt that burden of proving that no influence

creditor and debtor.<sup>30</sup> The relationship of trust and confidence presents a very good opportunity to the person in whom confidence is held to exploit it to his own use. A contract between persons so related is, therefore, voidable if the consent was obtained by abusing the confidence. The duty of the person in whom confidence is reposed was explained by the Court of Appeal in *Moody v Cox*.<sup>31</sup> A solicitor sold certain property to one of his clients. The client subsequently alleged that the property was considerably overvalued. SCRUTTON LJ proceeded as follows: "Generally when you have made a legal contract and correctly expressed it in writing, and it has not been obtained by any misstatement of facts, innocent or fraudulent, the contract stands, and the fact that one party or the other knows facts about which he says nothing, which made the contract unprofitable one to the other party, is of no legal consequence. But there are certain relations and certain contracts in which a higher duty is imposed upon the parties and they must not only tell the truth, but they must tell the whole truth so far as it is material, and they must not only not misrepresent by words, they must not misrepresent by silence if they know of something that is material. Some of those cases depend on the relationship between the parties, and, generally speaking, are cases where the relation is such that there is confidence reposed by one party and influence exercised by the other. In that class of relation of parties you may get the duty, first of all, that the party who has influence must make a full disclosure of everything that he knows material to the contract, and, secondly, that the party who has the influence must not make a contract with the party over whom he has influence unless he can satisfy the court that the contract is an advantageous one to the other party."

#### *Mental distress*

The last category of persons whose will is vulnerable to all sorts of influences is that of "persons in mental distress". A person is said to be in distress when his mental capacity is temporarily or permanently affected. It may be due to extreme old age or mental or bodily illness or any other cause. Such a person is easily persuaded to give consent to a contract which may be unfavourable to him. Accordingly, if a contract is made with him by taking advantage of his distress, it is voidable on the ground of undue influence. In a case, for example, before the Madras High Court, a poor Hindu widow, who was in great need of money to establish her right to maintenance, was persuaded by a moneylender to agree to pay 100 per cent rate of interest.<sup>32</sup> This is a clear instance of undue influence being exerted upon a person in distress, and the court reduced the interest to 24 per cent.

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was exerted on the father's mind was upon her. The presumption could not be dethroned and therefore the settlement was liable to be set aside.

30. *Diala Ram v Sarga*, AIR 1927 Lah 536.

31. (1917) 2 CH 71.

32. *Rannee Annapurni Nachiar v Swaminatha Chettiar*, ILR (1909–11) 34 Mad 7.

### *Urgent need of money, no distress*

But mere urgent need of money on the part of the borrower is not, of itself, a sufficient evidence of mental distress. Thus, where a person was facing criminal prosecution at the instance of his father and borrowed on exorbitant terms a sum of money to defend himself, it was held that he was not in such mental distress as would enable a moneylender to dominate his will.<sup>33</sup> Similarly, where a person, fearing the result of the prosecution pending against him, enters into an agreement in favour of the complainant in consideration of his abandoning the prosecution, it cannot be held simply upon these facts that the consent of such person was caused by undue influence.<sup>34</sup>

### *Statutory compulsion, no distress*

A contract made under statutory compulsion cannot be regarded as one made under undue influence. In a case before the Supreme Court, a cane grower had the freedom to offer canes to the factory of his area or not but if he made an offer, the factory was bound under an Act to accept. The court pointed out that in such a case the consent, though compulsory, is not caused by undue influence, fraud, misrepresentation or mistake. The compulsion of law is not coercion. "As a result of economic compulsions and changes in the political outlook, the freedom of contract is now being confined gradually to narrower and narrower limits. Here is a case where one party to contract of sale is compelled to enter into it on rigidly prescribed terms and conditions and has no freedom of bargaining. But, in the eyes of the law, the agreement is freely made."<sup>35</sup> Where the parties voluntarily executed a power purchase agreement pursuant to an order passed by the Electricity Regulatory Commission, avoidance of the agreement on the ground of duress, coercion or undue influence was held to be not sustainable.<sup>36</sup>

### **Burden of proof**

In an action to avoid a contract on the ground of undue influence the plaintiff has to prove two main points. He must show, in the first place, that the other party was in a position to dominate his will, and, secondly, that he actually used his influence to obtain the plaintiff's consent to the contract. The law says that: (1) not only must the defendant have a dominant position, but (2) he must use it.<sup>37</sup> It is not enough, for a person to avoid the contract,

33. *Raghunath Prasad Sahu v Sarju Prasad Sahu*, (1924) 19 LW 470: AIR 1924 PC 60.

34. *Masjidi v Ayisha*, 1880 Punj Rec No. 135, p. 398.

35. *Andhra Sugars Ltd v State of A.P.*, AIR 1968 SC 599: (1968) 1 SCR 705; *U.P. Coop Cane Unions Federations v West U.P. Sugar Mills Assn*, (2004) 5 SCC 430: AIR 2004 SC 3697, compulsory pricing for sale is not undue influence, nor does it affect the character of the transaction as a sale.

36. *Alva Aluminium Ltd v Gabriel India Ltd*, (2011) 1 SCC 167: (2011) 98 AIC 228.

37. Both these requirements must coexist for the reversal of the rule as to burden of proof under this section and S. 111 of the Evidence Act, 1872. *Sundari Devi v Narayan Prasad*, AIR 2011 Pat 89, for proving coercion (S. 15) and undue influence, the defendant in his evidence stated

to show that the other party is his father who could have influenced him. He must go further and show that his father actually did influence him.<sup>38</sup>

### Presumption of undue influence

But in certain cases presumption of undue influence is raised. The effect of the presumption is that once it is shown that the defendant was in a position to dominate the will of the plaintiff it will be presumed that he must have used his position to obtain an unfair advantage. It will be then for the defendant to show that the plaintiff freely consented.<sup>39</sup> For example, in *Lancashire Loans v Black*:<sup>40</sup>

The defendant was a married girl of full age. She gave a security for the loan which her mother took from a company. The only advice she had was from the solicitor of the company.

SCRUTTON LJ held that “in the case of the benefit of contractual advantage obtained from a person coming within certain defined relations, such as the relation of parent and young child, solicitor and client, religious superior

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that signatures were taken on blank papers and the agreement created, but this was not supported by pleadings. Under S. 102 of the Evidence Act, 1872, onus was upon him to prove the facts alleged, but he could not do so, the agreement was enforceable.

38. *Anjadennessa Bibi v Rahim Buksh*, ILR (1915) 42 Cal 286. All the particulars must be given as in the case of fraud. *Subhas Chandra Das Mushib v Ganga Prasad Das Mushib*, AIR 1967 SC 878: (1967) 1 SCR 331; *Alec Lobb (Garages) Ltd v Total Oil Great Britain Ltd*, (1983) 1 WLR 87 (Ch D). Every person occupying a position of influence does not necessarily abuse it. Thus where finance was provided twice over to a garage subject to certain protective clauses but with a genuine concern to help its business, no undue influence was found though a part of the agreement was struck down as unreasonable restraint of trade. *Afsar Sheikh v Soleman Bibi*, (1976) 2 SCC 142: AIR 1976 SC 163, the fact of undue influence must be made out of the particulars pleaded by the plaintiff and not from the written statement. Where an ailing father executed a sale deed in favour of his two sons who were caring for him and the third living apart questioned validity, the court held that though the burden was on those who were favoured, the transaction did not disclose any element of influence or fraud. *Sukhdeo Rai v Champa Devi*, (1986) 34 BLJR 90, gift deed in favour of grandson upheld though executed by the donor only a few days before his death. The court followed the remark in HALSBURY'S LAWS OF ENGLAND, Vol 17 (3rd Edn) 678, to the effect that: “There is no presumption of undue influence in the case of gift to a son, grandson or son-in-law, although made during the donor's illness and a few days before his death.” *Shrimati v Sudhakar R. Bhatkar*, AIR 1998 Bom 122: (1997) 4 Bom CR 237, the mere fact that the person in whose favour a property was gifted by registered deed was the tenant of the owner was held to be not sufficient to shift the burden of proof on the donee. *Kartick Prasad Gorai v Neami Prasad Gorai*, AIR 1998 Cal 278, there was no consideration and the sale deed seemed to be fake, hence presumption and shifting of burden of proof on to the beneficiary of the sale deed. *Savithramma v H. Gurappa Reddy*, AIR 1996 Kant 99, allegation of undue influence, level of proof required is extremely high, it is rated on a par with criminal trial. *Dalbir Singh v Vir Singh*, AIR 2001 P&H 216, sale of land, agreement between an *adatia* and his customer, the former could influence the latter and, therefore, better proof of fairness was expected. *NTPC Ltd v Reshma Constructions, Builders & Contractors*, (2004) 2 SCC 663: AIR 2004 SC 1330: (2004) 1 KLT 1065, conduct of the parties is relevant for arriving at a conclusion with respect to allegations of coercion and undue influence. The case involved full and final settlement.
39. *Krishna Mohan Kul v Pratima Maity*, (2004) 9 SCC 468: AIR 2003 SC 4351, burden on the person standing in fiduciary relationship.
40. (1934) 1 KB 380 (CA).

and inferior, by the related member of that class, it is enough to prove the existence of such a relation to throw on the recipient of the advantage the burden of proving independent advice to the donor and in other respects justifying the transaction." His Lordship then pointed out that a married woman is not necessarily independent of the influence of her mother. Such cases should be dealt with on their own facts, and not on any general presumption. On the facts of the case the court found that she was under the influence of her mother.<sup>41</sup>

Similarly, where a *parda* lady of 70 years, having three daughters, was supposed to have gifted her entire land to the defendant, who was the tenant of that land, it was held that from the position of his possession of the land he must have dominated the woman and burden lay upon him to show the circumstances of the gift. He being not able to do so, the gift deed was set aside.<sup>42</sup>

The presumption is raised at least in the following cases:

#### 1. Unconscionable bargains, inequality of bargaining power or economic duress

##### *Unconscionableness*

Where one of the parties to a contract is in a position to dominate the will of the other and the contract is apparently unconscionable, that is, unfair, the law presumes that consent must have been obtained by undue influence. The burden is shifted to the stronger party to prove that he did nothing to overbear the will of the other. An instructive illustration is the decision of the Privy Council in *Wajid Khan v Raja Ewaz Ali Khan*:<sup>43</sup>

An old and illiterate woman, incapable of any business, conferred on her confidential managing agent, without any valuable consideration, an important pecuniary benefit under the guise of a trust.

Their Lordships said that "all the facts of the case go to show that there was active undue influence. The onus is on the grantee to show conclusively that the transaction is honest, bona fide, well-understood, the subject of independent advice and free from undue influence".

##### *Some instances of unconscionableness*

The presumption of undue influence was raised where a poor Hindu widow, having no means for maintenance, borrowed, in order to establish

41. For a survey of a large number of such cases see *Che Som Binte Yip v Maha P Ltd*, (1989) 2 CLJ 802, 906–911, High Court, Singapore.

42. *Chand Singh v Ram Kaur*, (1987) 2 PLR 70; *Surjit Singh v Bimla Devi*, AIR 2008 NOC 969 (HP), old, illiterate lady was taken by her collateral, in whom she had confidence, to his house and put under "dhoomi" (somekind of smoke treatment), she said that in that state her signatures were taken on two papers that were represented to her as pension papers, on realising that papers were gift deeds, she promptly took action, gift deeds set aside.

43. (1890–91) 18 IA 144.

her right to maintenance, a sum of money at 100 per cent rate of interest;<sup>44</sup> where a person, without having the means of subsistence, in order to prefer an appeal against a judgment, borrowed Rs 3700 on a bond promising to pay Rs 25,000 within a year from recovery of the possession of an estate;<sup>45</sup> where a youth of 18 years of age, spendthrift and a drunkard, borrowed Rs 900 on a bond bearing compound interest at 2 per cent per mensem with monthly rests, the court saying that “the instrument itself bears upon its face the impress of unconscionable dealing, the rate of interest charged being so exorbitant”;<sup>46</sup> where a person of the age of some 28 years, the son of a wealthy man, but of profligate habits and greatly in need of money, his father having refused to supply him, executed a bond to secure a sum of Rs 500 with 37 ½ per cent interest with six-monthly rests, the bond further providing that the sum would not be repayable within three years and even if it was repaid the interest would run for three years.<sup>47</sup> In all these cases the court gave relief by scaling down the rate of interest to what appeared to be reasonable in the circumstances. Gift in favour of a religious organisation by a person weak in mind and suffering in health has been held to be one which carries the apparent impress of undue influence.<sup>48</sup>

#### *Unconscionableness in moneylending transactions*

Unconscionable bargains have been witnessed mostly in moneylending transactions and in gifts. But the principle is not confined to such transactions only. In a case before the Bombay High Court,<sup>49</sup> a poor farmer, being unable to pay back a loan, executed a sale deed in favour of the creditor of his property three times the value of the sum due, the court granted relief by setting aside the sale and allowing the farmer to pay back the lender within a fixed period.

#### *Position of dominance necessary for presumption to arise*

It should, however, be borne in mind that the presumption of undue influence on the ground of unconscionableness of the bargain is raised only when one of the parties is in a position to dominate the will of the other. As between parties on equal footing the mere unconscionableness of the bargain does not create the presumption of undue influence. The mere fact that the bargain is a hard one is no ground in itself for granting relief. This

44. *Rannee Annapurni Nachiar v Swaminatha Chettiar*, ILR (1909–11) 34 Mad 7.

45. *Chunni Kuar v Rup Singh*, ILR (1888–90) 11 All 57.

46. *Kirpa Ram v Sami-ud-din Ahmad Khan*, ILR (1901–03) 25 All 284, STANLEY CJ at p. 285.

47. *Balkishan Das v Madan Lal*, (1907) 29 All 303.

48. *Philip Lukka v Franciscan Assn*, AIR 1987 Ker 204.

49. *Bhimbha v Yeshwantrao*, ILR (1900) 25 Bom 126; *Union of India v M.V. Damodar*, AIR 2005 Bom 137, a loan transaction for purchase of sea going vessels was finalised through the medium of the Shipping Development Fund Committee. It could not be said that there was economic duress because of the monopolistic status of the Fund Committee.

was pointed out by the Privy Council in *Raghunath Prasad Sahu v Sarju Prasad Sahu*.<sup>50</sup>



The defendant and his father were equal owners of a vast joint family property over which they had quarrelled. Consequently the father had instituted criminal proceedings against the son. The defendant, in order to defend himself, mortgaged his properties to the plaintiff and borrowed from him about ten thousand rupees on 24 per cent compound interest. In eleven years this rate of interest had magnified the sum covered by the mortgage more than elevenfold, *viz.*, Rs 1,12,885. The defendant contended that the lender had, by exacting high rate of interest, taken unconscionable advantage of his mental distress and, therefore, there should be presumption of undue influence.

Their Lordships, however, held that there could be no such presumption in the circumstances of the case. Referring to sub-section (3) of Section 16, which provides for presumption of undue influence, Lord SHAW observed as follows: "By this sub-section three matters are dealt with. In the first place, the relations between the parties to each other must be such that one is in a position to dominate the will of the other. Once that position is substantiated the second stage has been reached, *viz.*, the issue whether the contract has been induced by undue influence. Upon the determination of this issue a third point emerges, which is that of the *onus probandi*. The burden of proving that the contract was not induced by the undue influence is to lie upon the person who was in a position to dominate the will of the other. Error is almost sure to arise if the order of these propositions be changed. The unconscionableness of the bargain is not the first thing to be considered. The first thing to be considered is the relations of these parties. Were they such as to put one in a position to dominate the will of the other?"

The borrower failed to prove that the lender was in a position to dominate his will. The only relation between the parties that was proved was simply that they were lender and borrower. The first requirement of Section 16 was, therefore, not fulfilled and, therefore, the borrower got no relief.<sup>51</sup>

### *Unconscionable gifts*

Where a person was suffering from a number of ailments which confined him to a nursing-home and from there he made a deed gifting all his

50. (1924) 19 LW 470: AIR 1924 PC 60. See also *Maria Eudaria Apolonia Gonsalves v Shripad Vishnu Kamat Tarcar*, AIR 1998 Bom 46, agreement for sale of property, immaterial that it was written in Portuguese, seller's son knew that language, no particulars of undue influence alleged, agreement enforceable, the price was found by experts to be reasonable and fair.

51. See also *Rani Sundar Koer v Rai Sham Krishen*, ILR (1906–07) 34 IA 9: (1907) 34 Cal 150. Their Lordships distinguished the case from *Dhanipal Das v Raja Maheshwar Baksh Singh*, (1905–06) 33 IA 118: ILR (1906) 28 All 570 and *Raja Maheshwar Baksh Singh v Shadi Lal*, ILR (1908–09) 36 IA 76: (1909) 31 All 386, on the ground that in these cases the borrower was placed under the Court of Wards and was, therefore, under a peculiar disability. This enabled the lender to dominate his will.

properties to one of his sons to the exclusion of others, the Supreme Court held that the presumption of undue influence was proper.<sup>52</sup> Gifts of this kind are often made under influence. In another case before the Privy Council:<sup>53</sup>

An old Malay widow, wholly illiterate, was the owner of considerable rent-producing landed property. She gifted all her property to her nephew who was helping her, leaving for her an income only of about 30 dollars. The deed of gift was prepared with the help of a lawyer.

On these facts the Lord CHANCELLOR observed: "In the present case their Lordships do not doubt that the lawyer acted in good faith, but he seems to have received a good deal of his information from the respondent (nephew); he was not made aware of the material fact that the property which was being given away constituted practically the whole estate of the donor, and he certainly does not seem to have brought home to her mind the consequences to herself of what she was doing, or the fact that she could more prudently and equally effectively, have benefited the donee without undue risk to herself by retaining the property in her own possession during her life and bestowing it upon him by her will. In their Lordships' view the facts proved by the respondent are not sufficient to rebut the presumption of undue influence which is raised by the relationship proved to have been in existence between the parties; and they regard it as most important from the point of view of the public policy to maintain the rule of law which has been laid down and to insist that a gift made under circumstances which gave rise to the presumption must be set aside unless the donee is able to satisfy the court of the facts sufficient to rebut the presumption."<sup>54</sup>

In another case of benefits without consideration and which was also before the Privy Council,<sup>55</sup> a woman, who was described as a submissive wife and who at the bidding of her husband, gave security of her *stridhan* (personal property), which comprised some land, to secure the growing indebtedness of her husband, Lord GODDARD expressed the opinion that "it is unnecessary to enter into a discussion as to the burden of proof in such a case as this as the evidence here abundantly justifies a presumption that she was acting under the influence of her husband for whose benefit the mortgage was being executed". His Lordship continued: "It would certainly



52. *Lakshmi Amma v Talengalanarayana*, (1970) 3 SCC 159: AIR 1970 SC 1367. In another case of gift of entire property by an old lady to the exclusion of her sons the court said that the age of the donor is definitely one of the most important facts to be taken into account in the totality of the circumstances surrounding the transaction. *M. Karunnakara Kurup v Vaniyarambath Lakshmikutty Amma*, 1984 KLT 83 (SN).
53. *Inche Noriah Binte Mohd Tahir v Sk Allie*, AIR 1929 PC 3; *Hamela v Jang Sher Singh*, AIR 2002 P&H 147, 99 year lease signed by a lady who was old, illiterate and sick, also victim of fraud because nominal consideration, held voidable.
54. *Ramu Mahabir v Ghurbo Samu*, AIR 2006 All 273: 2006 AIHC 3035 (All) vendor, old man of 70 years, living with his nephew who dominated him, transferred his whole property to the nephew to the exclusion of the whole number of his daughters, burden on the nephew to prove *bona fides* and genuineness of consideration in the transaction, burden not discharged.
55. *Tungabai Bhratar Purushottam Shamji Kumbhojkav v Yeshvant Dinkar Jog*, AIR 1945 PC 8.

not be true to say that there is a presumption in every case where a wife confers a benefit on her husband without consideration. Equally it is not necessary in order to establish the presumption that the parties should stand in some particular category of relationship to each other. The presumption no doubt can be more easily established and indeed may be assumed in such cases as transactions between parent and infant child, solicitor and client, or spiritual adviser and penitent, but it will arise in any case in which the facts show that the circumstances are such that influence can fairly be inferred.”

#### *Relationship of blood, marriage or adoption not sine qua non*

Thus, what is necessary to establish the presumption is not that the parties should be related by blood, marriage or adoption, but that their relations are, or position towards each other is, such that one is in a superior position over the other.<sup>56</sup> Even where they are so related, the presumption may not arise for the influence may as well be fairly and wisely exercised. This has been pointed out by the Supreme Court in *Subhas Chandra Das Mushib v Ganga Prasad Das Mushib*:<sup>57</sup>

Some agricultural property was gifted by a person to his only grandson through one of his two sons to the total exclusion of his sons. Although the donor was of great age, he was taking active interest in his property. Four years after the gift he died and still four years after that the other sons questioned the validity of the gift on the ground of undue influence.

The court approved the principles laid down by the Privy Council in *Raghunath Prasad Sahu v Sarju Prasad Sahu*<sup>58</sup> and also noted the fact that Section 16 of the Contract Act is based on the English common law as noted in the judgment of the Supreme Court in *Ladli Prasad Jaiswal v Karnal Distillery Co Ltd*<sup>59</sup> and held that on the facts of the case no presumption of undue influence could arise. “The circumstance that a grandfather made a gift of a portion of his properties to his only grandson (on account of natural love and affection) a few years before his death is not on the face



56. See, for example, *Avon Finance Co v Bridger*, (1985) 2 All ER 281 (CA). An elderly couple, willing to purchase a retirement house, signed certain documents at the bidding of their son which were prepared by the finance company's solicitors and executed at the solicitor's office, the son acting as an agent to procure signature and did so by committing a fraud on his parents, the Court of Appeal unanimously held that the charge should be set aside. Similarly, in

*Kingsworth Trust Ltd v Bell*, (1986) 1 WLR 119, the Court of Appeal set aside the transaction of a mortgage which was executed by a wife upon her property under misrepresentation from her husband whose company had been provided the loan and who was authorised by the lending company to get the documents executed.

57. AIR 1967 SC 878: (1967) 1 SCR 331; *M. Rangasamy v Rengammal*, (2003) 7 SCC 683: AIR 2003 SC 3120, presumption of undue influence only because of near relationship has been held to be not permissible. *Munna Kumari v Umrao Devi*, AIR 2006 Raj 152, gift deed in favour of adopted son influenced by a woman with whom the adoptive father had been living since 35 years. The donor died within a year after the gift. Undue influence, transaction set aside.

58. (1924) 19 LW 470: AIR 1924 PC 60.

59. AIR 1963 SC 1279: (1964) 1 SCR 270.

of it an unconscionable transaction." Where, on the other hand, a person made a very negligible provision for his third wife and the daughters borne by her, and donated the whole of his property only to one of his grandsons, the Supreme Court held that, in the absence of any explanation from the side of the donor for the discrimination, the presumption of undue influence arose.<sup>60</sup>

### *Inequality of bargaining power*

The presumption of undue influence may also arise from the fact that there is such an inequality of bargaining power between the parties that one can cause economic duress to the other. The decision of the Court of Appeal in *Lloyds Bank v Bundy*<sup>61</sup> is a remarkable illustration of the concept of inequality of bargaining power.

60. *Lakshmi Amma v Talengalanarayana*, (1970) 3 SCC 159: AIR 1970 SC 1367. See also *Takri Devi v Rama Dogra*, AIR 1984 HP 11, where the donor was an illiterate lady separated from her husband and the donee was her legal advisor, held, presumption of undue influence. *Marci Celine D'Souza v Renie Fernandez*, AIR 1998 Ker 280, the person executing settlement of property in favour of the defendants was ill and totally dependent on them for existence. The defendants had no other claim to or interest in the property. Held, the document was vitiated by undue influence. *Kennedy Alemas v Executive Engineer*, (1998) 2 Bom CR 320, the doctrine of inequality of bargaining power does not apply where the Government is a party to the contract. A tender for one-year supply system was approved for 3 months' supplies with right to extend up to 12 months. No extension was granted after first extension. No illegality on the part of the Government. The court distinguished the case from *Central Inland Water Transport Corpn v Brojo Nath Ganguly*, (1986) 3 SCC 156: AIR 1986 SC 1571; *Shrilekha Vidyarthi v State of U.P.*, (1991) 1 SCC 212: AIR 1991 SC 537 and *LIC v Consumer Education and Research Centre*, (1995) 5 SCC 482: AIR 1995 SC 1811 where it was observed that the State could not be allowed to enforce a contract which has been entered into with a citizen where there did not exist equality of bargaining power. *Nirmal Chandra Haldar v Sumitra Naskar*, AIR 2007 NOC 1978 (Cal), donor 60 years old, she was under treatment at the house of two of the defendants, though the husband was present, the gift deed was not attested by him. Attestation was by one of the beneficiaries. The burden of proving that the gift deed was executed without fraud or coercion not discharged.

61. (1975) 1 QB 326. See also *Midland Bank Plc v Massey*, (1995) 1 All ER 929 (CA), where the woman borrower for the benefit of another had the independent advice of her solicitors. The bank was entitled to treat the solicitors as respectable solicitors who would take seriously their obligation to give Ms Massey independent advice. It was not for the bank to check up and find out exactly what advice had been given. *Banco Exterior International v Mann*, (1995) 1 All ER 936 (CA), wife mortgaging her joint property with her husband for the husband's loan. The court said that the bank was not required to conduct a meticulous examination of the advice given by the solicitor. Once the bank knows that the wife had received advice from a solicitor, the bank was entitled to think that the solicitor's advice would be such as a reasonably competent professional person would give. *TSB Bank plc v Camfield*, (1995) 1 WLR 430 (CA), the husband misrepresented to induce his wife to charge her property for the husband's loans. She had no advice. The whole transaction was set aside and not merely the extent to which she was told that her estate would be burdened. *Barclays Bank Plc v O'Brien*, (1994) 1 AC 180: (1993) 3 WLR 786 (HL), wife standing surety for the husband's debt without independent advice, held voidable because of undue influence or misrepresentation. *C.I.B.C. Mortgages plc v Pitt*, 1994 AC 200: (1993) 3 WLR 802 (HL), wife told loan needed for buying holiday home, she agreed to give her property in mortgage, money spent by husband on investment in shares, loss, wife allowed to avoid, for the finance company did not take care to see that she had independent advice. *D.N. Jeevaraj v State of Karnataka*, (2016) 2 SCC 653, an influential political person cannot by itself be taken to mean that he will have the ability

A contractor borrowed a sum of money from a bank. He could not pay back in time. The banker pressed for payment or for security. He suggested that his father might mortgage the family's only residential house. The bank officer visited the father and obtained his signatures upon readymade papers. The contractor still could not pay and the banker sought to enforce the mortgage which might have meant throwing out of the family from its only residence. Accordingly Mr Bundy relied upon the unfair character of the mortgage.

He was allowed to set aside the mortgage. Lord DENNING MR tried to locate the principle which runs through all the varied situations in which relief is allowed on account of unequal bargaining power. He said: "English law gives relief to one who, without independent advice, enters into a contract upon terms which are very unfair, or transfers property for a consideration which is grossly inadequate, when his bargaining power is grievously impaired by reason of his own needs or desires, or by his own ignorance or infirmity, coupled with undue influence or pressure brought to bear on him by or for the benefit of the other."

The bank exploited the vulnerability of the father, caused by his desire to help his son, to such an extent that he charged his house to his ruin for a very short moratorium, which was a highly inadequate consideration for the mortgage.

#### *Influence distinguished from persuasion*

"Influence" has to be distinguished for this purpose from persuasion. This distinction was put to work by the Bombay High Court<sup>62</sup> in a case in which the only relationship between the parties was that the defendant was a tenant of a part of the plaintiff's premises. The owner was an illiterate widow, but she had been managing her agricultural property for over two decades. The tenant treated her as his mother and persuaded her to gift to him her entire property. The gift deed, as duly executed by her, was registered. The court felt that it could not be said that the tenant was in a position to dominate her will. The gift deed was not the result of undue influence. The court said:<sup>63</sup> "Influence in the eyes of the law has to be contradistinguished with persuasion. Every persuasion is not the same thing as influence. One may by his acts and conduct convince and persuade the other party to do a particular act and if the other party does such an act freely and out of own volition, may be to his prejudice or disadvantage or peril, it cannot be said that such act was influenced by the other."<sup>64</sup>

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to influence the judgment of the housing land development authority. Possibility of influence must be substantiated with sufficient material and surrounding circumstances.

62. *Shrimati v Sudhakar R. Bhatkar*, AIR 1998 Bom 122; (1997) 4 Bom CR 237.

63. At p. 125.

64. The court distinguished the case from *Shivgangawa Madiwalappa Vulaviv v Basangouda Govindgoura Patil*, AIR 1938 Bom 304. In this case a widow's husband's brother was living with her. They quarrelled and the man threw her out. She recovered the premises with the

*Economic duress by forcing renegotiation of terms*

The House of Lords in their decision in *Universe Tankships Inc v International Transport Workers' Federation*<sup>65</sup> allowed the shipping company to recover back from the Workers' Federation 80,000 US Dollars which were paid under an agreement and which agreement the shipping company had to execute because the workers did not permit the ship to leave without signature. It amounted to economic duress upon the shipowners. The conduct was so catastrophic as to amount to coercion of the shipowner's will which vitiated their consent to those agreements and payments made by them.

The Bombay High Court<sup>66</sup> followed this case so as to hold that where a supplier of raw materials to the ONGC, which was an import substitution, gave a bank guarantee to the ONGC, which was to be enforced only when the customs duty paid by the supplier was refunded to him, and he was subsequently asked to drop this condition and make the guarantee enforceable absolutely and that the condition would be orally observed, it amounted to economic duress and fraud. The court cited Lord DIPLOCK in *Pao On v Lao Yiu Long*<sup>67</sup> as saying that the rationale behind the developing law of economic duress was that the apparent consent of the party aggrieved was induced by pressure exercised upon him by the other party which the law does not regard as legitimate with the consequence that his consent was treated as revocable unless approbated expressly or by implication after the illegitimate pressure had ceased to operate on mind.<sup>68</sup> His Lordship took specific precaution to distinguish the concept of economic duress from mere

help of an influential *Watandar Patil*, who started living with her in immorality. He drove her out after obtaining from her the gift of her property. The court observed that the gift was presumably obtained through undue influence. The court also distinguished *Miti Bewa v Daitari Nayal*, AIR 1982 Ori 174, where the sale deed was executed by an illiterate lady thinking that it was a power of attorney in favour of her son-in-law who was living with her and managing her property. The burden was on the latter to prove that there was no undue influence. Similarly in *Takri Devi v Rama Dogra*, AIR 1984 HP 11, an illiterate lady, living separately from her husband, donated her apple orchard to her lover and the same was held to be the result of undue influence. *Annarpurna Barik Dei v Inda Bewa*, AIR 1995 Ori 273, deed executed by illiterate woman, burden is on the other party to prove that terms were fair and equitable, that she had independent advice and that the document was explained to and understood by her.

65. (1983) 1 AC 366; (1982) 2 WLR 803 (HL). For further study, see, M.H. Ogilvie, *Economic Duress, Inequality of Bargaining Power and Threatened Breach of Contract*, (1980) 26 McGill LJ 289.

66. *Dai-Ichi Karkaria (P) Ltd v Oil and Natural Gas Commission*, AIR 1992 Bom 309. Followed in *B & S Contracts and Designs Ltd v Victor Green Publications Ltd*, 1989 ICR 419 where it was observed that for the purpose of this case it was sufficient to say that if the claimant had been influenced against his will to pay money under the threat of unlawful damage to his economic interest, he would be entitled to claim that money back.

67. 1980 AC 614; (1979) 3 WLR 435.

68. For example, in *North Ocean Shipping Co Ltd v Hyundai Construction Co Ltd*, 1979 QB 705; (1979) 3 WLR 419, the shipbuilders refused to honour the contract unless the stipulated payment was increased by 10 per cent. They made the final payment without protest and thereafter claimed refund. But their conduct was held as amounting to ratification. The pressure on mind had ceased to exist when final bills were under consideration.

commercial pressure which in some degree always exists whenever one party to a commercial transaction is in a stronger bargaining position than the other party. Commercial pressure by itself does not amount to economic duress. In the view of the Privy Council, two elements were necessary to constitute duress, i.e. (1) pressure amounting to compulsion of the will of the victim, and (2) the illegitimacy of the pressure exerted. For all practical purposes the victim of the duress must have no other choice.

In another case on the subject,<sup>69</sup> a national road carrier backed out of the contract already entered into and compelled the other side to renegotiate the terms of the contract. The defendants were heavily dependent on the retail chain's contract and were unable at the time to find an alternative carrier. They agreed to the new terms but later on refused to pay at the new rate. The court observed: "Where a party to a contract was forced by the other party to re-negotiate the terms of the contract to his disadvantage and had no alternative but to accept the new terms offered, his apparent consent to the new terms was vitiated by economic duress."

The court cited the dictum of Lord DENNING in *D.&C. Builders v Rees*:<sup>70</sup>

"No person can insist on a settlement procured by intimidation."

The party had to surrender to the demand of increased charges for carriage because they had to meet their commitment to customs. Accordingly, there was no consideration for the promise to pay increased charges and the same was held to be not enforceable.

Where a government department refused to extend time for completion of the ongoing works unless the contractor agreed to do the same type of further work at the old rates, the court said that it amounted to economic duress.<sup>71</sup>

### *Exploitation of needy*

This approach has been used in some other cases also. One of them is *A. Schroeder Music Publishing Co v Macaulay*:<sup>72</sup>

There was an agreement between a young songwriter and a music publishing company. The arrangement was to remain in force for 5 years and was to be automatically extended for another five years should the boy's royalty reach the figure of £ 5000. The company could terminate the agreement at any time by a month's notice. The boy had no such right and he wanted to get out of it.

The House of Lords ordered his liberation from the bond. The contract was on the terms of company's standard terms and was, therefore, the result of the company's dictation.

69. *Atlas Express Ltd v Kafco (Importers and Distributors) Ltd*, 1989 QB 833: (1989) 3 WLR 389.

70. (1966) 2 QB 617 (CA).

71. *Irrigation Dep'tt v Progressive Engg Co*, (1997) 4 ALD 489 (AP).

72. (1974) 1 WLR 1308.

A similar relief was allowed in a case where a songwriter's copyright was purchased on terms that he was not to publish his songs through any other company but the company had the right to reject his songs.<sup>73</sup> "In determining the respective bargaining positions of the parties, the courts will look at a number of factors, such as age, poverty, illiteracy and emotional state."<sup>74</sup>

With these should be contrasted *National Westminster Bank P&C v Morgan*.<sup>75</sup> A self-employed businessman's joint home with his wife was mortgaged to a building society who were threatening foreclosure. A bank provided him money with which he paid off the society and a new charge on the house was created in favour of the bank for all his present and future liabilities. When his wife was called upon to sign the papers, she was told that it covered only the loan and not business liabilities. The House of Lords were not able to relieve her from the consequences of her signature. The charge had conferred reasonably equal benefit on both parties. The relationship of banker and customer is not automatically characterised as one to which the doctrine of undue influence attaches.

#### *Technique of judicial intervention in unfair bargains*

These developments show that undue influence or duress has become a technique of judicial intervention in unfair bargains.<sup>76</sup> The traditional approach of confining duress to threats to the person and to goods is about to undergo expansion to include other threats, particularly those forms of economic coercion which force a person to enter or vary a contract against his will.<sup>77</sup> Forcing a person to accept less money than is due to him by exploiting his economic stringency is an example of this kind.<sup>78</sup> The principle has been

73. *Clifford Dav Management Ltd v W.E.A. Records Ltd*, (1975) 1 WLR 61 (CA). An illiterate donor transferring all her property to her lawyer, held, unconscionable. *Takri Devi v Rama Dogra*, AIR 1984 HP 11.
74. Nicholas Rafferty, *Recent Developments in the Law of Contract*, (1978) 24 McGill LJ 236, 271.
75. (1985) 2 WLR 588 (HL); noted, *The Limits of Undue Influence*, (1985) 48 Mod LR 579.
76. *Vinayakappa Suryabhanappa Dahlenkar v Dulichand Hariram Murarka*, AIR 1986 Bom 193, consideration for a multistorey commercial complex unnaturally low.
77. For one-time spurt of literature on the subject see, Waddam, *Unconscionability in Contract*, (1976) 39 Mod LR 369; Ogilvie, *Swiss Atlantique Revisited: How Long, O'Lord's How Long?* (1980) 5 Can Bus LJ 100; Dalzell, *Duress by Economic Pressure*, (1942) 20 N Carolina L Rev 237, 341.
78. *D.&C. Builders v Rees*, (1966) 2 QB 617 (CA); Llewellyn, *Bargaining, Duress and Economic Liberty*, (1943) 43 Colum LR 603 and *What Price Contract*, (1931) 40 Yale LJ 704. Beatson, *Duress by Threatened Breach of Contract*, (1976) 92 LQR 496. Sutton, *Duress by Threatened Breach of Contract*, (1974) 20 McGill LJ 554. Adams, *Contract Law at Sea*, (1979) 42 Mod LR 557: (1979) 95 LQR 475; Coote, (1980) Camb LJ 40; Charles Fried, *CONTRACTS AS PROMISES: A THEORY OF CONTRACTUAL OBLIGATIONS*, where it is observed: "Many lawyers have a growing conviction that some degree of paternalistic protection of unsophisticated and unskilful bargains is necessary to avoid results that shock the conscience and this has led to the development of doctrines of unconscionability and a host of *ad hoc* statutory protections that violate the basic principle of freedom of contract"; Melvin Avon Eisenberg, *The Bargain Principle and its Limits*, (1982) 95 Harv LR 741; P.S. Atiyah, *THE RISE AND FALL OF FREEDOM OF CONTRACT*, where it is observed that society should not tolerate the results

applied to grant of licences as a part of the principle of distributive justice. In this case there was a large disparity in the bargaining power of the applicant and the granting authority. The applicant had no choice but to give his consent to the terms and conditions imposed by the authority. In such cases most of the time applicants are expected to sign on dotted lines.<sup>79</sup>

### *Rescuing employees and others from unreasonable terms*

Picking up the meaning of the word “unconscionable” from a dictionary<sup>80</sup> the Supreme Court has noted that it means something that shows no regard for conscience and which is irreconcilable with what is right or reasonable. The matter before the court was a service contract.<sup>81</sup> A clause in the contract empowered the employer (a Government undertaking) to remove an employee by three months’ notice or pay in lieu. The employee, who contested the validity of this clause, was removed by handing him over a three months’ pay packet. The Supreme Court regarded the clause to be constitutionally as well as contractually void. The court added that any term which is so unfair and unreasonable as to shock the conscience of the court would be opposed to public policy and therefore also void under Section 23. The contract was not based upon a real consent. It was rather an imposition upon a needy person.<sup>82</sup> The term was unconstitutional because it was so absolute that any officer could be made a target irrespective of his conduct, good or bad.

Commenting upon this expanding power of the court to relieve a party from the consequences of his own contract, a learned writer says that “freedom of contract turns out to be a misleading guide when so many contracts are not free in the economic sense. The notion of contract as private legislation appears less attractive when legislation is always drawn up one-sidedly. Judges are empowered to read in terms which are not there, or read out terms which are there. They are to impose reasonableness. Whatever is not reasonable is not law. If the parties have agreed to something unreasonable, they should be treated as if they have not agreed at all and released.”<sup>83</sup>

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of unequal starting points for the trading process as the lottery of nature or as the price of civilisation.

79. *Mahavir Singh v State of Haryana*, (2005) 4 ICC 47 (P&H). See further, Lord Steyn, *Common law: Fulfilling the Reasonable Expectations of Honest Men*, (1997) 113 LQR 433.
80. SHORTER OXFORD ENGLISH DICTIONARY, Vol II (3rd Edn) 2288.
81. *Central Inland Water Transport Corpn v Brojo Nath Ganguly*, (1986) 3 SCC 156, 206.
82. The court consulted the following on the subject of unconscionable bargains: CHITTY ON CONTRACTS, Vol I, Para 4 (25th Edn), where contracts by way of imposition are considered; BLACK’S LAW DICTIONARY (5th Edn) 38, for definition of ADHESION CONTRACT; RESTATEMENT OF THE LAW by the American Law Institute, 107, Sec. 28, Vol II for *Unconscionable Contract Terms*; John R. Peden, THE LAW OF UNJUST CONTRACTS, 28–29 (1982); the court noted the influence of the emerging doctrines of distributive justice and unfairness and their impact upon the law of contract at pp. 210–211; as to relationship between unfairness and public policy under S. 23 see the judgment of MADON J at p. 217. Reaffirmed in *DTC v Mazdoor Congress*, 1991 Supp (1) SCC 600: AIR 1991 SC 101.
83. J.H. Baker, *From Sanctity of Contract to Reasonable Expectation*, Current Legal Problems 1979. The law plays in this respect the role of a parent. See Anthony T. Kronman, *Paternalism*

### *Natural justice*

The process of contracting has also been subjected to the requirements of natural justice. The acceptance of a revised price by a low bidder without giving any such opportunity to the highest bidder was held by the Supreme Court to be a denial of natural justice rendering the auction to be void.<sup>84</sup>

## 2. Contracts with pardanashin women

A contract with a *pardanashin* woman is presumed to have been induced by undue influence. She can avoid the contract unless the other party can show that it was her “intelligent and voluntary act”.<sup>85</sup> There is, however, no statutory or judicial definition of the term “*pardanashin* woman”. In the opinion of the Bombay High Court<sup>86</sup> a woman does not become *pardanashin* simply because “she lives in some degree of seclusion”. The concept probably means a woman who is totally “secluded from ordinary social intercourse”. The following observation of the Privy Council explains the concept to a certain extent.<sup>87</sup> “It is abundantly clear that Mrs Hodges was not a *pardanashin*. The term *quasi-pardanashin* seems to have been invented for this occasion. Their Lordships take it to mean a woman, who not being of the *pardanashin class*, is yet so close to them in kinship and habits, and so secluded from ordinary social intercourse, that a like amount of incapacity for business should be ascribed to her, and the same amount of protection which the law gives to *pardanashins* must be extended to her. The contention is a novel one, and their Lordships are not favourably impressed by it. As to a certain well-known and easily ascertained class of women, well-known rules of law are established with the wisdom of which we are not now concerned; outside that class it must depend in each case on the character and position of the individual woman whether those who dealt with her are or are not bound to take special precautions that her action shall be intelligent and voluntary, and to prove that it was so in case of dispute.”

In a case before the Bombay High Court:<sup>88</sup>

It was found that a lady appeared before the Registrar for registration of certain documents, that she stood as a witness in the box in a suit, that

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and the Law of Contracts, (1988) 32 Yale Law Journal 763. A person who would give away too much of his own liberty must be protected from himself, no matter how rational his decision or compelling the circumstances. *Hamela v Jang Sher Singh*, AIR 2002 P&H 147, plaintiff, illiterate, old and sick lady, was taking guidance from the defendant consulting him off and on, the court said that he must be taken to be in a position to influence her. She was told that she was signing a one-year lease but the same was in fact for 99 years, consideration was Rs 2500 per year and even that was not paid to her. The court rescued her by cancelling the document.

84. *Ram & Shyam Co v State of Haryana*, (1985) 3 SCC 267: AIR 1985 SC 1147.

85. *Bellachi v Pakeeran*, (2009) 12 SCC 95: (2009) 4 SCC (Civ) 640, burden of proving genuineness of the document is on the other party. But in the case of registered instruments there is equally the presumption that it was executed in accordance with the law.

86. *Shaik Ismail v Amir Bibi*, (1902) 4 Bom LR 146, 148.

87. *Hodges v Delhi & London Bank Ltd*, (1899–1900) 27 IA 168, 175–76.

88. *Shaik Ismail v Amir Bibi*, (1902) 4 Bom LR 146.

she put in tenants and fixed and recovered rents from them in respect of her house. The court held that she could not be treated as a *pardanashin* lady.

Once it is shown that a contract is made with a *pardanashin* woman, the law presumes undue influence. The burden lies on the other party to show that no undue influence was used, that the contract was fully explained to her and that she freely consented. The following statement of the Privy Council in *Kalibakhsh Singh v Ram Gopal Singh*<sup>89</sup> explains the extent of this onus: "In the first place, the lady was a *pardanashin* lady, and the law throws around her a special cloak of protection. It demands that the burden of proof shall in such a case rest, not with those who attack, but those who found upon the deed, and the proof must go so far as to show affirmatively and conclusively that the deed was not only executed by, but was explained to, and was really understood by, the grantor. In such cases it must also, of course, be established that the deed was not signed under duress, but arose from the free and independent will of the grantor."

In this case:

About two months before her death, a Hindu widow (who was a *pardanashin* woman) gifted half of her landed properties to the son of her paramour, who was also the manager (*mukhtar*) of her estate.

This, it was contended, combined with the fact that she had no independent advice, was sufficient to show that the gift was the result of the influence the *mukhtar* had over the lady. Their Lordships, however, held that there is no rule of law which makes independent advice necessary in every case. "The possession of independent advice, or the absence of it, is a fact to be taken into consideration and will be weighed on a review of the whole of the circumstances relevant to the issue of whether the grantor thoroughly comprehended, and deliberately and of her own free will carried out the transaction. If she did, the issue is solved and the transaction is upheld."<sup>90</sup>

The extent of burden was further explained by the Privy Council in more concrete terms in *Moonshe Buzloor Raheem v Shumsoonisa Begum*.<sup>91</sup> A widow remarried and endorsed and delivered to her new husband certain valuable Government papers. In an action to recover them back from him she proved that she lived in seclusion and that she had given over the papers to him for collection of interest. He contended that he had given her full consideration for the notes. It was held that the mere fact of endorsement and the allegation of consideration were not sufficient to lift the presumption of undue influence. He should prove that the transaction was a bona fide sale and that he gave full consideration for the paper which he received from his wife.

89. (1913-14) 41 IA 23, 28-29.

90. *Kali Bakhsh Singh v Ram Gopal Singh*, (1913-14) 41 IA 23, 31. See also *LIC v Nandarani Dassi*, AIR 1970 Cal 200.

91. 1867 MIA 551 (PC). See further *Kharbuja Kuer v Jangbahadur Rai*, AIR 1963 SC 1203: (1963) 1 SCR 456.

### Rescission [S. 19-A]

Rescission of contract for undue influence is allowed under the provisions of Section 19-A.

**S. 19-A. Power to set aside contract induced by undue influence.**—When consent to an agreement is caused by undue influence, the agreement is a contract voidable at the option of the party whose consent was so caused.

Any such contract may be set aside either absolutely or, if the party who was entitled to avoid it has received any benefit thereunder, upon such terms and conditions as to the Court may seem just.

#### *Illustrations*

(a) A's son has forged B's name to a promissory note. B, under threat of prosecuting A's son obtains bond from A for the amount of the forged note. If B sues on this bond, the Court may set the bond aside.

(b) A, a moneylender advances Rs 100 to B, an agriculturist and, by undue influence, induces B to execute a bond for Rs 200 with interest at 6 per cent per month. The Court may set the bond aside, ordering B to repay Rs 100 with such interest as may seem just.

[For comments see notes on Sections 19 to 19-A under the heading "Limits of Rescission", *infra*.]

## MISREPRESENTATION [S. 18]

### Definition

A contract the consent to which is induced by misrepresentation is voidable at the option of the deceived party. Misrepresentation means misstatement of a fact material to the contract. Misrepresentation is defined in Section 18:

**S. 18. "Misrepresentation" defined.**—"Misrepresentation" means and includes—

(1) the positive assertion, in a manner not warranted by the information of the person making it, of that which is not true, though he believes it to be true;

(2) any breach of duty which, without an intent to deceive, gains an advantage to the person committing it, or any one claiming under him, by misleading another to his prejudice, or to the prejudice of any one claiming under him;

(3) causing, however innocently, a party to an agreement, to make a mistake as to the substance of the thing which is the subject of the agreement.

The section includes the following types of misrepresentation:

#### 1. Unwarranted statements

When a person positively asserts that a fact is true when his information does not warrant it to be so, though he believes it to be true, this is misrepresentation.<sup>92</sup> In a Bombay case<sup>93</sup> for example:

92. See illustrations (a) and (c) to S. 19.

93. *Oceanic Steam Navigation Co v Soonderdas Dharamsey*, ILR (1890) 14 Bom 241.

The defendants chartered a ship from the plaintiffs, who stated that the ship was certainly not more than 2800 tonnage register. As a matter of fact the ship had never been in Bombay and was wholly unknown to the plaintiffs. She turned out to be of the registered tonnage of more than 3000 tonnes.

It was held that the defendants were entitled to avoid the charterparty. "There was the positive assertion by the plaintiffs about the size of the ship—an assertion not warranted by any information the plaintiff had at the time, and which was not true."<sup>94</sup>

A statement is said to be warranted by the information of the person making it when he receives the information from a trustworthy source. It should not be a mere hearsay. In a Calcutta case:<sup>95</sup>

*B* told the plaintiff that one *C* would be the director of a company. *B* had obtained this information not from *C* direct, but from another person, called *L*. The information proved untrue.

The judge said: "I am not inclined to think that if *B* relied on second-hand information he derived from *L*, he was warranted in making the positive assertion that *C* would be a director."

Where a representation acquires the status of being a term of the contract, and it turns out to be untrue, the disadvantaged party may, not only avoid the contract but also sue for damages for breach. Where in the course of negotiations for the sale of lamb, the seller stated that the whole of the lot was fully serviced, whereas this was not so, the buyer was allowed damages for the breach of the warranty.<sup>96</sup> In another case<sup>97</sup> the plaintiff was orally assured that his containers would be carried under the deck, but by mistake they were loaded on deck and were lost. The defendant was not allowed to claim the protection of a clause in the contract limiting his liability only to wilful misconduct. The oral assurance had overridden the written clauses.

A land was purchased expressly for the construction of a duplex. The seller represented that he saw no difficulty in any such use of the land. But a permission to build such a complex was refused unless a sewage costing some 3000 dollars was provided. Though the misrepresentation was

94. PARSONS J at p. 248. Contrast this with *Howard Marine & Dredging Co Ltd v Ogden & Sons (Excavations) Ltd*, 1978 QB 574: (1978) 2 WLR 515 (CA), where the sellers of the barges were convinced about their dead weight capacity having seen it in the Lloyd's register and, therefore, they were not held guilty of misrepresentation though Lloyd entries were found to be wrong.

95. *Mohanlal v Sri Gungaji Cotton Mills Co*, (1899–90) 4 CWN 369.

96. *Richview Construction Co v Raspa*, (1975) 11 Ont CA (2d) 377. See also *Birch v Paramount Estates Ltd*, (1956) 167 EG 396 (CA), oral warranty that the house would be of the same standard of workmanship as the company's show house. The buyer was allowed compensation for inferior paintwork which deteriorated faster. The court said that "the very purpose of having a show house was that a prospective purchaser might be attracted by what he saw and might have the opportunity of knowing what he was to get".

97. *J. Evans & Son (Portsmouth) Ltd v Andrea Merzario Ltd*, (1976) 1 WLR 1078.

innocent, the buyer was allowed to avoid the sale.<sup>98</sup> Where an advertisement in a local newspaper said the land to be 9000/5600 square feet, and that it had a “beautiful reflective pool”, but it turned out that the property was not beautiful and that the reflective pool showed a massive crack and water seepage, the buyer was not allowed to rescind the option to purchase. The court said that the statement in the advertisement had not become incorporated as an implied term of the option to buy and the plaintiffs had seen the reflective pool before they made the offer to purchase.<sup>99</sup>

Where the seller of a car stated that the car had done only 20,000 miles, the representation being untrue, the buyer was allowed to recover compensation for the misrepresentation.<sup>100</sup>

## 2. Breach of duty

Any breach of duty which brings an advantage to the person committing it by misleading the other to his prejudice is a misrepresentation. “This clause is probably intended to meet all those cases which are called in the court of equity—cases of ‘constructive fraud’,<sup>101</sup> in which there is no intention to deceive, but where the circumstances are such as to make the party who derives a benefit from the transaction equally answerable in effect as if he had been actuated by motives of fraud or deceit”.<sup>102</sup> In that case, for example:

The plaintiff, having no time to read the contents of a deed, signed it as he was given the impression by the defendant that it contained nothing but formal matters already settled between them. The deed, however, contained a release in favour of the defendants.

Accordingly, the plaintiff was allowed to set aside the deed. “The defendant,” the court said, “was under no obligation, legally or morally, to communicate the contents of the deed. But the plaintiff placed confidence. It

98. *Alessio v Jovica*, (1973) 42 DLR (3d) 242, Canada.

99. *Chuan Bee Realty Pte Ltd v Teo Chee Yeow*, (1996) 2 SLR 758. See Luh Luh Lan, *An Overview of the Advertising Laws and Regulations in Singapore*, 2001 JBL 399.

100. *Dick Bentley Productions Ltd v Harold Smith (Motors) Ltd*, (1965) 1 WLR 623.

101. It was observed in *Dynamics Corp of America v Citizens and Southern National Bank*, 356 Fed Supp 991 that fraud had a broader meaning in equity than at law and an intention to defraud or to misrepresent was not a necessary element. “Fraud, indeed, in the sense of a court of equity includes all acts, omissions and concealments which involve a breach of legal or equitable duty, trust or confidence justly reposed and are injurious to another or by which an undue or unconscientious advantage is taken of another.” Applying this to the facts of a case before it, *Dai-Ichi Karkaria P Ltd v Oil and Natural Gas Commission*, AIR 1992 Bom 309, the Bombay High Court held that to force a person, at the pain of stopping business with him, to change the conditions attached to the encashment of his bank guarantee was a fraud on him. *Oil and Natural Gas Commission v Dai-ichi Karkaria (P) Ltd*, 1994 Mah LJ 1084, no fraud or coercion could be proved, encashment of bank guarantee not stayed.

102. *Oriental Bank Corporation v John Fleming*, ILR (1879) 3 Bom 242, per SARGENT LJ at p. 287.

then became his duty to state fully without concealment, all that was essential to a knowledge of the contents of a document.”<sup>103</sup>

A female patient was told that her sterilisation would be irreversible, but was not told that there was the minute risk (less than 1 per cent) of failure and of pregnancy. She conceived again, delivered a child and sued the gynaecologist for his breach of contract. The representation that the operation was “irreversible” was held as not amounting to an express guarantee that the operation was bound to achieve its acknowledged object of sterilising the plaintiff. The representation meant no more than this that the operative procedure in question was incapable of being reversed. The court would be slow to imply a term that the expected result would actually be achieved.<sup>104</sup> Where, on the other hand, a husband undergoing vasectomy operation was not warned that there was a slight risk of his wife becoming pregnant, the surgeon was held responsible to the man and his wife for the pains of unwanted pregnancy. The court said that the plaintiffs were entitled to damages for distress, pain and suffering, since the personal distress of both plaintiffs and the pain and suffering of the birth was a separate head of claim which was not cancelled out by the relief and joy felt after the birth of a healthy baby and there was no reason in principle why damages could not be recovered for the discomfort and pain of a normal pregnancy and delivery.<sup>105</sup>

Persons of full age and understanding who subscribe their signature to a document cannot be heard to say that they had affixed the signatures on blank papers or that they signed without appraising themselves about the recitals. Persons so imprudent as that have to take the consequences of such imprudence.<sup>106</sup>

### 3. Inducing mistake about subject-matter

Causing, however innocently, a party to an agreement to make a mistake as to the substance of the thing which is the subject of the agreement is also misrepresentation. [S. 18(3)]

103. Ibid. *Khandu Charan Polley v Chanchala Bhuiyia*, AIR 2003 Cal 213, the illiterate lady signed a document which she was given to believe by trusted agents was creating a licence but was in fact a settlement. This amounted to breach of duty. She had the right to cancel the licence.

104. *Eyre v Measday*, (1986) 1 All ER 488 (CA), distinguishing *Thake v Maurice*, (1985) 2 WLR 215, where the husband became fertile after vasectomy operation and his wife conceived and on the facts the doctor was held liable. *State of Punjab v Shiv Ram*, (2005) 7 SCC 1: AIR 2005 SC 3280, pregnancy despite operation of sterilization, compensation could be awarded only if the failure of operation was attributable to doctor's negligence, not when failure was due to natural causes, no compensation for upbringing if the couple opted for bearing the child.

105. *Thake v Maurice*, 1986 QB 644 (CA). See further *Parkinson v St James and Seacroft University Hospital NHS Trust*, 2002 QB 266: (2001) 3 WLR 376 (CA), liability for failed sterility operation, disabled and deformed child attributable to negligence.

106. *Chokkamal v K. Balraj*, (2008) 5 CTC 690.

The subject-matter of every agreement is supposed by the parties to possess certain value or quality. If one of the parties leads the other, however innocently, to make a mistake as to the nature or quality of the subject-matter, there is misrepresentation. For example, in a Bombay case:<sup>107</sup>

The directors of a company, while acting within their authority, sold on the company's behalf a bill of exchange to a bank. The company denied liability on the bill.

But the bank was held entitled to recover the amount of the bill from the company as money received to the use of the bank. "The bill was different from what it was expressly represented to be by the agents of the company."

The Government auctioned certain forest coupes. A part of the land was occupied by tenants. The Forest Department knew this fact but did not disclose it to the purchaser. The contract was held to be vitiated by misrepresentation. The purchaser was allowed to recover damages for loss.<sup>108</sup>

A second-hand car dealer attached a disclaimer to the car under sale stating that the mileage reading was incorrect. The dealer knew the true mileage of the car but did not disclose it. It was held that the dealer was bound to disclose the real position because he knew it and also knew that the odometer materially understated the mileage. The court said that although, in the ordinary way, dealers were under no positive duty to disclose the defects and disadvantages of their wares, they were required to volunteer the truth, in so far as they knew it with regard to the inaccurate mileage reading. The disclaimer seriously understated the fact. The defendants knew not only that the reading was incorrect but that it was grossly and potentially misleadingly so.<sup>109</sup>

### Suppression of vital facts

Misrepresentation may also arise from suppression of vital facts. Cases of concealment or suppression will fall either under sub-section (2), when it amounts to a breach of duty or under sub-section (3) when it leads the other party to make a mistake about the subject-matter of the agreement. For example, in *R. v Kylsant*,<sup>110</sup> the prospectus of a company stated that the company had regularly paid dividends, which created the impression that the company was making profits, whereas the truth was that the company had been running into losses for the last several years and dividends could only be paid out of wartime accumulated profits. The suppression of this fact was held to be a misrepresentation. Similarly, where in the negotiations for a marriage contract, those speaking for the girl failed to disclose that she

107. *Nursey Spg & Wvg Co Ltd, re*, ILR (1880) 5 Bom 92.

108. *Dambarudhar Behera v State of Orissa*, AIR 1980 Ori 188.

109. *Farrand v Lazarus*, (2002) 3 All ER 175 (QBD).

110. (1932) 1 KB 442.

was suffering from epileptic fits, the engagement was held to be voidable, a very material fact having been suppressed.<sup>111</sup>

The fact that the girl was married before and was a widow at the time of remarriage was held to be a vital fact. Its non-disclosure enabled the husband to get a decree of nullity.<sup>112</sup>

### Of material facts

Misrepresentation should be of facts material to the contract. Mere "commendatory expression" such as men of business will habitually make about their goods are not sufficient to avoid the contract. In a sale of land, for example, "a mere general statement that the land is fertile and improvable, whereas parts of it had been abandoned as useless, cannot, except in extreme cases, as, for instance, where a considerable part is covered with water, or otherwise irreclaimable, be considered such a misrepresentation as to entitle a purchaser to be discharged."<sup>113</sup> But, when, in the sale of a hotel, the tenant was described "as a most desirable tenant", whereas his rent was in arrears, this was held to be a material misrepresentation.<sup>114</sup>

In the matters of matrimony it has been held that qualifications of the spouse are a material fact. Where the girl was in possession of high academic qualifications and agreed to matrimony because she was told that her match was in an attractive job whereas he was only an apprentice in a factory, the court ruled that it was a misrepresentation and, therefore, annulment of the marriage would have to be decreed.<sup>115</sup> Where the fact suppressed was that the girl was incapable of child bearing because of operation for excision of fallopian tube, this was held to be a material misrepresentation enabling the court to pass a decree of nullity.<sup>116</sup>

A fact is said to be material if it would affect the judgment of a reasonable person in deciding whether to enter into the contract and, if so, on what

111. *Haji Ahmad Yarkhan v Abdul Gani Khan*, AIR 1937 Nag 270. A 56-year-old man got himself insured and died within 2 years of heart attack. LIC refused to pay on the ground that he suffered from diabetes and carbuncle, but did not disclose. The family doctor produced by LIC could not give any information about the family. Held, fraud was not proved. Insurance of a man of that age carries its own risks and LIC had accepted it with eyes wide open. *Kamla Wanti v LIC*, AIR 1981 All 366. A person authorising an agent to sell but prohibiting him from making any representation and excluding his liability if the agent makes any, protects him from liability, *Excluding Liability for Misrepresentation*, (1981) 97 LQR 522, considering *Overbrooke Estates Ltd v Glencombe Properties Ltd*, (1974) 1 WLR 1335.

112. *Asha Qureshi v Asfaq Qureshi*, AIR 2002 MP 263.

113. *Dimmock v Hallett*, (1866) LR 2 Ch App 21, per TURNER LJ at p. 27. See further, *Amina v Hasan Koya*, 1985 KLT 596; 1985 Cri LJ 1996; where the fact that the girl was running pregnancy was concealed from the would be groom and it was held that no fact could be more material than this, for it would possibly have deterred the groom from going ahead and when he avoided the marriage, it became nullity *ab initio*, as if it never existed.

114. *Smith v Land & House Property Corp*n, (1884) LR 28 Ch D 7 (CA).

115. *Bindu Sharma v Ram Prakash Sharma*, AIR 1997 All 429; *Anurag Anand v Sunita Anand*, AIR 1997 Del 94, monthly income and property status of groom misrepresented, annulment of marriage.

116. *Benjamin Dominc Cardoza v Gladys Benjamin Cardoza*, (1997) 3 Bom CR 553.

terms. Misrepresentation of the age of a car, showing it to be five years younger, was held to be material because it affected the price which a willing purchaser would have liked to pay for it. But putting forth exaggerated measurement of land by 2.3 per cent was held to be not material.<sup>117</sup>

Peptic ulcer is a common disease which appears and which gets cured on proper treatment. This is not a serious disease which may result in death and it is only in cases where proper care is not taken, it may prove fatal. Therefore, non-disclosure by the assured deceased that at a particular point of time, he was suffering from peptic ulcer did not amount to deliberate suppression of material fact so as to enable the insurance company to repudiate the contract.<sup>118</sup>

### Expression of opinion

A mere expression of opinion cannot be regarded as a misrepresentation of facts even if the opinion turns out to be wrong. But in some cases, a statement of opinion may also amount to misrepresentation. One such situation was stated by BOWEN LJ in *Smith v Land & House Property Corp*n<sup>119</sup> "It is often fallaciously assumed that a statement of opinion cannot involve a statement of fact. In a case where the facts are equally well-known to both parties, what one of them says to the other is frequently nothing but an expression of opinion. But if the facts are not equally well-known to both sides, then a statement of opinion by one who knows the facts best involves very often a statement of a material fact, for he impliedly states that he knows facts which justify his opinion."

This statement was affirmed by the Privy Council in *Bisset v Wilkinson*.<sup>120</sup>

Certain lands were sold. The seller was aware that the land was required for sheep-farming and, therefore, expressed the opinion that "the land had a carrying capacity of 2000 sheep". The land turned out to be unsuitable for sheep-farming and the purchaser refused to pay the price.

Their Lordships found no ground for enabling the buyers to avoid the agreement. Lord MERRIVALE felt that where relief is sought on the basis of misrepresentation, it is necessary that there should be representation of a specific fact. A representation of fact may be inherent in a statement of opinion. But it depends upon the material facts of the transaction, the knowledge of the parties respectively and their relative positions, etc. The most material fact in the case was that both parties were aware that the vendor had not and no other person had carried on sheep-farming in that unit of land. "In these circumstances the purchasers were not justified in regarding anything

117. *Baker v Asia Motor Co Ltd*, 1962 MLJ 425.

118. *LIC v Beni Bai*, (1998) 2 BC 157 (MP) (DB).

119. (1884) LR 28 Ch D 7 (CA).

120. 1927 AC 177 (PC). *Rajshree Sugars & Chemical Ltd v Axis Bank Ltd*, (2009) 1 CTC 227 (Mad), representation made by the bank that the US Dollar would never reach the stipulated level of exchange rate against the Swiss Franc was held to be not the statement of a fact because both parties knew how currency behaves and no body has any control on it.

said by the vendor as to the carrying capacity as being anything more than an expression of opinion on the subject.”

Where a claim was made through an advertisement that the defendants were the “top flight cabaret performers in Europe”, the court said that it was a statement of opinion. The hotel which engaged them on the basis of the claim could not terminate the contract on the ground of misrepresentation.<sup>121</sup> An advertisement for sale of residential property claimed that foreigners were eligible to purchase it. This was held to be the statement of an existing fact.<sup>122</sup> “There is a difference between an indiscriminate praise and specific promises or assertion of verifiable facts.”<sup>123</sup>

### Representation of state of mind

A representation of one’s state of mind is also a representation of fact. In *Edgington v Fitzmaurice*,<sup>124</sup> the prospectus of a company misstated the purpose to which the money to be borrowed by issuing debentures was going to be applied. The directors contended that the representation related to the state of their mind as to what use the money was going to be put and they could change their mind and, therefore, it was not a misrepresentation of a specific fact. The Court of Appeal, however, pointed out that the state of a man’s mind is as much a fact as the state of his digestion. A misrepresentation as to the state of a man’s mind is, therefore, a misstatement of fact.

The intention of the parties is very important in the matter of contracting. “The intention of the parties governs in the making and in the construction of all contracts. If the parties so intend, the sale may be absolute, with a warranty superadded or the sale may be conditional, to be null and void if the warranty is broken.”<sup>125</sup>

### Change of circumstances

A petroleum company acquired a site on a main road for constructing a petrol pump estimating its annual consumption to be 2,00,000 gallons from the third year of operation. The planning authority, however, permitted the pump to be erected only at the back side of the site which was accessible only from the side streets and not at all visible from the busy main road and this considerably affected the sale potential. But even so they failed to

121. *Hotel de L'Europe Ltd v Curgie-Freyer*, (1956) 3 MC 89 (Singapore CA). The hotel was able to prove that the defendants had given only one performance previously at a private party.

122. *Teb Pek Cheong v Wong Soon Kwong*, Singapore HC (unreported). See 2001 JBL 403.

123. Treitel GH, *LAW OF CONTRACT*, (9th Edn, 1995).

124. (1885) 29 Ch D 459, 476 (Ch).

125. ERLE CJ in *Bannerman v White*, (1861) 10 CBNS 844, the buyer of hops particularly asked the seller whether sulphur had been used in growth or treatment of the crop and he was told that no sulphur had been used. After delivery the buyer found that sulphur had been used in the cultivation of a portion of the hops only but the whole crop had become inseparably mixed up. The buyer was allowed to reject all the hops. The court said that the intention of the parties appeared to be that the contract should be null if sulphur had been used.

point this out to the lessee of the pump who in consequence invested money on the basis of the originally intimated estimates and suffered loss. They were held liable for the plaintiff's loss. The court laid down that where during the course of precontractual negotiations, one party, who had special knowledge and expertise concerning the subject-matter of the negotiations, made a forecast with the intention of inducing the other party to enter into a contract, and the other party did so, the court can construe that the forecast was not merely an expression of opinion but as constituting a warranty and accordingly they were liable for the breach of the warranty. Every person who offers an advice, information or opinion of this kind is under a duty of reasonable care to see that it is true, and this duty was not limited to persons carrying on the profession or business of giving advice.<sup>126</sup>

There is often a gap of time between the representation of a fact and the ultimate conclusion of the contract. Any change of circumstances in the meantime affecting the fact represented must be brought to the knowledge of the other party. This was pointed out by the Court of Appeal in *With v O'Flanagan*.<sup>127</sup>

In the negotiations for the sale of his medical practice, the defendant represented that his practice had brought in £2000 per annum for the preceding three years and that he had a specified number of patients on his panel. Negotiations resulted in a contract in about five months. During this time the defendant became ill and could not attend to his practice. This resulted in a serious loss of practice, but the purchaser could learn about it only after the completion of the sale. It was held that the plaintiff was entitled to rescind the contract. The court emphasised that the change of circumstances should have been brought to the notice of the purchaser.<sup>128</sup>

### Inducement

It is further necessary that misrepresentation must be the cause of the consent, in the sense that but for the misrepresentation the consent would not have been given.<sup>129</sup> The explanation to Section 19 provides:

126. *Esso Petroleum Co Ltd v Mardon*, 1976 QB 801 (CA).

127. 1936 Ch 575 (CA).

128. Lord WRIGHT relied upon *Davies v London & Provincial Marine Insurance Co*, (1878) LR 8 Ch D 469.

129. See *Hims Enterprises v Ishak Bin Subari*, (1992) 1 CLJ 132 (HC), Johor Bahru, where the agreement between the parties was made on terms with which the plaintiffs were familiar, as they were terms previously used by the plaintiffs in their earlier contracts, that being so, the terms contained no surprise for the plaintiffs and hence no culpable misrepresentation. *County Nat West Ltd v Barton*, (2002) 4 All ER 494 (CA) (Note), the appeal considered issues concerning the rebuttable presumption that arises from the making of a fraudulent representation, namely, that if a false statement is of such a nature that it would be likely to play a part in the decision of a reasonable person, it will be presumed to have done so unless the representor satisfies the court to the contrary.

A fraud or misrepresentation which did not cause the consent to a contract of the party of whom such fraud was practised, or to whom such misrepresentation was made, does not render a contract voidable.

If the plaintiff would have consented in any case, he can hardly complain. Again the representation must be made with the intention that it shall be acted upon by the other party. The plaintiff must have been affected by the false representation. There would be no misrepresentation, even if the advertisement was false, if the buyer had inspected the goods before buying them unless he was the victim of some concealed defect which could not be known by external examination.<sup>130</sup> If a person to whom the statement was not addressed voluntarily chooses to act upon it, he is not entitled to rescission.<sup>131</sup>

### Means of discovering truth

A party cannot complain of misrepresentation if "he had the means of discovering the truth with ordinary diligence."<sup>132</sup> This is recognised by way of an exception stated along with Section 19. The statement is as follows:

If such consent was caused by misrepresentation or by silence, fraudulent within the meaning of Section 17, the contract, nevertheless, is not voidable, if the party whose consent was so caused had the means of discovering the truth with ordinary diligence.

A person who bought a quantity of rice, was precluded from alleging misrepresentation about its quality because he lived very near the place where the goods were lying and, therefore, might have discovered the truth with ordinary diligence.<sup>133</sup> But where the truth cannot be discovered with ordinary diligence, the party guilty of misrepresentation cannot rely on the defence. Thus, for example, in a case<sup>134</sup> the director of a company falsely told a bank that the bill they were selling to the bank was one on which the company was liable, it was held that "no ordinary diligence would have enabled the bank to discover that the company was not liable on the bill."<sup>135</sup>

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130. *Chuan Bee Realty Pte Ltd v Teo Chee Yeow*, (1996) 2 SLR 758.

131. *Peek v Gurney*, (1873) LR 6 HL 377.

132. See *Balraj Chibber v NOIDA*, 1995 All LJ 1513: (1996) 27 ALR 10, allotment of plots to members of a society, allotment to some of the allottees was cancelled on the ground that they misrepresented to be members, the cancellation was set aside because they proved their membership in fact; even otherwise the truth of their membership could have been easily discovered. *Nasiran Bibi v Mohd Hasan*, (1996) All LJ 1648, a person who himself appeared before the Registrar to receive a part of the consideration and acknowledged receipt of notice of execution of sale deed, not allowed to say that he was the victim of fraud or misrepresentation.

133. *Shoshi Mohun Pal Chowdhry v Nobo Krishto Poddar*, ILR (1874) 5 Cal 801. See *Misrepresentation, Warranty and Estoppel*, 9 Aust LJ 347.

134. *Nursey Spg & Wwg Co Ltd, re*, ILR (1880) 5 Bom 92.

135. *Ibid. U.P. State Sugar Corp v Karamchari Assn v State of U.P.*, 1995 All LJ 937, a person entering into a contract with a company which is under industrial sickness proceedings, and if he did so because he was kept in the dark, he is entitled to be relieved of the bargain and, if he did so with full knowledge, no relief can be granted to him because he was not induced

A difficult question about this exception is that where a person has the means of discovering the truth, but does not use them and contracts in reliance upon the statements made to him, whether the contract would be voidable? In such cases the principle seems to be that if he relies upon those means he cannot afterwards complain of the misrepresentation. But if he does not use the means and relies upon the statements made to him, he can avoid. This was laid down by the Court of Appeal in *Redgrave v Hurd*.<sup>136</sup> Here also a medical practice was under sale. The seller misrepresented the income which it produced, but gave documents to the purchaser from which he could have verified, but he did not do so and having only cursorily looked at them, purchased the business. On learning the truth he sought to avoid the contract and was allowed to do so. Sir GEORGE JESSEL MR remarked: "If a man is induced to enter into a contract by false representation, it is not sufficient answer to him to say: 'If you had used due diligence, you would have found out that the report was untrue. You had the means afforded you of discovering its falsity, which you did not choose to avail yourself of.' One of the most familiar instances in modern times is this. Men issue a prospectus containing false statements, and then say the contracts themselves may be inspected at the office of the solicitors. It has always been held that those who accept those false statements as true are not deprived of their remedy merely because they neglected to go and look at the contracts themselves. Another instance with which we are familiar is a false statement as to the contents of a lease; in such a case as a man saying that there was no covenant or provision in the lease to prevent the carrying on, in the house to be sold, the trade which the purchaser was known by the vendor to be desirous of carrying on therein. Although the lease itself might be produced at the sale or might have been open to the inspection of the purchaser, it was held that the vendor could not be allowed to say: 'You are not entitled to give credit to my statement.' It is not sufficient, therefore, to say that a man has had the opportunity of investigating the real state of the case, but has not availed himself of that opportunity."

## FRAUD

### Definition

Intentional misrepresentation of facts, speaking broadly is called "fraud". According to Section 17:

**S. 17. "Fraud" defined.**— "Fraud" means and includes any of the following acts committed by a party to a contract, or with his connivance, or by his agent,

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by fraud or misrepresentation. *Oriental Insurance Co Ltd v Gowramma*, AIR 1994 Kant 29, motor vehicle insurance policy issued after due verification about the ownership of the vehicle. After accident, the company was not allowed to take the plea that the policy was obtained by misrepresentation and that the claimant was not the owner of the vehicle.

136. (1881) LR 20 Ch D 1.

with intent to deceive another party thereto or his agent, or to induce him to enter into the contract—

- (1) the suggestion, as a fact, of that which is not true, by one who does not believe it to be true;
- (2) the active concealment of a fact by one having knowledge or belief of the fact;
- (3) a promise made without any intention of performing it;
- (4) any other act fitted to deceive;
- (5) any such act or omission as the law specially declares to be fraudulent.

*Explanation.*—Mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud, unless the circumstances of the case are such that, regard being had to them, it is the duty of the person keeping silence to speak, or unless his silence is, in itself, equivalent to speech.

*Illustrations*

- (a) A sells, by auction, to B, a horse which A knows to be unsound. A says nothing to B about the horse's unsoundness. This is not fraud in A.
- (b) B is A's daughter, and has just come of age. Here, the relation between the parties would make it A's duty to tell B if the horse is unsound.
- (c) B says to A—"If you do not deny it, I shall assume that the horse is sound". A says nothing. Here A's silence is equivalent to speech.
- (d) A and B, being traders, enter upon a contract. A has private information of a change in prices which would affect B's willingness to proceed with the contract. A is not bound to inform B.

### Assertion of facts without belief in truth

In English law "fraud" was defined in the well-known decision of the House of Lords in *Derry v Peek*.<sup>137</sup> Lord HERSCHELL said:

"Fraud is proved when it is shown that a false representation has been made,—

- (1) knowingly, or
- (2) without belief in its truth, or
- (3) recklessly careless whether it be true or false."

In this case:

A company's prospectus contained a representation that the company had been authorised by a special Act of Parliament to run trams by steam or mechanical power. The authority to use steam was, in fact, subject to the approval of the Board of Trade, but no mention was made of this. The Board refused consent and consequently the company was wound up. The plaintiff, having bought some shares, sued the directors for fraud. But they were held not liable.

They were not guilty of fraud as they honestly believed that once the Parliament had authorised the use of steam, the consent of the Board was

137. (1889) LR 14 AC 337 at p. 374.

practically concluded. It follows, therefore, that the person making a false representation is not guilty of fraud if he honestly believes in its truth. Thus intentional misrepresentation is of the essence of fraud. The first three clauses of Section 17 deal with this kind of fraud.<sup>138</sup>

### Active concealment

“Active concealment” is something different from mere “passive concealment”.<sup>139</sup> Passive concealment means mere silence as to material facts. An active concealment of a material fact is a fraud; mere silence, excepting the few cases noted below, does not amount to fraud.

The expression “any other act fitted to deceive” naturally means any act which is done with the obvious intention of committing fraud. For example, a husband persuaded his illiterate wife to sign certain documents telling her that by them he was going to mortgage her two lands to secure his indebtedness and in fact mortgaged four lands belonging to her. This was an act done with the intention of deceiving her.<sup>140</sup> Where a person surrendered his land to the State which was accepted after inquiry, but the land had already been acquired under the Land Acquisition Act, it was held that the fact of inquiry could not wipe out the consequence of fraud. The transaction of surrender was a nullity. Where the seller of property did not disclose to the buyer pending litigation about the property, the buyer was allowed refund of his money with 6 per cent interest.<sup>141</sup>

### Mere silence is no fraud

False impression is ordinarily conveyed by deliberate misstatement of facts. But it may also be done by active concealment of material facts. “I do not care,” said Lord HALSBURY, “by what means a false impression is conveyed—by what trick or device or ambiguous language, all those are expedients by which fraudulent people seem to think that they can escape from the real substance of the transaction.”<sup>142</sup> Ordinarily, of course, mere silence is no fraud, even if its result is to conceal “facts likely to affect the

138. *A.L. Mustaneer Establishment v. Varuna Overseas (P) Ltd*, (1998) 72 DLT 186, fraud is a facet of dishonesty, fraud in connection with letters of credit. *Santhakumari v Lakshmiammal*, (2004) 2 CTC 259, a lessee in possession and who had put up a building also and had purchased the lessor's interest was not allowed to say that the lessor had made fraudulent misrepresentations. He could not recover back the money paid by him without seeking cancellation of the sale deed.

139. *Gowrishankar v Joshi Amba Shankar Family Trust*, (1996) 3 SCC 310: AIR 1996 SC 2202.

140. *Ningawwa v Byrappa Shiddappa Hirekrabar*, AIR 1968 SC 956, 958: (1968) 2 SCR 797; *Visveswaran v State*, (2003) 6 SCC 73: AIR 2004 SC 1227 months old pregnancy could not have been concealed. The defendant married her, accepted the child and some 4 years later divorced her. Bound to pay maintenance. *B.R. Chowdhury v Indian Oil Corpn Ltd*, (2004) 2 SCC 177, concealment of the fact of previous employment under the Government for getting dealership, allowed to be terminated.

141. *P.L. Raju v Dr Nandan Singh*, (2005) 5 ALD 402.

142. *Aaron's Reefs v Twiss*, 1896 AC 273, 281 (HL).

willingness of a person to enter into a contract.”<sup>143</sup> A contracting party is under no obligation to disclose the whole truth to the other party or to give him the whole information in his possession affecting the subject-matter of the contract. It is under this principle that a trader may keep silent about a change in prices. A seller who puts forth an unsound horse for sale, but says nothing about its quality, commits no fraud. In a case before the Supreme Court,<sup>144</sup> a candidate, who had full knowledge of the fact that he was short of attendance, did not mention this fact in his examination form. This was held to be no fraud, it being the duty of the University to scrutinise forms and to call for verification or information in case of doubts. The University having failed to do so, was estopped from cancelling the examination of the candidate.

A house was let out for three years without disclosing to the tenant that it was in such a ruinous and dangerous state as to be dangerous to occupy, a fact in the landlord’s knowledge. When the tenant discovered this fact he applied to have the contract set aside, arguing that the landlord should have disclosed the real state of the house. The court did not allow the relief. There was no warranty that the house was fit for immediate occupation. No misrepresentation was made, nor it was the case that the plaintiff was acting on the impression produced by any conduct on the part of the owner as to the state of the house or that he was not to make investigation before he began to reside in it. There was no obligation on the owner to say anything about the state of the house.<sup>145</sup>

#### *Misdeclaration in application form*

In an application for dealership of petroleum products, the applicant made a misdeclaration about his income in the application form. It was held that cancellation of the letter of intent issued to him was proper. The contention that the fact wrongly declared had no bearing on the eligibility criterion was not accepted.<sup>146</sup>

#### **When silence is fraud**

But then how far may silence go? Silence may become deceptive in certain cases.

##### **1. Duty to speak (*contracts uberrima fides*)**

The first such case is when the person keeping silence is under duty to speak. Duty to speak arises where one contracting party reposes trust and confidence in the other. A father, for example, selling a horse to his son must tell him if the horse is unsound, as the son is likely to rely upon his father.

143. S. 17 (Explanation). See, for example, Illustrations (a) and (d).

144. *Shri Krishnan v Kurukshestra University*, (1976) 1 SCC 311: AIR 1976 SC 376.

145. *Keats v Earl of Cadogan*, (1851) 20 LJ CP 76 Common Pleas.

146. *Shiv Kant Yadav v Indian Oil Corp*, (2007) 4 SCC 410: AIR 2007 SC 1534.

But the principle is not so confined. The duty to disclose the truth will arise in all cases where one party reposes, and the other accepts, confidence.<sup>147</sup> Duty to speak also arises where one of the parties is utterly without any means of discovering the truth and has to depend on the good sense of the other party. An insurance company, for example, knows nothing about the life or circumstances of the assured. It has to depend on the disclosures made by the assured. It is, therefore, the duty of the assured to put the insurer in possession of all the material facts affecting the risk covered. A contract of insurance is, for this reason, called a contract of absolute good faith, *uberrima fides*.<sup>148</sup> Where false answers as to the state of health were given in a proposal for life insurance, the policy was held to be voidable and it was not material that the medical officer of the corporation had certified the life assured as good.<sup>149</sup> Where a person got his motor vehicle insured in the evening, when in the morning, the vehicle had met with an accident, the policy was held to be not enforceable, the duty of the insurer to check the vehicle notwithstanding.<sup>150</sup> Burden of proof lies on the insurer to show that the fact misstated or suppressed was of material nature to the risk covered and that the same was done to cause misconception about the risk undertaken by the insurer.<sup>151</sup>

In the absence of any such relationship there is no duty to speak and mere silence even if it amounts to misrepresentation, will be no fraud. For example, in *Haji Ahmad Yarkhan v Abdul Gani Khan*:<sup>152</sup>

The plaintiff spent a sum of money to mark the engagement of his son. He then discovered that the girl suffered from epileptic fits and so broke off the engagement. He sued the other party to recover from them compensation for the loss which he had suffered on account of their deliberate suppression of a vital fact which amounted to fraud.

The court relied upon the decision of the House of Lords in *Nocton v Lord Ashburton*<sup>153</sup> where it was pointed out that a mere passive non-disclosure of

147. See for example, *Nursey Spg & Wvg Co Ltd, re*, ILR (1880) 5 Bom 92, *Sri Alam v Newaires*, (1994) 1 Current LJ 32 (Malaysia); *Saroj Agarwal v LIC*, (2004) 4 CLT 490 (Jhar), positive “No” answer was given to the question of any treatment about the state of heart, the answer being false, the claim failed.

148. See Reuben Hasson, *The Special Nature of the Insurance Contract: A Comparison of the American and English Law of Insurance*, (1984) 47 Mod LR 523.

149. *P. Sarojam v LIC*, AIR 1986 Ker 201; *P.J. Chacko v LIC*, AIR 2008 SC 424, non-disclosure in insurance proposal that the insured had undergone operation for a thyroid adenoma; held, policy voidable, the insured was estopped from saying that even if that fact had been disclosed, it would not have affected the transaction.

150. *George P. Varghese v G. Daniel*, AIR 1998 Ker 120; *Rajesh Kumar Choudhary v United India Insurance Co Ltd*, (2005) 3 CCC 64 (Gau), non-disclosure that an earlier proposal of insurance for the same property and on the same ground had been refused by the same company, held suppression of material fact. The subsequent insurance was obtained by suppressing that fact.

151. *LIC v B. Kusuma T. Rai*, (1989) 1 Kant LJ 52.

152. AIR 1937 Nag 270.

153. (1914) AC 932 (HL).

the truth, however deceptive in fact, does not amount to fraud, unless there is a duty to speak. Referring to the facts the court said that the law imposes no general duty on anyone to broadcast the blemishes of his female relations; not even to those who are contemplating matrimony with them. There was no fiduciary relation between the parties. The engagement was, however, held to be voidable by reason of the misrepresentation, but the plaintiff was not entitled to recover any compensation under Section 75 of the Contract Act.

## 2. *Where silence is deceptive*

Silence is sometimes itself equivalent to speech. A person who keeps silent, knowing that his silence is going to be deceptive, is no less guilty of fraud. Where, for example, the buyer knows more about the value of the property, which is the subject of sale, but prefers to keep the information from the seller, the latter may void the sale. [Illustration (d), S. 17]

## 3. *Change of circumstances*

Sometimes a representation is true when made, but, it may, on account of a change of circumstances, become false when it is actually acted upon by the other party. In such circumstances, it is the duty of the person who made the representation to communicate the change of circumstances. In an English case,<sup>154</sup> for example:

A medical practitioner represented to the plaintiff that 'his practice was worth £2000 a year'. The representation was true. But five months later when the plaintiff actually bought the practice, it had considerably gone down on account of the defendant's serious illness.

It was held that the change of circumstances ought to have been communicated. Similarly, in a case before the Madras High Court:<sup>155</sup>

"A company's prospectus represented that certain persons would be the directors of the company. This was true. But before the allotment took place, there were changes in the directorate, some directors having retired."

That was held to be sufficient to entitle an allottee to avoid the allotment.

## 4. *Half-truths*

Even when a person is under no duty to disclose a fact, he may become guilty of fraud by non-disclosure if he voluntarily discloses something and then stops half the way. A person may keep silence, but if he speaks, a duty arises to disclose the whole truth. "Everybody knows that sometimes half

154. *With v O'Flanagan*, 1936 Ch 575 (CA).

155. *T.S. Rajagopala Iyer v South Indian Rubber Works Ltd*, (1942) 2 MLJ 228.

a truth is no better than a downright falsehood.”<sup>156</sup> In a US case,<sup>157</sup> for example:

The plaintiff purchased a tract of land. The contract of sale stated that the land was subject to a right of the Borough to open two streets within the area. But as a matter of fact the Borough had the right to open three streets.

Holding that the plaintiff had the right of rescission, CORDOZO CJ said: “We do not say that the seller was under a duty to mention the projected streets at all. That question is not here. What we say is merely this, that having undertaken or professed to mention them, he could not fairly stop halfway.”

As in misrepresentation, so in fraud by silence, if the plaintiff had means to discover the truth by ordinary diligence, he cannot obtain rescission. But in any other case the fraudulent party cannot say that the other could have discovered the truth. In a case, for example, before the Gujarat High Court:<sup>158</sup>

False estimates of the costs of construction were given in a tender. The contractor agreed to some reduction on the belief that the estimate was correct. The court held that the representations contained in the tender were fraudulent and that it was no defence that the plaintiff could have discovered the true costs by reasonable effort.

### Promise made without intention of performing

To tie-up a person to a promise with no intention of performing from one's side and with the intention of only preventing the other from dealing with others, is an example of a promise made without the intention of performing it. This is the third type of fraud included in the definition in Section 17. A purchase of goods without any intention of paying the price is a fraud of this species.<sup>159</sup> A builder entered into a large number of bookings, nearly three times the available units of accommodation and collected monies. This was held by the Supreme Court to be fraud because he should have known that he would not be able to perform the contract with all of them. There was no provision for interest on the deposit money. Inspite of this he was held liable to pay interest. The Court said that there was fraud causing inducement for booking by the purchasers: such fraud creates liability even outside the agreement.<sup>160</sup>

156. Per Lord MACNAUGHTAN in *Gluckstein v Barnes*, 1900 AC 240, 250.

157. *Junius Construction Corp v Cohen*, (1931) 257 NY 393. Facts and opinion collected from Thurston and Seavey, CASES OF TORTS, 677 (1942).

158. *R.C. Thakkar v Bombay Housing Board*, AIR 1973 Guj 34. But see *M. Hassanji & Sons v State of M.P.*, AIR 1965 SC 470, 472: 1963 Supp (2) SCR 235.

159. *Clough v London & N.W. Rly Co*, (1871) LR 7 Exch 26; *Whitaker, ex p*, (1875) LR 10 Ch 449.

160. *DDA v Skipper Construction Co (P) Ltd*, (2000) 10 SCC 130.

### Any other act fitted to deceive

The fourth kind of fraud identified by Section 17 is any act which is fitted to deceive. In a case before the Calcutta High Court where a practitioner cast aspersions on the court and also on the opposite lawyer, the court cited generally the following statement about the concept of fraud: Fraud has been defined in Section 17 of the Contract Act, 1872. As per interpretation of the statute, two kinds of fraud are mentioned, (i) actual or positive fraud which includes cases of intentional and successful employment of any cunning, deception, or artifice, used to circumvent, cheat or deceive another; and (ii) constructive or legal fraud which includes such contracts or acts as though not originating in any actual evil design or contrivance to perpetrate a fraud yet, by their tendency to deceive or mislead others, or to violate private or public confidence, are prohibited by law (*COMMENTARIES ON EQUITY JURISPRUDENCE* by Justice STORY).<sup>161</sup>

### Any act or omission specially declared to be fraudulent

The last category includes cases in which the law specially declares an act or omission to be fraudulent. For example, the Insolvency Act and Companies Act declare certain kinds of transfer to be “fraudulent preference”.

The fifth and the last category of frauds included in the definition of Section 17 is intended to cover all such acts which under any other branch of law are regarded as fraudulent. In insolvency law there is, for example, the concept of fraudulent preference and in the Transfer of Property Act, there is the concept of fraudulent transfer.

These words seem to have been inserted for ensuring that all kinds of intentional cheating is covered and nothing of the sort escapes.<sup>162</sup>

### Distinction between fraud and misrepresentation

Misrepresentation and fraud have many points in common. For instance, both render the contract voidable; there is a false representation in both; in either case it is necessary that the consent should have been caused by the fraud or misrepresentation and finally, where there is a fraud by silence, the fact, that there were “means of discovering the truth by ordinary diligence”, is a good defence.<sup>163</sup> This is so in misrepresentation also. Damages for loss caused by innocent misrepresentation are assessed on the same principles as in the case of a deliberate fraud.<sup>164</sup> Yet the following points of distinction are also noticeable:

161. *Hungerford Investment Trust Ltd v Turner Morrison & Co Ltd*, (2009) 2 CHN 330.

162. Application for allotment of premises containing false particulars, fraud, allotment liable to be set aside, *Ponnurangam v Slum Clearance Board of T.N.*, 1986 SCC OnLine Mad 20: AIR 1996 Mad 274. *Nedungadi Bank Ltd v Ezhimala Agri Products*, AIR 2004 Ker 62, court sale at gross under value, purchaser son of one of the judgment-debtors and the joint purchaser was a relative of the judgment-debtor, fraud, upon the process of the court.

163. S. 19 (Exception).

164. *Royscot Trust Ltd v Rogerson*, (1991) 2 QB 297: (1991) 3 WLR 57 (CA).

Firstly, fraud is more or less an intentional wrong, whereas misrepresentation may be quite innocent.

Secondly, fraud, in addition to rendering the contract voidable, is a cause of action in tort for damages. Simple misrepresentation is not a tort but under Section 75 of the Contract Act, “a person who rightfully rescinds a contract is entitled to compensation for any damage which he has sustained through the non-fulfilment of the contract.”<sup>165</sup> The (English) Misrepresentation Act, 1967, also enables the court to award damages instead of rescission.<sup>166</sup> A person who purported to sell his wife’s property without obtaining her consent and she refused to sign the deed, was held liable to the buyer for his loss.<sup>167</sup> A purchaser of premises completed the purchase even after discovering that a tenancy agreement affecting one of the flats was concealed from him. He was nevertheless allowed to sue for damages for the loss caused to him, though he had in tort the right to rescind.<sup>168</sup>

Lastly, a person complaining of misrepresentation can be met with the defence that he had “the means of discovering the truth with ordinary diligence”, [S. 17, Exception] but excepting fraud by silence,<sup>169</sup> it does not lie in the mouth of the person committing fraud to say that his victim was too easily deceived or had the means of discovering the truth. “Fools have to be protected against knaves.”

### Limits of rescission [Ss. 19 and 19-A]

A contract the consent to which is caused by coercion, undue influence, fraud or misrepresentation is voidable at the option of the party whose consent was so caused.<sup>170</sup> Section 19 provides:

165. The section gives illustration [See under the Section]. There is no such right if the damage is not caused by non-fulfilment of the contract. See *Haji Ahmad Yarkhan v Abdul Gani Khan*, AIR 1937 Nag 270.

166. S. 2(2). See *William Sindall plc v Cambridgeshire County Council*, (1994) 1 WLR 1016 (CA), loss in value of land because of foul sewer under it, compensation for loss instead of rescission.

167. *Watts v Spence*, 1976 Ch 165: (1975) 2 WLR 1039.

168. *Production Technology Consultants v Bartlett*, (1988) 25 Eg 121 CA (Estate’s Gazette): 1988 CLY 460.

169. *Ibid*. See *John Minas Apcar v Louis Caird Matchus*, AIR 1939 Cal 473. The P&H High Court laid emphasis in *Sardara v State of Haryana*, 1995 AIHC 1163 (P&H) upon the fact that there are no other grounds for cancelling and rescinding a contract than those provided in the Act and that any other kind of cancellation would be a breach. A rescission of contract notified by unauthorised functionaries of the State was set aside. *P. Anasuyamma v Commr of Land Revenue*, 1995 AIHC 2082 (AP), the period of limitation for filing a suit for rescission is three years. A suit commenced 12 years after an assignment was quashed.

170. Ss. 19 and 19-A. Burden is on the party alleging fraud to establish it. *Hajra Bai v Jadavabai*, AIR 1986 MP 106. He has also to disclose in his plaint the full particulars of the acts that constitute any of the vitiating factors entitling him to avoid the contract. See *G. Subhashini v P. Lakshmi Bai*, (1987) 1 MLJ 107. Vague and general allegations are insufficient. The vitiating factors must be separately pleaded with specificity, particularity and precision, (1987) 1 All LJ 64, following *Bishundeo Narain v Seogeni Rai*, AIR 1951 SC 280: 1951 SCR 548; *Kuluwa v Punia*, 1995 AIHC 8 All, an illiterate person who was the victim of fraud was held

When consent to an agreement is caused by coercion, fraud or misrepresentation, the agreement is a contract voidable at the option of the party whose consent was so caused.

The provision does not refer to “undue influence” because this is specially dealt with by Section 19-A. Section 19 further goes on to provide something special about the effect of fraud and misrepresentation. It says:

A party to a contract, whose consent was caused by fraud or misrepresentation, may, if he thinks fit, insist that the contract shall be performed, and that he shall be put in the position in which he would have been if the representation made had been true.

The party affected by the factors that make the contract voidable, has to avoid it because otherwise it remains valid. It is not like that of a void agreement that does not require to be avoided.<sup>171</sup> He has the option either to avoid the contract or, alternatively, to affirm it. When fraud is proved, the whole proceedings fails. The suit and execution proceedings are all a nullity.<sup>172</sup> The onus is on the plaintiff to prove fraud, etc. For this purpose he has to plead the precise particulars which constitute the alleged fraud. This onus is quite as high as the burden to prove in criminal law that the accused is guilty beyond a reasonable doubt.<sup>173</sup> He can exercise his option only once. If the contract is affirmed, it becomes enforceable by both the parties and, if it is avoided, it becomes void as against both.<sup>174</sup> The effect of rescission is that the contract is set aside and the parties are restored to their original position. Where a State Financial Corporation had taken over the

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entitled to the same amount of protection as a *pardanashin* woman, namely, burden of proof on the other party to prove fairness of the transaction. *Upendra Mohant v Champa*, 1996 AIHC 3449 (Ori), an illiterate woman entitled to the protection of a *pardanashin* woman. *N. Narayani Ammal v P. Sanjeev*, AIR 2001 Ker 305, document obtained by fraud is voidable and not void. *Rajinder Singh v Joginder Singh*, (2003) 1 ICC 705 (P&H), a fraudulent decree can neither create nor take away any rights.

171. *HD Hanumanthappa v Mohd Sab*, (2011) 1 Kant LJ 49.
172. *T. Vijayendras v M. Subramanian*, 2006 SCC OnLine Mad 1315: (2006) 2 LW 572; *Harmesh Kumar v Maya Bai*, AIR 2006 P&H 1, illiterate widow authorised special power of attorney to attend to litigation against her, transferred her property to his son in fraud, held, *non-est*.
173. *Krishna Wanti v LIC*, AIR 2000 Del 63, the LIC could not prove that the assured had concealed or suppressed knowledge about his heart condition at the time of taking out the policy. *Jibrail Mian v Lalu Turi*, AIR 2004 Jhar 139, fraud on illiterate woman by fraudulent sale deed, whole deed, set aside, it could not be avoided in one part only unless it was severable from the rest. *Damodar Tukaram Gaunkar v Gopinath Rama Gaunkar*, (2006) 6 Bom CR 454 (Panaji Bench), setting aside of consent decree on the ground of fraud, pleadings should give particulars of fraud, mere vague and sweeping allegations are of no avail. *Soraban Bewa v Jinnath Bibi*, (2004) 1 ICC 273 (Cal), fraud or undue influence to be specifically pleaded in the manner required under Order 6, Rule 4, CPC. In the absence of such specific pleading fraudulent intention or undue influence cannot be inferred.
174. Ss. 2(j) and 64 which say that when a person at whose option a contract is voidable rescinds it, the other party need not perform his part of the promise. The Supreme Court has gone to the extent of holding that a licence obtained by misrepresentation is voidable and remains good till it is avoided by the licensing authority in the manner prescribed by law. *East India Commercial Co Ltd v Collector of Customs*, AIR 1962 SC 1893: (1963) 3 SCR 338.

unit of the borrower, but an offer was made to the defaulting borrower to take back the unit on paying certain price which offer was accepted by his widow by making the payment, but subsequently the Corporation came out with a revised and a higher claim, it was held that the earlier figure was a misrepresentation on which the widow acted. She had the right to have the deal set aside and recover back the amount paid by her which could not be considered as repayment of the loan.<sup>175</sup> A purchaser of immovable property who alleged that there were fraudulent statements in the sale deed was not allowed to recover back the purchase money without having the documents set aside because of fraud.<sup>176</sup> Moreover, the right to rescind is subject to certain infirmities which defeat it in the following circumstances:

#### *Loss of right of rescission*

##### *1. By affirmation*

Where the party, after becoming aware of his right to rescind, affirms the contract, the right of rescission is lost. Affirmation may be express or implied. An implied affirmation takes place when he does some act inconsistent with his right to rescind, for example, where he appropriates to his use the goods received under a voidable contract or has sold or attempted to sell them. An interesting illustration of implied affirmation is to be found in *Long v Lloyd*.<sup>177</sup>

The defendant induced the plaintiff to buy his lorry by falsely convincing him that it was "in excellent condition". On the very first journey the plaintiff discovered serious defects, but accepted the defendant's offer to bear half the cost of repairs. The lorry completely broke down on the next journey and he then claimed rescission.

The court held that on the first breakdown the plaintiff came to know that the representation was false. But, instead of asking for rescission then, he accepted the offer of repair and sent the lorry on a second trip. This amounted to "a final acceptance... for better or for worse and conclusively extinguished any right of rescission remaining to the plaintiff after completion of the sale."<sup>178</sup>

Similarly, it has been observed by the Supreme Court that "if it can be shown that the party defrauded has at any time after knowledge of the fraud either by express words or by unequivocal acts affirmed the contract, his election is determined forever. The party defrauded may keep the question

175. *Sita Devi v Bihar State Financial Corpn*, AIR 2003 Pat 92; *Markande v Sudama Chaubey*, AIR 2007 All 70, plaintiff consented to execution of power of attorney but fraudulently it was converted into a sale deed. Allowed to be cancelled.

176. *Santhakumari v Lakshmiammal*, (2004) 2 CTC 259.

177. (1958) 1 WLR 753 (CA); *Broadway Centre v Gopaldas Bagri*, AIR 2002 Cal 78, allegation by the partner that he signed the retirement deed while in police station was rejected, he had already taken a big sum of money under the retirement deed.

178. See P.S. Atiyah, (1959) 22 MLR 76 and J.D. Davies, 75 LQR 32.

open so long as he does nothing to affirm the contract.<sup>179</sup> The provision is not applicable to a concluded contract when the party challenging it had voluntarily chosen to implement it knowing all the relevant facts and circumstances.<sup>180</sup>

## 2. By lapse of time

Rescission must be claimed within reasonable time after discovering the misrepresentation. Thus where shares were allotted to a person on the basis of a misleading prospectus in July and in December he moved to set aside the contract, it was held that the unexplained delay of five months precluded him from obtaining the relief.<sup>181</sup>

The challenge to an arbitration award on the ground of fraud is to be established by filing an independent suit or filing an application under Section 34 of the Arbitration and Conciliation Act, 1996. A writ petition on the ground of fraud, that too after inordinate delay, created a question mark about *bona fides* of the petitioner. The court refused to set aside the award on the ground of fraud.<sup>182</sup>

In respect of defences of this nature, including that of mistake, it is necessary that they should be raised while contracting or immediately thereafter. Once the contract has run its full period, such a plea may cease to be available.<sup>183</sup>

## 3. Intervention of rights of third parties

The right of rescission is lost as soon as a third party, acting in good faith, acquires rights in the subject-matter of the contract. Thus, where a person obtains goods by fraud and, before the seller is able to avoid the contract, disposes them off to a *bona fide* party, the seller cannot then rescind.

### Mode of rescission

The usual method of rescinding a contract is by giving a notice to the other party of the intention to rescind. But what should he do if the other party cannot be contacted? The answer is to be found in *Car & Universal Finance Co Ltd v Caldwell*:<sup>184</sup>

The plaintiff gave the possession of his car to a buyer for his cheque. The cheque turned out to be worthless. The plaintiff wanted to give notice to the buyer of his intention to avoid the contract and to take back his car, but could not trace him. He thereupon informed the police and the

179. *Ningawwa v Byrappa Shiddappa Hireknarab*, AIR 1968 SC 956, 958: (1968) 2 SCR 797, 800–01, quoting from *Clough v London & N.W. Rly Co*, (1871) LR 7 Exch 26, 34.

180. *Ganga Retreat & Towers Ltd v State of Rajasthan*, (2003) 12 SCC 91.

181. *Christineville Rubber Estates Ltd, re*, (1911) 81 LJ Ch 63; *Jagannath Prasad, re*, AIR 1938 All 193.

182. *Guwahati Municipal Corpn v International Construction Ltd*, AIR 2014 Gau 101.

183. *Oriental Insurance Co Ltd v Mantora Oil Products (P) Ltd*, (2000) 10 SCC 26.

184. (1965) 1 QB 525: (1964) 2 WLR 600 (CA).

Automobile Association to trace his car. Sometime later the fraudulent buyer sold the car to the defendant and the plaintiff sought to recover it.

It was held that by informing the police and the Association the plaintiff had done an *overt act* clearly showing his intention to rescind and the sale of the car after rescission could not convey to the defendant a good title. To hold otherwise, said SELLERS LJ "would involve that the defrauding party, if skilful enough to keep out of the way, would deprive the other party to the contract of his right to rescind. That another innocent party or parties may suffer does not justify imposing on a defrauded seller an impossible task. He has to establish clearly and unequivocally that he terminates the contract and is no longer to be bound by it. If he cannot communicate his decision he may still satisfy a judge that he had made a final and irrevocable decision and ended the contract."

A similar problem was before the Allahabad High Court in *Official Receiver v Jugal Kishore Lachhi Ram Jaina*:<sup>185</sup>

Under an agreement for sale of certain goods, the plaintiff received through a bank the railway receipts supposed to represent the goods and obtained them from the bank after paying Rs 15,000. The amount was sent to the seller's account at his place of business. Meanwhile the plaintiff discovered that the railway receipts were bogus and immediately informed the bank not to part with the amount which was accordingly withheld. But before the plaintiff could inform either the fraudulent seller or file a suit for rescission an insolvency judge ordered the bank not to pay the amount to either party.

The plaintiff then filed a suit for declaration that he was entitled to his money. The Full Bench was of the view that the plaintiff had parted with his money under a fraud. Thus the money came into the insolvent's account under a defeasible title and the plaintiff had defeated it when he directed the banker to stop payment which was done before the insolvency judge's order. Even if he had rescinded by filing the suit, he was entitled to the money, because he had done nothing to affirm the contract.

Section 66 lays down the way in which the communication of rescission is to be made effective.

**S. 66. Mode of communicating or revoking rescission of voidable contract.**—The rescission of a voidable contract may be communicated or revoked in the same manner, and subject to the same rules, as apply to the communication or revocation of a proposal.

### Restitution

Rescission is always subject to the condition that the party seeking rescission must be in a position to restore the benefits he may have obtained under the contract. Section 64 requires him to do so.

185. AIR 1963 All 459.

**S. 64. Consequences of rescission of voidable contract.**—When a person at whose option a contract is voidable rescinds it, the other party thereto need not perform any promise therein contained in which he is promisor. The party rescinding a voidable contract shall, if he has received any benefit thereunder from another party to such contract, restore such benefit, so far as may be, to the person from whom it was received.

A person avoiding a loan bond on the ground of undue influence has to pay back the loan, the court only reduces the rate of interest to what may seem to be reasonable in the circumstances.<sup>186</sup> A corporation supplied, after taking payment in advance, a quantity of rapeseed oil which turned out to be mixed with water, the corporation had to refund the money with interest.<sup>187</sup>

Even where the party seeking rescission is not in a position to restore to the defendant his *status quo ante*, the court may allow rescission by doing what is practically just in the circumstances.<sup>188</sup> Thus, where a wife wanted to set aside on the ground of misrepresentation the separation deed made with her husband, under which she had already received some maintenance, but she was not able to restore the money, the court allowed her relief holding that the money may be set-off against costs to which she was otherwise entitled.<sup>189</sup> SWINFEN EADY LJ said: “The general rule is that as a condition of rescission there must be *restitution in integrum*, but at the same time the court has the full power to make all just allowances. It was said by Lord BLACKBURN in *Erlangar v New Sombrero Phosphate Co*,<sup>190</sup> that the practice had always been for a court of equity to give relief by way of rescission whenever by the exercise of its power it can do what is practically just, though it cannot restore the parties precisely in the state that they were in before the contract. On the other hand, where both parties had spent money on the property in terms of the contract in such manner that restitution was not possible, rescission was not allowed even though there was innocent misrepresentation on the part of the seller of the property.<sup>191</sup> The position is thus summarised by Treital:<sup>192</sup> “As in cases of misrepresentation,

186. See, for example, *Bechu v Babbuti Prasad*, AIR 1931 All 201; *Muralidhar Chatterjee v International Film Co Ltd*, (1943) 56 LW 283: AIR 1943 PC 34 and the cases cited there under “Undue Influence.” *Mhow Hosiery (P) Ltd v Jitendra Nirlan Singh*, (2005) 3 MP LJ 179, employer company in financial difficulties, obtained resignation of 200–50 employees by pressuring them, the court set aside the resignations, awarded reinstatement with full back wages. The High Court awarded compensation of Rs 30,000 to each workman in place reinstatement and back wages.

187. *Ashok Vandhan Bhagat v W.B. Essential Commodity Supply Corp*n Ltd, AIR 1992 Cal 135.

188. *Neill v Morley*, 32 ER 687 and *Molton v Camroux*, 154 ER 1107: (1848) 2 Exch 487, mental patient's option to avoid, in England such contract being only voidable.

189. *Hulton v Hulton*, (1917) 1 KB 813.

190. 1878 AC 1218. S. 64 cannot be invoked where the party has abandoned the plea of misrepresentation and admitted breach; *Shree Hanuman Cotton Mills v Tata Aircraft Ltd*, (1969) 3 SCC 522: AIR 1970 SC 1986.

191. *Lagunas Nitrate Co v Lagunas Syndicate*, (1899) 2 Ch 392 (CA). Followed in *Spence v Crawford*, (1939) 3 All ER 271 (HL).

192. LAW OF CONTRACT (7th Edn) 321.

the party seeking rescission must restore benefits that he has obtained under the contract, but he is not required to make precise restitution: the principle of allowing rescission for misrepresentation so long as equity can achieve a result that is ‘practically just’ applies also where rescission is sought on the ground of undue influence.”

Following this position of law in a case, it was held that where a party received nothing under the mortgage which was set aside on the ground of undue influence, there was nothing for him to make restitution.

### Damages for innocent misrepresentation

A person who is the victim of a fraud is entitled to sue for damages, fraud being a tort also. But the victim of an innocent misrepresentation was not allowed to recover any compensation for any loss that might have been occasioned to him by the misrepresentation. Liability in tort for negligent or innocent misrepresentation is still growing for recognition. However, much of the suffering of the victims of innocent misrepresentations have now been relieved by the (English) Misrepresentation Act, 1967. Section 2 of the Act provides:

- (1) A person who has entered into a contract on account of a misrepresentation will have the same right to recover compensation for loss, if any, caused to him as if the misrepresentation had been made to him fraudulently. The defendant will not be liable if he had a reasonable ground to believe and did up to the time of the contract believe that the facts represented were true.
- (2) Where it is alleged in any proceeding that the contract ought to be or has been rescinded, the court may, instead, declare the contract to be subsisting and award damages in place of rescission, if it is equitable to do so.
- (3) Provisions in the contract which exclude or restrict liability would be of no effect, unless they are fair and reasonable in the circumstances of the case.

The vendor of a property relied on her husband to deal with her business affairs. The husband stated to the purchaser that to the vendor's knowledge there was no dispute with any neighbour over boundary. In fact there was a dispute of this kind, though the husband did not know it. His statement amounted to an innocent misrepresentation. The purchaser was allowed rescission and refund of deposit.

He was further entitled under Section 2(1) to an inquiry into damages suffered arising out of the loss of interest for the period between the date of deposit and its placement in an interest-earning account.<sup>193</sup>

193. *Walker v Boyle*, (1982) 1 WLR 495. See Anthea Cameron, *Measuring Dilectual Damages for Fraudulent Misrepresentation*, (1982) 99 SALJ 99. *McGrath v Shah*, (1989) 57 P&CR 452 Ch D, misrepresentations in a building contract. The court held that a contract can

### Rescission for failure to perform within time [S. 75]

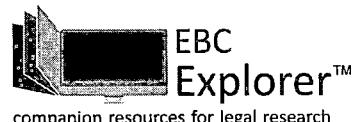
A contract for construction of a bridge was a time-bound work. The contractor failed to complete the work within the stipulated time. The State rescinded the contract. The contractor did not challenge it. The contract was allotted to another party. The State was held entitled to recover the loss of money thereby caused.<sup>194</sup>

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contain a provision that it contains its entire terms. Such an exhaustive clause does not invalidate the contract.

194. *Shiv Construction v PWD*, AIR 2015 MP 42.

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- *Lakshmi Amma v Talengalanarayana*, (1970) 3 SCC 159
- *Raghunath Prasad Sahu v Sarju Prasad Sahu*, (1924) 19 LW 470:  
AIR 1924 PC 60
- *Subhas Chandra Das Mushib v Ganga Prasad Das Mushib*,  
AIR 1967 SC 878: (1967) 1 SCR 331



# Mistake

## Definition of “consent” [S. 13]

The provisions of the Contract Act relevant to a study of the effect of “mistake” upon a contract that the parties have purported to make may be noted first. Mistake may operate upon a contract in two ways. It may, firstly, defeat the consent altogether that the parties are supposed to have given, that is to say, the consent is unreal. Secondly, the mistake may mislead the parties as to the purpose which they contemplated.

The cases in which the consent is defeated or is rendered unreal fall under Section 13. This section defines “consent” as follows:

Two or more persons are said to consent when they agree upon the same thing in the same sense.

An agreement upon the same thing in the same sense is known as true consent or *consensus ad idem*, and is at the root of every contract.

This seems to have been picked up from a passage<sup>1</sup> in the judgment of Lord HANNEN in *Smith v Hughes*.<sup>2</sup> “It is essential to the creation of a contract that both parties should agree to the same thing in the same sense. Thus if two persons enter into an apparent contract concerning a particular person or ship, and it turns out that each of them, misled by a similarity of name, had a different person or ship in mind, no contract would exist between them: *Raffles v Wichelhaus*”.<sup>3</sup>

## Definition of “mistake”

Where the mistake does not defeat consent, but only misleads the parties, Section 20 shall apply. This section provides:

1. *Central National Bank Ltd v United Industrial Bank Ltd*, AIR 1954 SC 181: 1954 SCR 391. Once “consent” has been proved, it cannot be defeated by application of criminal law. See, for example, *Kaur v Chief Constable, Hampshire*, (1981) 1 WLR 578, where it was held that a mistake as to price induced by wrong marking was not so fundamental as to destroy the validity of contract of sale.
2. (1871) LR 6 QB 597 (DC).
3. (1864) 2 H&C 906: 159 ER 375. If a thing is not understood by the parties in the same sense, the agreement would be invalidated at the inception stage itself even if the communication gap is discovered at a later stage, *Tarsem Singh v Sukhwinder Singh*, (1998) 3 SCC 471: AIR 1998 SC 1400.

Where both the parties to an agreement are under a mistake as to a matter of fact essential to the agreement, the agreement is void.

*Explanation.*—An erroneous opinion as to the value of the thing which forms the subject-matter of the agreement, is not to be deemed a mistake as to a matter of fact.

*Illustrations*

- (a) A agrees to sell to B a specific cargo of goods supposed to be on its way from England to Bombay. It turns out that, before the day of the bargain, the ship conveying the cargo had been cast away, and the goods lost. Neither party was aware of these facts. The agreement is void.
- (b) A agrees to buy from B a certain horse. It turns out that the horse was dead at the time of the bargain, though neither party was aware of the fact. The agreement is void.
- (c) A, being entitled to an estate for the life of B, agrees to sell it to C. B was dead at the time of the agreement, but both parties were ignorant of the fact. The agreement is void.

Section 20 will come into play:

- (1) when both the parties to an agreement are mistaken,
- (2) their mistake is as to a matter of fact, and
- (3) the fact about which they are mistaken is essential to the agreement.

*Supplementary provisions*

Two of these points are further supplemented by Sections 21 and 22. Section 21 emphasises that mistake should be of fact and not of law.

**S. 21. Effect of mistakes as to law.**—A contract is not voidable because it was caused by a mistake as to any law in force in India; but a mistake as to a law not in force in India has the same effect as a mistake of fact.

*Illustration*

A and B make a contract grounded on the erroneous belief that a particular debt is barred by the Indian law of limitation; the contract is not voidable.

Section 22 deals with a situation where only one party is mistaken:

**S. 22. Contract caused by mistake of one party as to matter of fact.**—A contract is not voidable merely because it was caused by one of the parties to it being under a mistake as to a matter of fact.

**What facts are essential**

What facts are essential to an agreement? The answer is naturally linked with the nature of promise in each case. The plaintiff was a wholesale dealer under a Rationing Order. He was entitled to transport charges variable according to distance for collecting goods from Government godowns. He was paid at the rate applicable to a zone less than 25 miles in distance. The distance in fact, exceeded 25 miles but both parties were unaware of it. As soon as the mistake was discovered future payments were made according to the actual distance. The plaintiff's claim for the arrears up to the time of rectification was dismissed, the court saying that the mistake did not relate

to an essential fact.<sup>4</sup> Thus essentiality depends upon each case. In the above case the mistake related to a minor distance. The fact would have become more important and essential to the contract if a longer distance had been involved. Speaking broadly, certain facts are essential to every agreement. They are:

- (1) The identity of the parties;
- (2) the identity and nature of the subject-matter of the contract; and
- (3) the nature and content of the promise itself.

The present study of the effects of mistake proceeds along these lines and includes the combined effect of Sections 13 and 20.

### MISTAKE AS TO IDENTITY

#### Assumption of false identity

Mistake as to identity occurs where one of the parties represents himself to be some person other than he really is. Thus, for example, in *Jaggan Nath v Secy of State for India*.<sup>5</sup> A person, called S, a brother of the plaintiff, represented himself as plaintiff, and thereby induced a Government agent to contract with him.

The court, finding that the Government's agent was deceived by the conduct of the plaintiff and his brother as to the person with whom he was dealing, held that there was no valid contract. The defendant's agent intended to contract only with S's brother and not with S and S knew this.

In the above case, the Government's offer was meant for S and his brother posing as S accepted it. This prevented real consent. It means that an offer which is meant for one person cannot be accepted by another.

#### Mistake caused by takeover of business

In England there is a long line of cases on the subject. In *Boulton v Jones*<sup>6</sup> the mistake arose naturally in the course of business.

The plaintiff had taken over the business of one Brocklehurst. The defendant used to deal with Brocklehurst and not knowing of the change sent him an order for certain goods. The order was received by the plaintiff who sent the goods. The defendant came to know of the change only when he received an invoice and by that time he had already consumed the goods. The defendant had a set-off against Brocklehurst and, therefore, refused to pay the price. The plaintiff sued him.

Four unanimous judges held the defendant not liable. "Now," said POLLOCK CB, "the rule of law is clear, that if you propose to make a contract

4. *A.P. Kochudevassy v State of Kerala*, AIR 1982 Ker 90.

5. (1886) 21 Punj Rec No 21, p. 37. The Supreme Court observed that mistake of identity will prevent consent in the sense of an agreement of two persons in the same sense. *Central National Bank Ltd v United Industrial Bank Ltd*, AIR 1954 SC 181: 1954 SCR 391.

6. (1857) 27 LJ Ex 117: 2 H&N 564: (1857) 157 ER 232.

with *A*, then *B* cannot substitute himself for *A* without your consent and to your disadvantage, securing to himself all the benefit of the contract.”<sup>7</sup> Similarly, BRAMWELL B said: “When anyone makes a contract in which the personality, so to speak, of the particular party contracted with is important, for any reason, whether because it is to write a book or paint a picture or do any work of personal skill, or whether because there is a set-off due from that party, no one else is at liberty to step in and maintain that he is the party contracted with.”

### Mistake of identity caused by fraud

The principle of this case found further support in *Hardman v Booth*:<sup>8</sup>

The plaintiffs, meaning to deal with Thomas Gandell & Sons, went to their office and took an order from a person who represented himself to be a partner in the firm. He told the plaintiffs that the goods should be sent in the name of Edward Gandell & Sons. He received the goods, carried them away and sold them to the defendant, a *bona fide* buyer. The plaintiffs sued the defendant to recover their goods.

POLLOCK CB explained the principle thus: “There are some cases in which it is very clear that there is no contract at all; and the present case seems to be one of those cases. It is argued that the contract was made personally with the particular individual who made the communication: it is very true that the words were uttered by and to him; but what they imported was a contract with Gandell & Co, the facts being that he was not a member of the firm, and had no authority to act as their agent, and Gandell & Co, therefore, were not the buyers; and, consequently, at no time were there two consenting minds drawn together to the same agreement.”

The principle established by this case was affirmed by the House of Lords in *James Cundy v Thomas Lindsay*:<sup>9</sup>

The plaintiffs received orders in writing from a fraudulent man, called *Blenkarn*. The order papers had a printed heading: ‘*Blenkarn & Co*, 37 Wood Street’. There was a well-known and respectable firm, named *Blenkiron & Co* in the same street. The plaintiff’s believing that the orders had come from this firm, sent a large quantity of handkerchiefs. *Blenkarn* received the goods and disposed them of to the defendants, who acted in good faith. The plaintiffs sued the defendants.

It was held that there was no contract between the plaintiffs and *Blenkarn* and, therefore, he had no right to sell the goods. The plaintiffs intended to contract with *Blenkiron & Co* and consequently no contract could have arisen between them and *Blenkarn*. “Of him they knew nothing, and of him they never thought. With him they never intended to deal. Their minds

7. (1857) 27 LJ 117, 118–19.

8. (1862) 1 H&C 803: 32 LJ Ex 105.

9. (1878) LR 3 AC 459: 38 LT 573: 47 LJ QB 481.

never for an instant of time rested upon him, and as between him and them there was no consensus of mind which could lead to any agreement or any contract whatever. As between him and them there was merely one side to a contract, whereas, in order to produce a contract, two sides would be required.”

### Distinction between identity and attributes

A distinction has been made for this purpose between a person's identity and his attributes and a mistake about the latter has been held not to avoid the agreement. There can be a mistake of identity only when a person bearing a particular identity exists within the knowledge of the plaintiff, and the plaintiff intends to deal with him only. If the name assumed by the swindler is fictitious, there will be no mistake of identity. For instance, in *King's Norton Metal Co Ltd v Edridge, Merrett & Co Ltd*:<sup>10</sup>

A man named Wallis adopted the name of 'Hallam & Co', a non-existent firm, and by letters placed order for some goods with the plaintiffs who complied with the order by sending the goods. Wallis sold the goods to the defendants, who acted in good faith. The plaintiffs sued the defendants for the value of the goods.

The facts of this case were different from those of *Cundy v Lindsay* as in that case *Blenkiron & Co* was a separate entity and the plaintiffs intended to contract only with it. But in this case there was no separate *Hallam & Co*. Accordingly the court said: With whom did the plaintiffs contract to sell the goods? Clearly with the writer of the letters. If it could have been shown that there was a separate entity called *Hallam & Co* and another entity called Wallis then the case might have come within the decision in *Cundy v Lindsay*. The contract with Wallis was, therefore, only voidable for fraud and it could not be disaffirmed after the defendants had acquired the property in good faith.

The scope for operative mistake as to identity is further reduced when the parties are in each other's presence. In *Phillips v Brooks Ltd*.<sup>11</sup>

A man, called North, entered the plaintiff's shop and selected some pearls and some rings worth £3000. He produced a cheque book and wrote out a cheque for the amount. In signing it he said: 'You see who I am, I am Sir George Bullough' and finding on reference to a directory that *Sir George Bullough* lived at the address mentioned, the plaintiff let him have a ring. He promised to come for the other articles after the cheque was cleared. Before the fraud was discovered he pledged the ring with the defendants who advanced money bona fide, and without notice. The plaintiff sued the defendants for the ring or its value.

10. Court of Appeal, (1897) 14 TLR 98 (CA).

11. (1919) 2 KB 243.



It is held that the plaintiff intended to contract with the person present before him. HORRIDGE J said: "The following expressions used in the judgment of MORTON CJ<sup>12</sup> seems to me to fit the facts in this case: 'The minds of the parties met and agreed upon all the terms of the sale, the thing sold, the price and time of payment, the person selling and the person buying. The fact that the seller was induced to sell by the fraud of the buyer made the sale voidable, but not void. He could not have supposed that he was selling to any other person; his intention was to sell to the person present, and identified by sight and hearing, it does not defeat the sale because the buyer assumed a false name...'"<sup>13</sup>

The authority of this case seems to have been considerably shaken by the decision of the Court of Appeal in *Ingram v Little*.<sup>14</sup>

Three ladies, the joint owners of a car, advertised it for sale. A person called at their house and offered to pay an acceptable price. But, when he pulled out a cheque book, the ladies told him that the deal was over as they would not accept a cheque. He then persuaded them to believe that he was one *Hutchinson*, a leading businessman, and quoted an address and a telephone number. On verification of the particulars from a directory, the ladies gave him the car for a cheque. He resold the car to the defendant and absconded. The cheque proved worthless and the plaintiffs sued the defendant for the car or its value.

The defendant was held liable. In the opinion of the court the decision must depend upon the intention of the ladies. The question was with whom did they intend to contract, with the man present in their drawing room or with the real Hutchinson? Did the identity of Hutchinson or the physical presence of the man in the room preponderate? Can it be said that the *prima facie* predominance of the physical presence of the false Hutchinson identified by sight and hearing was over-borne by the identity of the real Hutchinson on the facts of the present case? In answer to these questions the court said that there could be no doubt that the offer which the plaintiffs made was one made solely to, and one which was capable of being accepted only by, the honest Hutchinson. So far as the rogue was concerned there was no offer made to him and consequently there could be no contract with him. His right to the car was no more than that of a thief or a finder and he could not convey a good title to the defendant.<sup>15</sup>

12. *Edmunds v Merchant Despatch Co*, (1883) 135 Mass 283, 286.

13. For a criticism of this decision see E.C.S. Wade, *Mistaken Identity in the Law of Contract*, 38 LQR 201, 204; A.L. Goodhart, *Mistake as to Identity in the Law of Contract*, (1941) 57 LQR 228, 241. See also 35 LQR 289.

14. (1961) 1 QB 31 (1960) 3 WLR 504 (CA). Noted in A.L.G.: *Mistake as to Identity in the Law of Contract*, (1961) 77 LQR 31; J.C. Hall: *New Developments in Mistake of Identity*, (1961) Camb LJ 86.

15. See also *Hardman v Booth*, (1862) 1 H&C 803; *Lake v Simmon*, 1927 AC 487 (HL); *Macleod v Kerr*, 1965 SLT 358 and *Car & Universal Finance Co Ltd v Caldwell*, (1965) 1 QB 525: (1964) 2 WLR 600 (CA), noted in 1966 Journal of Business Law, pp. 79 and 259.

### Where fraud does not lead to mistake of identity

In the dissenting judgment DEVLIN LJ emphasised the need for a new approach. In his view cases like these pose a problem of practical justice, and theoretical considerations such as whether the contract is void or voidable should not stand in the way of doing practical justice. Why should the title of the innocent buyer be made to depend on the state of a contract between third parties? It was this approach that found favour with the Court of Appeal in *Lewis v Avery*:<sup>16</sup>

Lewis, the plaintiff, had a car to sell. A man, described in the judgment as 'rogue', came along and introduced himself as Richard Green, a famous film actor. He tested and liked the car and offered a cheque. The plaintiff told him to wait till the cheque was cleared, but when his resistance was broken, he demanded proof of identity. The rogue produced a special pass of admission to a film studio which showed his photograph and the official stamp. This convinced the plaintiff and he allowed the car to be taken away for the cheque. The rogue lost no time in disposing of the car to an innocent buyer, the defendant. The worthless cheque came back and the plaintiff sued the defendant to recover his car.

The Court of Appeal held that the car was delivered under a contract voidable by reason of the fraud and the contract having not been avoided before the car passed into the hands of an innocent buyer, he acquired a good title. Lord DENNING felt that the facts of *Phillips v Brooks Ltd*,<sup>17</sup> *Ingram v Little*<sup>18</sup> and those of the present case were indistinguishable and that the contradictory decisions in these two earlier cases cannot be reconciled. In each case, his Lordship pointed out, an innocent seller is visited by a rogue, who by the usual tricks of his trade, convinces that he is a man of standing and credit and thereby induces the seller to part with his possession for a cheque. In each case he disposes of the goods to an innocent buyer. Whose failure has brought about this misfortune upon the two innocent parties? Should the title of the ultimate buyer be made to depend upon fine questions as to whether the fraud was committed before or after the contract was struck, or whether the mistake related to identity as opposed to attributes or whether the contract was void or voidable? Referring to these needless subtleties Lord DENNING said: "For instance, in *Ingram v Little*,<sup>19</sup> the majority of the court suggested that the difference between *Phillips v Brooks Ltd*<sup>20</sup> and *Ingram v Little* was that in *Phillips v Brooks* the contract of sale was concluded after the rogue made the fraudulent misrepresentation<sup>21</sup> whereas in *Ingram v Little* the rogue made the fraudulent representation before the

16. (1972) 1 QB 109: (1971) 3 WLR 603 (CA).

17. (1919) 2 KB 243.

18. (1961) 1 QB 31: (1960) 3 WLR 504 (CA).

19. *Ibid.*

20. (1919) 2 KB 243.

21. See (1961) 1 QB 51, 60: (1960) 3 All ER 337, 343.

contract was concluded. My own view is that in each case the property in the goods did not pass until the seller let the rogue have the goods.”

“Again it has been suggested that a mistake as to the identity of a person is one thing; and a mistake as to his attributes is another. A mistake as to identity, it is said, avoids a contract, whereas a mistake as to attributes does not. But this is a distinction without a difference. A man’s very name is one of his attributes. It is also a key to his identity. If then, he gives a false name, is it a mistake as to his identity? Or, a mistake as to his attributes? These fine distinctions do no good to the law.

As I listened to the arguments in this case, I felt it wrong that an innocent purchaser (who knew nothing of what passed between the seller and the rogue) should have his title depend on such refinements. After all he has acted with complete circumspection and in entire good faith; whereas it was the seller who let the rogue have the goods and thus enabled him to commit the fraud. I do not therefore accept the theory that a mistake as to identity renders a contract void.”

When the parties are present face to face, the presumption is that the contract is made with the person actually present, even though there is a fraudulent impersonation by the buyer representing himself as a different man than he is. This approach was heralded by PEARCE LJ and also by DEVLIN LJ in *Ingram v Little*, in support of which DEVLIN LJ quoted not only the English case of *Phillips v Brooks Ltd*, but also cases in the United States where:<sup>22</sup> “The courts hold that if A appeared in person before B, impersonating C, an innocent purchaser from A gets the property in the goods against B.”

PHILLIMORE LJ and MEGAW LJ also subscribed to the view that there was nothing in the conduct of the plaintiff to overthrow the presumption of contracting with the person who was present in person.<sup>23</sup>

### Where identity specially important

Where, however, the identity of the other party is of vital importance to the offeror, a mistake as to identity will prevent an agreement from arising. Importance of identity must depend upon the nature of the promise in each case. In *Said v Butt*<sup>24</sup>, for example:

The plaintiff knew that on account of his adverse criticism of some members of a theatre, he would not be allowed to be present at the first performance of a play at the theatre. A ticket was obtained for him by one of his friends without disclosing that it was for him. But the defendant,

22. This quotation is from CORBIN ON CONTRACTS, Vol 3, S. 602.

23. The same approach was adopted where a person by forgery of signature of a customer induced the banker to issue a draft which was ultimately received by an innocent person and it was held that the issuing bank must suffer this loss. *Citibank N.A. v Brown Shipley & Co Ltd*, (1991) 2 All ER 690.

24. (1920) 3 KB 497.

the managing director of the theatre, refused him admission on the night in question. And the plaintiff sued him for inducing breach of contract.

But it was held that there was no contract between him and the theatre. "The non-disclosure of the fact that the ticket was bought for the plaintiff prevented the sale of the ticket from constituting a contract, the identity of the plaintiff being in the circumstances a material element in the formation of the contract."

Yet another illustration is *Sowler v Potter*:<sup>25</sup>

The defendant was convicted for permitting disorderly conduct in a cafe. She subsequently assumed a false name and obtained from the plaintiff a lease of premises in the same neighbourhood with a view to conducting a restaurant therein. The plaintiff contended that if he had known her true identity he would never have granted the lease and the same was therefore void for mistake.

It was held that the consideration of the person with whom the plaintiff was entering into the lease was a vital element in that agreement so that the plaintiff having been mistaken with regard to the identity of the defendant, the lease was void *ab initio*.

In a German case,<sup>26</sup> a room was booked in a private hotel. When the plaintiff and his lady arrived, the hotelier discovered that they were affianced but not married. The room was refused. The hotelier was held not liable for damages for breach of contract: "The defendant, when accepting the plaintiff's booking, had acted on the assumption that he and his lady were a married couple, whereas in fact they were not. In view of the defendant's own feelings and the effect which it might have on other guests if they learned that the defendant rented out double rooms to unmarried couples, the mistake was a material one and negated consent."

### MISTAKE AS TO SUBJECT-MATTER

Another fact essential to every agreement is the identity or quality of the subject-matter of the contract. Mistake as to subject-matter may take various forms.

#### 1. Non-existent subject-matter

In the first place, the subject-matter may have ceased to exist before the contract was made. This happened in *Gustavus Couturier v Robert Hastie*:<sup>27</sup>

The defendant was employed to sell the plaintiff's cargo which was on voyage. After the defendant had sold the cargo to a third person, it was discovered that the cargo, having been damaged by bad weather, had

25. (1940) 1 KB 271.

26. Noted in H.R. Hablo, *Morality Vindicated*, (1975) SALJ 440.

27. (1856) 5 HL Cas 673: 10 ER 1065.

been sold at an intermediate port. The buyer repudiated the contract and the defendant, being a *del credere agent* was sued for the price.

But he was held not liable. Lord CRANWORTH said: "The contract plainly imports that there was something which was to be sold at the time of the contract, and something to be purchased." But as the goods had been totally lost before the contract was made, the contract was void *ab initio* (from the very beginning). On the same principle, the sale of a horse which, unknown to the parties, was dead at the time of the bargain and the sale of the life estate of a person who, unknown to parties, was dead at the time of the sale, would be void.

## 2. Mistake as to title or rights

"Corresponding to mistake as to the existence of subject-matter is mistake in cases where, unknown to the parties, the buyer is already the owner of that which the seller purports to sell to him. The parties intend to effectuate a transfer of ownership: such a transfer is impossible...."<sup>28</sup>

In such a case, however, equity only allowed the agreement to be set aside. This was affirmed by the House of Lords in 1867 in the great case of *Cooper v Phibbs*.<sup>29</sup> In that case an uncle had told his nephew, not intending to misrepresent anything but being in fact in error, that he (the uncle) was entitled to a fishery, and the nephew, after the uncle's death, acting in the belief of the truth of what the uncle had told him, entered into an agreement to rent the fishery from the uncle's daughter, whereas it actually belonged to the nephew himself. The House of Lords held that the mistake was such as not only to make the agreement voidable, but also liable to be set aside on such terms as the court thought fit to impose.

The principle was further explained by the Court of Appeal in *Solle v Butcher*<sup>30</sup> where DENNING LJ stated the position thus:

"All previous decisions on this subject must now be read in the light of *Bell v Lever Bros Ltd*<sup>31</sup>. The correct interpretation of that case, to my mind, is that once a contract has been made, that is to say, once the parties, whatever their inmost states of mind, have to all outward appearances agreed with sufficient certainty in the same terms on the same subject-matter, then the contract is good unless and until it is set aside for breach of some condition expressed or implied in it, or for fraud, or on some equitable ground. Neither party can rely on his own mistake to say it was a nullity from the beginning, no matter that it was a mistake

28. Lord ATKIN in *Bell v Lever Bros Ltd*, 1932 AC 161, 218 (HL). His Lordship cited *Cooper v Phibbs*, (1867) LR 2 HL 149: 16 LT 678 (HL), "where A agreed to take a lease of fishery from B, though contrary to belief of both parties at the time A was tenant for life of the fishery and B appears to have had no title at all". The agreement was set aside. But the decision is criticised by his Lordship.

29. (1867) LR 2 HL 149: 16 LT 678 (HL).

30. (1950) KB 671 (CA).

31. 1932 AC 161 (HL).

which to his mind was fundamental, and no matter that the other party knew he was under a mistake. *A fortiori* if the other party did not know the mistake, but shared it.”

In this case:

A landlord carried out repairs to a house which was with a tenant on a standard rent fixed in 1939. The tenant expressed the opinion that after the reconstruction the standard rent would not be applicable. If it was applicable the landlord could have increased it by notice to the tenant by taking into account the costs of improvement. Without giving such notice the tenancy was renewed in favour of the tenant for seven years on the increased rent. The tenant paid the increased rent for some time and then started proceedings for restoring the original rent and for recovering overpaid rent.

The court held that the standard rent was still applicable and the plaintiff was prevented from giving notice by the misrepresentation made by the tenant. It was liable to be set aside, but was not a nullity from the very beginning. “The parties agreed in the same terms on the same subject-matter. It is true that the landlord was under a mistake which was to him fundamental. But whether it was his own mistake or a mistake common both to him and the tenant, it is not a ground for saying that the lease was from the beginning a nullity.” His Lordship further pointed out that what the tenant said was not merely an expression of opinion but an unambiguous statement as to private rights and a misrepresentation as to private rights is equivalent to a misrepresentation of fact for this purpose.

This opinion has been expressly disapproved by the Court of Appeal in *Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd*.<sup>32</sup> The court applied the ruling in *Bell v Lever Bros Ltd*<sup>33</sup> to the facts of the case. The facts and decision in the *Great Peace* case have been discussed under the ruling in *Bell* case.

No contract would follow where though the buyer is not owner, the vendor also does not have the right to sell and the parties have mistakenly believed that he has the right.<sup>34</sup> Where a vendor purported to sell all his rights in a land, including the rights to mine minerals, the agreement was held void when it was subsequently found that the vendor’s rights simply did not include the right to mine. Without this right the land was worthless for the buyer whose only object was to work the mines.<sup>35</sup> A mistake of this kind must be reasonable in the circumstances. Where, for example, “the position was too notorious and well-known to all concerned in the locality that the

32. 2003 QB 679: (2002) 3 WLR 1617: 2002 EWCA Civ 1407 (CA). Considered by Adrian Chandler, James Devenney and Jill Poole, *Common Mistake: Theoretical Justification and Remedial Inflexibility*, 2004 JBL 34.

33. 1932 AC 161 (HL).

34. *Rani Kunwar v Madhub Baksh*, 132 IC 39; *U. Pan v Maung Po Tu*, AIR 1927 Rang 90.

35. *Ramchandra v Bisra Gonesh Chandra*, 39 IC 78.



tenants of an estate, which was the subject-matter of sale, had the right to sell Tendu leaves to whomsoever they pleased”, the buyer’s ignorance of this right was not reasonable and consequently the contract was valid.<sup>36</sup> In a case before the Bombay High Court:<sup>37</sup>

C mortgaged the property of his brother L.M. fraudulently representing himself to be L.M. The defendant, who was the mortgagee transferred his interest to the plaintiff. The plaintiff insisted that the owner of the property should join the transfer and C again committing the same fraud, executed the transfer. On discovering the fraud, the plaintiff sued the defendant for the return of the purchase money.

It was held that he must succeed. “Both the parties being in the belief that the real owner had joined in the transfer were under a mistake of fact essential to the agreement which was, therefore, avoided under Section 20.”

### 3. Different subject-matters in mind

Where the parties, due to a reasonable mistake of fact, have different subject-matters in mind, the agreement will be void for want of true consent. As, for example, in *Raffles v Wichelhaus*:<sup>38</sup>

The defendant bought of the plaintiff a quantity of Surat Cotton “to arrive *ex Peerless* from Bombay”. Two ships with the name Peerless sailed from Bombay, one in October, which the defendant had in mind and the other in December which the plaintiff had in mind.

The court said: “the defendant meant one Peerless and the plaintiff another. That being so, there was no *consensus ad idem* and therefore no binding contract.”

Where the buyer believed that the land was being sold at the stated price per bigha and the seller thought the price was applicable per *kanal*, it was held that there was no agreement on the matter of an essential fact and, therefore, no contract.<sup>39</sup>

### 4. Mistake as to substance of subject-matter

Another kind of mistake as to subject-matter may relate to its substance, nature or quality. The parties may be mistaken as “to the existence of some fact or facts forming an essential and integral element of the subject-matter.”<sup>40</sup>

36. *State of Orissa v Khan Saheb Mohd Khan*, AIR 1961 Ori 75.

37. *Ismail Allarkhia v Dattatraya*, ILR (1916) 40 Bom 638.

38. (1864) 2 H&C 906: 159 ER 375. In a sale by auction, the seller intending to sell tow and the buyer intending to buy hemp and the jury found that the two commodities were commercially different, the seller could not recover the price, *Scriven Bros & Co v Hindley & Co*, (1913) 3 KB 564.

39. *Tarsem Singh v Sukhminder Singh*, (1998) 3 SCC 471. The court added that no part of the agreement is enforceable unless it is severable from the void features and is capable of supporting an independent contractual tie.

40. See HALSBURY’S LAWS OF ENGLAND, (2nd Edn, Vol 23), p. 135 and para 89.

The decision of the Privy Council in *Seikh Bros Ltd v Ochsner*,<sup>41</sup> on appeal from Kenya and decided under Section 20 of the Indian Contract Act, provides an instructive illustration.

The appellant-company, the lessor of a forest in Kenya, granted a licence to the respondent to cut, process and manufacture all sisal growing in the forest. The respondent, in return, undertook to manufacture and deliver to the appellant 50 tons of sisal fibre per month. But it turned out that the leaf potential of the sisal area was not sufficient to permit the manufacture of the stipulated quantity and the respondent was sued for the breach.

The agreement was held to be void. Their Lordships, relying upon the statements in *Bell v Lever Bros Ltd*,<sup>42</sup> came to the conclusion that “having regard to the nature of the contract, which was a kind of joint adventure, it was the very basis of the contract that the sisal area should be capable of producing an average of 50 tons a month throughout the term of the licence, and the mistake was as to a matter of fact essential to the agreement”.<sup>43</sup>

On the same principle an agreement for the sale of land was held void as, unknown to the parties, the land had been notified for acquisition at the time of the contract.<sup>44</sup> An agreement to compromise a suit already decided in favour of the plaintiff, but unknown to the parties, is void for the same reason.<sup>45</sup> The acquisition of a land, which is the subject-matter of a sale, after the contract is made will not upset the contract,<sup>46</sup> so also a contract for the sale of goods on certain price cannot be avoided by the seller on the ground that a new excise tax has made the goods dearer and the buyer is unwilling to pay the extra price.<sup>47</sup> This will be so even if the parties have made the bargain in the expectation that there will be no upward revision of taxes.<sup>48</sup> Where the expectations of the parties are frustrated by subsequent events, their contract may fall under Section 56 but cannot be declared void *ab initio* under Section 20.<sup>49</sup> In such cases there is no mistake as to existing facts. The distinction was emphasised by the Calcutta High Court<sup>50</sup> in a case where a contract was entered into upon the assumption that the Jute Control Order, which was due to expire, would be continued and extended, but it was not extended. Rejecting the plea of mistake, HARRIES CJ observed as follows: “The difference between a mistake as to an existing fact and a mistake as to a future occurrence is clear and the consequences are very

41. 1957 AC 136: (1957) 2 WLR 254 (PC).

42. 1932 AC 161 (HL).

43. At p. 147.

44. *Nursing Dass Kothari v Chuttoo Lall Misser*, ILR (1923) 50 Cal 615.

45. *Bibee Solomon v Abdool Azeez*, ILR (1881) 6 Cal 687.

46. *Jodha Mal Kuthalia v Associated Hotels of India Ltd*, AIR 1950 Lah 106.

47. *Chin Gwan & Co v Adamjee Haji Dawood & Co*, AIR 1939 Rang 79.

48. *Babsheetti v Venkatramana*, ILR (1879) 3 Bom 154.

49. *Shree Chand Daga v Sohanlal Daga*, AIR 1943 Cal 257.

50. *Ibid.*

different. A mistake as to an existing fact will render the contract void *ab initio*. In short, if the parties have entered into a contract upon such a mistake, there is and never has been any contract at all between them. On the other hand, if the mistake is as to some future event, a binding contract is entered into between the parties. The contract may be avoided or rescinded at some future date if the expected event does or does not happen.”

The fact about which the parties are mistaken must be “essential” to their agreement. A mistake as to a collateral fact, which leaves the subject-matter substantially what it was supposed by the parties to be, does not negative the contract. Thus the lease of a mining estate which was known by reputation to measure 100 bighas was not regarded as void on discovering that the area was actually less. “The exact area of 100 bighas more or less was not essential for the colliery purpose for which agreement was arrived at and, therefore, there was no common mistake with regard to an essential fact.”<sup>51</sup> Similarly, a contract for the sale of goods “to arrive by a certain ship” is not void, if the ship does not bring the goods.<sup>52</sup> Since, land acquired under statutory power cannot be divested in favour of any person, much less in favour of the person from whom it was acquired, any such divesting under mistaken notion of the rights was held to be void. The agreement was also opposed to public policy.<sup>53</sup> Handing over by Zila Parishad of the right to collect fee to the highest bidder was held to be against law.<sup>54</sup>

A road builder, while tendering, calculated his costs on the basis that necessary material would be available from a nearby quarry. But that turned to be wrong. He had to go to more distant quarry. That cost him more. The court said that this was not a mistake which would enable him to avoid the contract. A special clause in the contract carried a provision that the contractor had to make his own arrangement for obtaining material.<sup>55</sup>

#### *Mistake as to quality of subject-matter as distinguished from substance*

A mistake as to the quality of the subject-matter as distinguished from its substance may not render the agreement void. *Smith v Hughes*<sup>56</sup> is well-known for this distinction between quality and substance.

51. *Soorath Nath Banerjee v Babasanker Goswami*, AIR 1929 Cal 547.

52. *Bhaiyal Chaturbhai Patel v Kalyanrai*, 63 IC 952.

53. *Seth Srenikbhai Kasturbhai v Seth Chandulal Kasturchand*, AIR 1997 Pat 179.

54. *Surendra Kumar Rai v Zila Parishad Jhansi*, AIR 1997 All 387, the collections were not accounted for by the person, that amount was held to be recoverable. But the amount could not be recovered as arrears of land revenue. In another similar case, *Mahesh Chandra v Zila Panchayat Mainpuri*, AIR 1997 All 248, the Parishad authorised a bidder the right to remove and dispose of dead animals. The amount which became due from him could not be recovered as arrears of land revenue. Such authority can be given to the Collector only under a statute. *State Industrial and Investment Corpn of Maharashtra Ltd v Narang Hotels (P) Ltd*, AIR 1995 Bom 275, a mistake as to whether a particular type of industry was included in the subsidy scheme of a backward area did not make the contract to provide subsidy by the Financial Corporation voidable.

55. *State of Karnataka v Stellar Construction Co*, AIR 2002 Kant 6: (2002) 5 Kant LJ 474.

56. (1871) LR 6 QB 597 (DC).

The defendant wanted to buy old oats for his horses. The plaintiff showed him the sample of the oats he had, but said nothing about their age. The defendant kept the sample for twenty-four hours and then placed an order for the oats. After a portion of them was delivered to him he found that they were new and, therefore, rejected them on the ground that he was mistaken about their quality.

But the court could find no ground entitling the buyer to reject. COCKBURN CJ summed up by saying: "All that can be said is that the two minds were not *ad idem* as to the age of the oats; they certainly were *ad idem* as to the sale and purchase of them."<sup>57</sup>

The effect of mistake as to quality was further explained by the House of Lords in *Bell v Lever Bros Ltd*<sup>58</sup> where Lord ATKIN said: "Mistake as to quality of the thing contracted for raises more difficult questions. In such a case a mistake will not affect assent unless it is the mistake of both parties, and is as to existence of some quality which makes the thing without the quality essentially different from the thing as it was believed to be."<sup>59</sup> The facts of the case were as follows:

Lever Bros. appointed one Bell as a managing director for five years on an annual salary of £8000 to manage one of their subsidiaries in Africa. Much before the expiry of this term his services had to be dispensed with on account of the merger of the subsidiary with a third company. Bell agreed to retire on a compensation of £30,000. After this sum was paid, it was discovered that during his term of service, Bell had made secret profits and was, therefore, guilty of breach of duty which entitled the company to dismiss him without compensation. The company, therefore, claimed the return of the money on the ground *inter alia* that it was paid under a mutual mistake of fact.

But their action failed. It was held by a majority "that the mutual mistake related not to the subject-matter, but to the quality of the service contract". The plaintiffs contended that they agreed to pay compensation on the assumption that the service contract was one which could not be terminated without compensation, whereas the true fact was that the defendant could have been dismissed without compensation. Referring to this contention, Lord ATKIN said:<sup>60</sup> "I have come to the conclusion that it would be wrong to decide that an agreement to terminate a definite specified contract is void if it turns out that the agreement had already been broken and could have been terminated otherwise. The contract of release is the identical contract in both cases, and the party paying for release gets exactly what he bargains for. It seems immaterial that he could have got the same result in another way, or that if he had known the true facts he would not have entered into

57. *Smith v Hughes*, 1871 LR 6 QB 597, 606.

58. 1932 AC 161 (HL).

59. *Bell v Lever Bros Ltd*, 1932 AC 161, 218 (HL).

60. At pp. 223–24.

the bargain." The mistake was mutual as the jury found that at the time of negotiating the compensation agreement the defendant had not in mind his breaches of duty.<sup>61</sup>

This ruling was applied by the Court of Appeal in *Great Peace Shipping Ltd v Tsaviris Salvage (International) Ltd*.<sup>62</sup> In this case two vessels were hired to reach for a stricken vessel to save the life of its crew. It was believed at the time of the contract that the two vessels were in close proximity to each other, located at a distance of 35 miles. Unknown to both the parties, the two vessels were at a distance of 410 miles and it would have taken 39 hours for the rescue vessels to reach the stricken vessel. The defendants looked for other vessels which they got and they cancelled the contract. This was held to be a breach of the contract. The defence of mistake failed. The court said that the mistake as to the distance between the two vessels had not rendered the services that the distant vessel was able to provide something essentially different from those which the parties had agreed. The vessel would have arrived in time to provide several days of escort service. The fact that the vessels were further apart than both the parties had appreciated did not mean that it was impossible to perform the contractual venture.

In a sale of table napkins under a mistake that they were of historic value, it has been suggested that the transaction could be regarded in two ways:

"1. The parties have intended to buy and sell table-linen: in this case a mistake as to its age or value would be irrelevant—it would be a mistake as to quality and therefore not an operative mistake.

2. The parties may have intended to buy and sell a Carolean relic, i.e., a mistake as to substance; in that case their mistake would be fundamental and make the contract void."<sup>63</sup>

### Misapprehension as to parties' respective rights

The Court of Appeal has reiterated in *Magee v Pennine Insurance Co Ltd*<sup>64</sup> that a common misapprehension either as to facts or as to the parties' relative and respective rights will not make the contract void but only voidable provided that the misapprehension was fundamental and that the party seeking to set aside was not himself at fault. The facts of the case were:

The plaintiff bought a car for his 18-year-old son. The son had a provisional driving licence. The proposal form for the insurance of the car was filled by the manager of the firm from where the car was bought and he happened to state that the plaintiff had a provisional driving licence when in fact he had none. The son made an accident and the plaintiff claimed

61. See also *Kennedy v Panama New Zealand and Australian Royal Mail Co*, LR 2 QB 580, where it was held that a material misrepresentation in a company's prospects does not make the shares an applicant obtained a different thing in substance from those which he applied for.

62. 2003 QB 679: (2002) 3 WLR 1617: 2002 EWCA Civ 1407 (CA).

63. *Nicholson & Venn v Smith-Marriott*, (1947) 177 LT 189 (KB).

64. (1969) 2 QB 507: (1969) 2 WLR 1278 (CA).

£600 for it. The company compromised the claim undertaking to pay £385. But before paying, the company came to know of the misstatement and declined to pay.

The agreement of compromise was entered into under the common and fundamental mistake that the original policy was valid and binding, when in fact it was voidable for the misstatement. In *Bell v Lever Bros*, the original contract of employment was supposed by the parties to be binding when in fact it was terminable for the breaches of duty. The only difference was that in *Bell* the compromise amount had already been paid. The Court of Appeal held that the agreement was liable to be set aside on the ground that the parties were mistaken as to a fundamental assumption.

In another similar case before the Court of Appeal<sup>65</sup> after a contract had been made for the purchase of a property at a relatively high price because of its suitability for occupation and redevelopment, the property was listed by the State as being of architectural or historic interest. The purchaser sought to avoid the contract on the ground of common mistake because unknown to the parties at the time of the contract the property was already under consideration for the purpose of listing. But he was not allowed to do so. The property was listed only after the contract had already been signed. No relief was allowed under the doctrine of frustration also. Listing was an inherent risk, of which every purchaser should be regarded as being aware. The plaintiffs had been aware that the risk existed and it was a risk they had to bear. It could not therefore be said that the performance of the contract that would be called for would, in consequence of the listing, be radically different from that which had been undertaken by the parties. The principle would, therefore, seem to be that a contract is void *ab initio* if its subject-matter is essentially and radically different from what both contracting parties believed it to be, provided that the party relying on the mistake has reasonable grounds for his mistaken belief.<sup>66</sup>

To the same effect is the decision of the Supreme Court in *Kalyanpur Lime Works Ltd v State of Bihar*:<sup>67</sup>

The State of Bihar granted the lease of a hill to one K. Co for quarrying limestone. The lease was not assignable to anyone else without the approval of the Government. K. Co went into liquidation and its liquidator assigned the lease to another without the approval of the State. This provoked the State to forfeit the lease and to offer it to the plaintiffs for a period of 20 years. K. Co started proceedings against the forfeiture and the same was held by the Privy Council to be invalid. K. Co was

65. *Amalgamated Investment & Property Co Ltd v John Walker & Sons Ltd*, (1977) 1 WLR 164 (CA).

66. *Associated Japanese Bank v Credit Dul Nuro S.A.*, (1989) 1 WLR 255 (QB). The principle of this case was applied in *William Sindall plc v Cambridgeshire County Council*, (1994) 1 WLR 1016 (CA) where the party was held to be entitled to rescind the contract for a common mistake as to the existence of a sewer.

67. AIR 1954 SC 165; *Dalmia Jain & Co Ltd v Kalyanpore Lime Works Ltd*, AIR 1952 Pat 393.

restored to its lease and vacated after the expiry of its full term, that is after about 11 years. The plaintiffs now claimed the lease in terms of the agreement made before the forfeiture was declared to be invalid. But the Government allotted the same to another person and the plaintiff started the present proceedings. The Supreme Court held that the agreement was not void by reason of any mistake. The Government had the right to forfeit and to re-allot. The forfeiture having been declared void, its right was not wholly gone; it was restricted only by reason of the lease which had still several years to run. In these circumstances it might have been open to the plaintiffs to repudiate the contract if they so liked, but the defendant could not certainly plead that the contract was void on the ground of mistake and refuse to perform that part of the agreement which it was possible for it to perform.

Similarly, where the Government allotted certain plots assuming that the sitting tenants would vacate them, but they refused to oblige, it was held by the Allahabad High Court<sup>68</sup> that "Section 20 does not apply to a case where the contracting parties have made no mistake as to any fact existing at the making of the contract and it is complained that one of them is unable to carry out his part of the contract on account of the unexpected refusal of a third person to carry out his obligation under another agreement."

### MISTAKE AS TO NATURE OF PROMISE

The principle is well established by authorities that when a deed of one character is executed under the mistaken impression that it is of a different character, then it is wholly void and inoperative.<sup>69</sup> Thus where a gift deed is signed under the impression that it is only a power of attorney, the deed is inoperative.<sup>70</sup> If a mistake of this kind is common to both parties, the agreement is void under Section 20, the parties being mistaken about the very nature of the promise. But more frequently a mistake of this kind is brought about by the fraud of one party. One of the parties, being under a duty to do so, fails to disclose to the other the true nature of the document and thereby induces him to sign the same under the belief that he is signing some other instrument of a different nature. In such a case there is no real agreement as the consent is nullified by the mistake. This distinction has been thus indorsed by the Supreme Court:<sup>71</sup> "Though a contract or other transaction induced by fraud is not void, but only voidable at the option of the party

68. *U.P. Government v Lala Nanhu Mal Gupta*, AIR 1960 All 420.

69. *Appanna v Jami Venkatappadu*, AIR 1953 Mad 611. See also *Mandakini Pundalik Salker v Chandrasen Raiker*, AIR 1986 Bom 172 where the allegation that unknown to him the girl whom he married was illegitimate of her parents was not proved and even if proved, the court held that it would not have been a material fact. *Prem Singh v Birbal*, (2006) 5 SCC 353: (2006) 2 KLT 863: (2006) 5 Mah LJ 441, fraudulent representation as to the character of the document makes it void, when it is as to its contents, the document is voidable.

70. *Sarat Chandra v Kanailal*, AIR 1929 Cal 786.

71. *Dularia Devi v Janardan Singh*, 1990 Supp SCC 216: AIR 1990 SC 1173: 1990 All LJ 245.

defrauded, there is a clear distinction between fraudulent misrepresentation as to the character of the document as opposed to its contents. While in the former case the transaction is void, in the latter it is only voidable."

There is not the type of "consent" as is required by Section 13. In a case of this kind before the Patna High Court:<sup>72</sup>

The plaintiff appointed the defendant to look after his cultivation and his affairs, as he had become too old to manage them himself. The defendant asked him to grant him a lease of his land. The plaintiff agreed to it and placed his thumb-impression upon a deed which was in fact a gift of the land.

The court held the deed to be void *ab initio*.

In a similar case before the Madhya Pradesh High Court,<sup>73</sup> an illiterate lady who was the owner of farming land generally consulted her uterine brother on all important matters. Once, finding that some strangers were occupying her lands, she approached her brother, who advised that an application should be made to the Collector. He took her to the Collector's office and obtained her thumb-impressions upon some blank papers. These were then registered as sale deeds in the name of some persons. On discovering her mistake she challenged the transaction and obtained an order that the transaction was void and that she was still the owner of her lands. The court said: "There is a clear distinction between a fraudulent misrepresentation as to the character of a document and as to its contents. Where the misrepresentation is as to the character of the document, the transaction is wholly void."

This distinction was developed by the Supreme Court in *Ningawwa v Byrappa Shiddappa Hireknabar*<sup>74</sup> following the principle enunciated in *Foster v Mackinnon*.<sup>75</sup> Following these rulings again in another case of the same kind, where an illiterate woman was called upon by her son-in-law and his brothers to put her thumb-impression upon two stamp-papers telling her that she was thereby gifting her agricultural land to her daughter, who was her only child and one of the papers was a sale deed to them by which they became the registered owners of the land, the Supreme Court held that the document was a nullity by reason of the fraudulent misrepresentation as to its character.<sup>76</sup>

An agreement to pay money in final settlement under a contract of insurance in which there were false statements has been held by the Court of Appeal to be voidable at the option of the insurance company.<sup>77</sup>

72. *Raja Singh v Chaichoo Singh*, AIR 1940 Pat 201.

73. *Partap v Puniya Bai*, AIR 1977 MP 108.

74. AIR 1968 SC 956, 958: (1968) 2 SCR 797.

75. (1869) LR 4 CP 704.

76. *Dularia Devi v Janardan Singh*, 1990 Supp SCC 216: AIR 1990 SC 1173: 1990 All LJ 245.

77. *Magee v Pennine Insurance Co Ltd*, (1969) 2 QB 507: (1969) 2 WLR 1278, considered *Effective Mistake in Law of Contract*, (1963) 85 LQR 454. See also *Kaur v Chief Constable, Hampshire*, (1981) 1 WLR 578, where it was held that a mistake as to the price induced by



### Where the contract fails to express parties' intention

Where an agreement as finally made fails to express or embody the agreement between the parties as originally made, it can be had rectified so as to bring it in accord with the intention of the parties. An easy illustration is the decision of the Court of Appeal in *Hartog v Colin and Sheilds*:<sup>78</sup>

The defendants contracted to sell to the plaintiff 3000 Argentine hare skins, but by a mistake they offered the goods at so much per *pound* instead of so much per *piece*. The price per piece was roughly one-third that of a pound. The negotiations preceding the agreement took place on the basis of price per piece and that was also the usual practice of the trade. The buyers sued for the goods.

SINGLETON LJ felt satisfied "that it was a mistake on the part of the defendants which caused the offer to go forward in that way, and I am satisfied that anyone with any knowledge of the trade must have realised that there was a mistake. ... The offer was wrongly expressed, and the defendants by their evidence, and by the correspondence, have satisfied me that the plaintiff could not have reasonably supposed that the offer contained the offeror's real intention."

If relief of this kind was not allowed the result would be that one party would take an unconsentious advantage of the mistake of the other known to him. The Calcutta High Court followed this principle in granting relief in *New India Rubber Works (P) Ltd v Oriental Fire & General Insurance Co Ltd*.<sup>79</sup>

A policy of insurance, which had expired, covered risks arising out of fire, riot and strike. The company sent a renewal form to the assured showing the premium for the above risks. The assured sent lesser amount being equal to cover the fire risk only. The company issued a policy in usual terms covering the risks of fire, riot and strike. The factory was destroyed by fire due to riot. The company contended that in so far as the policy purported to cover the risk of riot and strike, it was void for mistake.

It was held that the company was entitled to raise this defence. The court considered the principles of equity under which documents executed under mistake are allowed to be rectified and that in reference to an insurance policy such rectification would be possible even after the loss has occurred because equity treats as done that which ought to have been done. The court then considered the effect of Section 26 of the Specific Relief Act, 1963, which provides that an instrument can be rectified if through fraud or a mutual mistake of the parties, the contract does not express their real intention. The

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wrong marking was not so fundamental as to destroy the validity of the contract of sale, but merely rendered it voidable.

78. (1939) 3 All ER 566.

79. (1969) 1 Comp LJ 153 (Cal).

court held that where on account of an error on the part of a party a written document fails to express their common intention it will be a case of mutual mistake. The court further pointed out that the defence of mutual mistake can be raised even where the document has become redundant by reason of the occurrence of the loss and there is nothing left to be rectified, for otherwise the assured will be allowed to take the advantage of a mistake which if pointed out would have been rectified at the proper time. The court relied upon its own earlier decision<sup>80</sup> where the defendant was allowed to seek the rectification of a conveyance in which he by mistake happened to include his homestead when that was not the intention of the parties.

The principles relating to this matter have recently been re-examined by the Court of Appeal in *Joselyne v Nissen*,<sup>81</sup> where the court cited a passage from an earlier judgment,<sup>82</sup> wherein it was observed that "it is not sufficient to show that the written instrument does not represent their common intention unless positively also one can show what their common intention was". The facts of the case were:

The plaintiff, who shared a house with his daughter, proposed that she should take over his car-hire business. It was made clear in the very early stage of negotiations that if the proposal was accepted, the daughter should pay all the household expenses, including the electricity, gas and coal bills due in respect of the part of the house occupied by her father. The written contract which followed from these discussions, however, failed to impose any liability on the daughter in respect of the household charges. After honouring the oral agreement for some time, she refused to meet the expenses although she continued to draw the profits of the business.

The plaintiff was held entitled to rectification so as specifically to impose that liability on the daughter. One of the difficulties was the remarks of DENNING LJ in an earlier case,<sup>83</sup> to the effect that mere common intention is not sufficient, it must have found expression in an outward agreement. He said: "There could be no certainty at all in business transactions if a party who had entered into a firm contract could afterwards turn round and claim to have it rectified on the ground that the parties intended something different. He is allowed to prove if he can, that they *agreed something different*."<sup>84</sup>

Referring to this passage RUSSEL LJ commented that if this means to suggest that an antecedent concluded contract is necessary, it would be contrary to the views in *Crane v Hegeman Harris Co Inc*.<sup>85</sup> The view supported by

80. *Mahendra Nath Mukherjee v Jogendra Nath Roy Chaudhury*, (1897–98) 2 CWN 260.

81. (1970) 2 QB 86; (1970) 2 WLR 509 (CA).

82. SIMMONDS J in *Crane v Hegeman Harris Co Inc*, (1971) 1 WLR 1390.

83. *Frederick E. Rose (London) Ltd v William H. Pim. Junior & Co Ltd*, (1953) 2 QB 450 (CA).

84. See *Lovell and Christmas v Wall*, (1911) 104 LT 88, 93 per Lord COZENS HARDY MR and per BUCKLEY LJ but not that they *intended* something different.

85. (1971) 1 WLR 1390.

other judgments is that there should be a convincing proof of an outward expression of accord.

Centrovincial's solicitors invited Merchant Investors to agree to the appropriate rental value of £65,000 per annum at the review date of 25 December 1982 which should have read £12,600 but Merchant Investors were not aware of the mistake. Merchant Investors agreed to the figure of £65,000 per annum. Centrovincial contended that no contract was formed because of mistake and Merchant Investors contended that a contract had been formed. It was held that it is a well-established principle that ordinarily an offer, where unequivocally accepted according to its precise terms, will give rise to a legally binding agreement as soon as acceptance is communicated to the offeror and cannot thereafter be revoked without the consent of the other party. Although the law is concerned with the objective appearance as well as the actual fact of agreement, if the intention of the parties is clear then their intention will prevail over any objective appearance.<sup>86</sup>

Where neither party had disclosed his intention as to the effect of the agreement but coincidentally both entertained the same thought as to the effect of their bargain, it was held that such undisclosed intention was irrelevant for the purposes of interpretation of their contract. It is necessary that each party should know what is agreed at the time the contract is made.<sup>87</sup>

### Documents mistakenly signed or non est factum

The defence of *non est factum* enables a person who has signed a contract to say that it is not his document because he signed it under some mistake. It was evolved by the courts to relieve illiterate or blind people from the effect of a contract which they could not read and which was not properly explained to them.<sup>88</sup> But subsequently it was extended to others. This extension occurred through the judgment of BYLES J in *Foster v Mackinnon*:<sup>89</sup>

"It seems plain, on principle and on authority, that, if a blind man, or a man who cannot read, or who for some reason (not implying negligence) forbears to read, has a written contract falsely read over to him, the reader misreading it to such a degree that the written contract is of a nature altogether different from the contract pretended to be read from the paper which the blind or illiterate man afterwards signs; then, at least if there be no negligence, the signature so obtained is of no force. And it is invalid not merely on the ground of fraud, where fraud exists but on the ground that the mind of the signer did not accompany the signature;

86. *Centrovincial Estates Plc. v Merchant Investors' Assurance Co Ltd*, 1983 Com LR 158.

87. *New Hampshire Insurance Co v MGN*, The Times, July 25, 1995 (CA).

88. *Noorudeen v Umairathu Beevi*, AIR 1998 Ker 171, signature of blind person by telling that the document was a hypothecation deed whereas in fact it was a sale deed of property, nullity.

89. (1869) LR 4 CP 704.

in other words, that he never intended to sign and therefore in contemplation of law never did sign, the contract to which his name is appended.”

The learned judge did not make any distinction between mistake as to the nature or character of the contract as opposed to its terms, for in a later part of his judgment he said: “But the position that, if a grantor or covenantor be deceived or misled as to the *actual contents* of the deed, the deed does not bind him, is supported by many authorities.”<sup>90</sup>

The facts of the case were that a person was induced to sign the back of a paper, the face of which was not shown to him, and he was told that it was an ordinary guarantee the like of which he had signed before and under which no liability came to him, when, in fact, the paper was a bill of exchange and he was sued by a holder in due course as an indorser.

The court held that “the defendant never intended to sign that contract or any such contract. He never intended to put his name to any instrument that then was or thereafter might become negotiable. He was deceived not merely as to the legal effect, but as to the actual contents of the document. It was as if he had written his name on a sheet of paper for the purpose of franking a letter, or in a lady’s album, or on an order for admission to the Temple Church, or on the flyleaf of a book, and there had already been, without his knowledge, a bill of exchange or a promissory note payable to order inscribed on the other side of the paper.”

The principle of this case has been with some qualification affirmed by the House of Lords in *Gallie v Lee*.<sup>91</sup>

Mrs G, a widow, then aged seventy-eight years, wanted to help her trusted nephew and intended to transfer to him her house on the condition that he was to permit her to reside there for the rest of her life and she handed the title deeds to him. The nephew came to her with one Lee and Lee told her to sign a document saying that it was a deed of gift to the nephew and everything was in order. She had broken her spectacles so she could not read. She put her signature which was witnessed by her nephew. The document was an assignment in favour of Lee. He mortgaged the house with the building society and, having defaulted in payment, the society claimed possession. She pleaded *non est factum*.

The House of Lords, affirming the decision of the Court of Appeal, held that she was bound by the contract. It was only voidable by reason of the misstatements made by Lee, but it was too late to avoid once the building society had advanced a sum of money on the house in good faith. In her own statements to the court she said that she thought that her nephew and Lee would raise money on the house and that she would do anything to help her nephew. She was not, therefore, mistaken about the character of

90. See *Edwards v Brown*, (1863) 2 H&C 175: 9 LJ (OS) Ex 84.

91. (1970) 3 WLR 1078 (HL).

the document. The only thing was that it was put to a use which she did not expect. Relying on this evidence in the Court of Appeal SALMON LJ felt that she would have executed the assignment to Mr Lee even if the transaction had been properly explained to her. Lord DENNING MR reached the same conclusion but was not prepared to be fettered by the distinction between character and contents. But Lord HODSON was not prepared to accept this rejection of a principle which is supported by authorities and is sound in principle. “The distinction is a valid one in that it emphasises that points of detail in the contents of a document are not to be relied on in support of a plea of *non est factum*. Lord DENNING MR did, however, demonstrate that using the words as terms of art for test purposes may produce ludicrous results; e.g., a mistake as to the amount of money involved may be described as a mistake as to contents although the difference between two figures may be so great as to produce a document of an entirely different character from the one the signer intended.”

His Lordship further pointed out that the plea of *non est factum*, requires clear and positive evidence before it can be established, and cited with approval the statement of DENOVAN LJ<sup>92</sup> that “the plea of *non est factum* is a plea which must necessarily be kept within narrow limits”. To take an example, the man who in the course of his business signs a pile of documents without checking them takes the responsibility for them by appending his signature. It would be surprising if he was to be allowed to repudiate one of those documents on the ground of *non est factum*. The person signing has to take care.<sup>93</sup>

Lord WILBERFORCE emphasised that the law in this respect must retain flexibility because it has to reconcile two conflicting objectives: relief to a signer whose consent is genuinely lacking; and protection to innocent third party who have acted on an apparently regular and properly executed document. Trying to work out the principles on which the plea of *non est factum* should be admissible, his Lordship said: “In my opinion, a document should be held to be void (as opposed to voidable) only when the element of consent to it is totally lacking, i.e. more concretely, when the transaction, which the document purports to effect is essentially different in substance or in kind from the transaction intended. Many other expressions, or adjectives could be used—‘basically’, or ‘radically’ or ‘fundamentally’.”

His Lordship then added three qualifications to the principle. Firstly, in the case of fraud, the principle of *Foster v Mackinnon* will apply and the transaction would be void. Secondly, a man cannot escape from the consequences, as regards innocent third parties, of signing a document, if being

92. *Muskhan Finance Ltd v Howard*, (1963) 1 QB 904 (CA).

93. The Supreme Court has similarly laid down in *Bihar State Electricity Board v Green Rubber Industries*, (1990) 1 SCC 731: AIR 1990 SC 699 that a person who signs a document which contains contractual terms is normally bound by them though he had not read them or was ignorant of precise legal effects.

a man of ordinary education and competence, he chooses to sign it without informing himself of its purports and effect. Thirdly, there is the case where the signer has been careless, in not taking ordinary precautions against being deceived.<sup>94</sup>

Commenting on this case it is observed in CHITTY ON CONTRACTS:<sup>95</sup> “The law on this subject was completely reviewed and restated by the House of Lords in *Saunders v Anglia Building Society*<sup>96</sup> and the distinction between the character or nature of a document and the contents of the document was rejected as unsatisfactory. It was stressed that the defence of *non est factum* was not lightly to be allowed where a person of full age and capacity had signed a written document containing contractual terms. But it was nevertheless held that in exceptional circumstances the plea was available so long as the person signing the document had made a fundamental mistake as to the character or effect of the document. Their Lordships appeared to have concentrated on the disparity between the effect of the document actually signed and the document as it was believed to be rather than on the nature of the mistake, stressing that the disparity must be ‘radical’, ‘essential’, ‘fundamental’ or ‘very substantial’.”

The Supreme Court of India considered the principle of *Foster v Mackinnon* in *Ningawwa v Byrappa Shiddappa Hirekurbabar*<sup>97</sup> and concluded on the facts that where a husband obtained the signature of his wife to a gift deed without making any misrepresentation as to its character, but subsequently included two more plots in the deed, the transaction was only voidable and not void.

The Supreme Court did not approve the finding of the arbitrator that the signature was mistakenly affixed on the document and therefore not binding. The court said that when a person signs a document, the presumption is that he has read the document properly and understood it and only then affixed his signature unless there is a proof of force or fraud. Such a presumption is stronger in the case of businessmen. There was no allegation of force or fraud in the present case.<sup>98</sup>

## LIMITATIONS

Mistake operates to avoid an agreement subject to the following limitations:

94. The principle of *Foster v Mackinnon*, (1869) LR 4 CP 704 has been followed in *Sanni Bibi v Siddik Hossain*, AIR 1919 Cal 728 and *Brindaban Mishra Adhikary v Dhurba Charan Roy*, AIR 1929 Cal 606 and considered in *Ningawwa v Byrappa Shiddappa Hireknabar*, AIR 1968 SC 956, 958: (1968) 2 SCR 797.
95. 194–95 (15th Edn) Vol 1, Chap 5 under S. 343, cited by S.S. SUBRAMANI J, in *Selvaraju Kounder v Sahadeva Kounder*, 1997 SCC OnLine Mad 126: (1997) 2 LW 197.
96. (1970) 3 WLR 1078 (HL).
97. AIR 1968 SC 956: (1968) 2 SCR 797. An illiterate woman signing under the impression that it was wakf, when, in fact, it was a sale deed. Held, void, *Ashok Kumar v Gaon Sabha*, AIR 1981 All 222.
98. *Grasim Industries Ltd v Agarwal Steel*, (2010) 1 SCC 83.

## 1. Mistake of both parties

Under Section 20 an agreement is void by reason of mistake when both parties are mistaken as to a matter of fact essential to the agreement. This is further supplemented by the declaration in Section 22 that "a contract is not voidable merely because it was caused by one of the parties to it being under a mistake as to matter of fact". Thus, where the Government sold by auction the right of fishery and the plaintiff offered the highest bid under the impression that the right was sold for three years, when in fact it was for one year only, he could not avoid the agreement because it was his unilateral mistake.<sup>99</sup> As to what is the nature of a unilateral mistake as provided under Section 22 of the Contract Act, would be best explained by the case of *Haji Abdul Rahman Allarakha v Bombay and Persia Steam Navigation Co.*<sup>100</sup> There the plaintiffs chartered a steamer which was to sail from Jeddah on "10th August, 1892 (fifteen days after the Haj)". The plaintiffs believed that "10th August, 1892" corresponded with the fifteenth day after the Haj. The defendant had no such belief and contracted only with respect to the English date, *viz.*, "10th August, 1892". The plaintiffs subsequently discovered that their belief was mistaken inasmuch as fifteen days after Haj fell on a different day and on the basis of that they sued the defendants for rectification of the charterparty. The court held that it was a unilateral mistake and the plaintiffs were not entitled to any relief. Similarly, where a tenderer, in calculating the price which he wanted to charge, happened, by mistake, to insert wrong figures, and the authority accepted the tender without knowing the mistake, no rectification was allowed.<sup>101</sup>

It should, however, be borne in mind that where the mistake, even if it is of one party only, has the effect of nullifying consent as defined in Section 13, no contract will arise. There is no real consent where mistake prevents the parties from coming to an agreement upon the same thing in the same sense. For an agreement to be avoided on the basis of unilateral mistake, it must be shown: first, that one party erroneously believed that the document sought to be rectified contained a particular term or provision, or possibly did not contain a particular term or provision which, mistakenly, it did not contain; second, that the other party was aware of the omission or the inclusion and that it was due to a mistake on the part of one party; third, that the party who was aware of the mistake omitted to draw the mistake to the notice of the other party and there must be a fourth element involved, namely, that the mistake must be one calculated to benefit one party. Applying these principles to the facts of the case in *Thomas Bates & Son Ltd v Wyndham (Lingerie) Ltd*<sup>102</sup> the court came to the conclusion that where a lease deed contained arbitration clause but the new deed which

99. *A.A. Singh v Union of India*, AIR 1970 Mani 16.

100. ILR (1892) 16 Bom 561.

101. *Higgins v Northampton Corpn*, (1927) 136 LT 235.

102. (1981) 1 WLR 505 (CA).

was prepared by the landlord did not contain that provision without the knowledge of the landlord and though the lessee was aware of the omission he did not draw it to the attention of the landlord, the landlord was entitled to seek rectification of the document for inserting arbitration clause.

The mistake of both parties of which Section 20 speaks may be either common or mutual. The classification of mistakes in terms of "common", "mutual" and "unilateral" is adopted by Cheshire and Fifoot, *THE LAW OF CONTRACT*. The expression "common mistake" is thus explained in this learned work: "In common mistake both parties make the same mistake. Each knows the intention of the other and accepts, but each is mistaken about some underlying and fundamental fact. The parties, for example, are unaware that the subject-matter of their contract has already perished."<sup>103</sup>

Common mistake will definitely render the agreement void if the parties are mistaken about the existence of the subject-matter. This type of mistake occurred in *Couturier v Hastie*<sup>104</sup> where the subject-matter unknown to the parties was extinct at the time of the agreement; in *Strikland v Turner*<sup>105</sup> payment of annuity upon the life of a person who was already dead; in *Pritchard v Merchants and Tradesmen Mutual Life Assurance Society*,<sup>106</sup> where a premium was paid for the revival of a lapsed policy at a time when the assured was already dead; in *Galloway v Galloway*,<sup>107</sup> where the parties made a separation deed under the mistaken assumption that they were in fact married.

The scope of this kind of mistake as to the validity of the contract has been considerably reduced since the decision of the House of Lords in *Bell v Lever Bros Ltd*<sup>108</sup> and its interpretation by DENNING LJ in *Solle v Butcher*.<sup>109</sup> Its operation has been growingly confined to cases where the subject-matter does not exist or is vitally different in character (as opposed to quality) than what it was supposed by the parties to be. Thus in *McRae v Commonwealth Disposals Commission*,<sup>110</sup> the defendants were not allowed to escape from the consequences of selling a ship supposed to be stranded at a described place when the plaintiff discovered at a considerable expense that there was no such ship. The court cited DENNING LJ in *Solle v Butcher*<sup>111</sup> to the effect: "Neither party can rely on his own mistake to say it was a nullity from the beginning." DENNING LJ reinforced his views in *Leaf v International*

103. *LAW OF CONTRACT* (8th Edn, 1972) 202. *M. Rathnam v Susheelamma*, AIR 2009 Kant 79, both parties thought that Development Authority's letter of allotment was equivalent to title to the property and they entered into sale transaction. The sale was held to be void because the allottee was not at the time the owner.

104. (1852) 8 Exch 40: 155 ER 1250.

105. (1852) 7 Exch 208.

106. (1858) 3 CB NS 622.

107. (1914) 30 TLR 531.

108. 1932 AC 161 (HL).

109. (1950) KB 671 (CA).

110. (1951) 84 CLR 377 (Aust); Reported, Smith and Thomas, *A CASE BOOK ON CONTRACT* (4th Edn) 345 and noted, (1952) 68 LQR 30-34: 15 Mod LR 229-32.

111. (1950) KB 671: (1949) 2 All ER 1107 (CA).

*Galleries*.<sup>112</sup> A picture was sold, the seller representing that it was by John Constable, when it turned out to be different. The picture was thus essentially different from what it was supposed to be, yet the contract was held to be only voidable. In a still subsequent case *Frederick E. Rose (London) Ltd v William H. Pim. Junior & Co Ltd*,<sup>113</sup> where the parties were confused between "horsebeans" and "feveroles", DENNING LJ explained the effect of common mistake in these words: "What is the effect in law of this common mistake on the contract between the plaintiff and defendant? I am clearly of opinion that the contract was not a nullity. It is true that both parties were under a mistake and that mistake was of a fundamental character with regard to the subject-matter. The goods contracted for—horsebeans—were essentially different from what they were believed to be—'feveroles'—Nevertheless, the parties to all outward appearances were agreed. They had agreed with the quite sufficient certainty on a contract for the sale of goods by description, namely horsebeans."

The expression "mutual mistake" is thus defined in the same work:<sup>114</sup> "In mutual mistake, the parties misunderstand each other and are at cross-purposes. A, for example, intends to offer his Ford Cortina car for sale, but B believes that the offer relates to the Ford Zephyr also owned by A." *Raffles v Wichelhaus*<sup>115</sup> involved a mistake of this kind.<sup>116</sup>

## 2. Erroneous opinion about value of subject matter

The explanation to Section 20 provides that "an erroneous opinion as to the value of the thing which forms the subject-matter of the agreement is not to be deemed a mistake as to a matter of fact". In a case before the Travancore-Cochin High Court:<sup>117</sup>

A property which was subject to a subsisting lease was sold. The lessee had the right to receive value of the improvements, but the agreement of sale was silent about this. The buyer wanted to have the agreement set aside on the ground of mistake about this right.

But the court held "that there was no mistake and that even if there was a mistake it was not as to a matter of fact essential to the agreement for sale. It could only be an erroneous opinion which the parties had formed as to the real value of the subject-matter and would not be deemed to be a mistake vitiating the agreement."

112. (1950) 2 KB 85 (CA).

113. (1953) 2 QB 450 (CA).

114. Cheshire & Fifoot (8th Edn 1972) 203.

115. (1864) 2 H&C 906: 159 ER 375.

116. ExCh (1864) 2 H&C 906: 159 ER 375.

117. *Kochavareed v Mariappa*, AIR 1950 TC 10; *State of Karnataka v Stellar Construction Co*, AIR 2002 Kant 6, a road building contractor was not allowed to claim additional payment by reason of the fact that he was mistaken about the distance from which the material had to be brought. The contract required him to study the work site and availability of material.

### 3. Mistake of fact and not of law

Mistake should be of fact and not of law, for Section 21 declares that “a contract is not voidable because it is caused by a mistake as to any law in force in India”. The section carries an illustration:

A and B make a contract grounded on the erroneous belief that a particular debt is barred by the Indian Law of Limitation; the contract is not voidable.

A mistake as to the effect of registration upon the validity of a document has been regarded by the Supreme Court as a mistake of law.<sup>118</sup> But a mistake as to a foreign law will avoid. In the case of a Government grant, the grantee claimed perpetual right of possession under the wrong assumption of factual aspects. The court said that a mistake in construing the terms of a grant could not be termed as “mistake of fact”. The contract would not be avoided.<sup>119</sup>

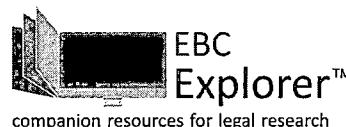
118. *Kalyanpur Lime Works Ltd v State of Bihar*, 1954 SCR 958: AIR 1954 SC 165; *Ganga Retreat & Towers Ltd v State of Rajasthan*, (2003) 12 SCC 91, at the time of sale buildings were in accordance with the law. No guarantee could be given that laws would not be changed for the future.

119. *M.R. Balakrishnan v Govt of Karnataka*, AIR 2010 NOC 1063 (Kant).

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- *Bell v Lever Bros Ltd*, (1932) AC 161 (HL)
- *Ningawwa v Byrappa Shiddappa Hireknarbar*, AIR 1968 SC 956: (1968) 2 SCR 797
- *Phillips v Brooks Ltd*, (1919) 2 KB 243



## Legality of Object

The fourth and the last requirement for the formation of a valid contract is that parties must contract for a lawful object. An agreement the object of which is opposed to the law of the land may be either unlawful or simply void, depending upon the provision of the law to which it is opposed.

### UNLAWFUL AGREEMENTS

Section 23 renders certain considerations and objects as unlawful.

**S. 23. What considerations and objects are lawful, and what not.**—The consideration or object of an agreement is lawful, unless—

- it is forbidden by law; or
- is of such a nature that, if permitted, it would defeat the provisions of any law; or
- is fraudulent; or
- involves or implies injury to the person or property of another; or the Court regards it as immoral, or opposed to public policy.

In each of these cases, the consideration or object of an agreement is said to be unlawful. Every agreement of which the object or consideration is unlawful, is void.

#### *Illustrations*

- (a) A agrees to sell his house to B for 10,000 rupees. Here B's promise to pay the sum of 10,000 rupees is the consideration for A's promise to sell the house, and, A's promise to sell the house is the consideration for B's promise to pay the 10,000 rupees. These are lawful considerations.
- (b) A promises to pay B 1000 rupees at the end of six months, if C, who owes the sum to B, fails to pay it. B promises to grant time to C accordingly. Here, the promise of each party is the consideration for the promise of the other party, and they are lawful considerations.
- (c) A promises, for a certain sum paid to him by B, to make good to B the value of his ship if it is wrecked on a certain voyage. Here A's promise is the consideration for B's payment, and B's payment is the consideration for A's promise, and these are lawful considerations.
- (d) A promises to maintain B's child, and B promises to pay A 1000 rupees yearly for the purpose. Here, the promise of each party is the consideration for the promise of the other party. They are lawful considerations.
- (e) A, B and C enter into an agreement of the division among them of gains acquired, or to be acquired, by them by fraud. The agreement is void, as its object is unlawful.

- (f) A promises to obtain for B an employment in the public service, and B promises to pay 1000 rupees to A. The agreement is void, as the consideration for it is unlawful.
- (g) A, being agent for a landed proprietor, agrees for money, without the knowledge of his principal, to obtain for B a lease of land belonging to his principal. The agreement between A and B is void, as it implies a fraud by concealment, by A, on his principal.
- (h) A promises B to drop a prosecution which he has instituted against B for robbery and B promises to restore the value of things taken. The agreement is void, as its object is unlawful.
- (i) A's estate is sold for arrears of revenue under the provisions of an Act of the Legislature, by which the defaulter is prohibited from purchasing the estate. B, upon an understanding with A, becomes the purchaser, and agrees to convey the estate to A upon receiving from him the price which B has paid. The agreement is void, as it renders the transaction, in effect, a purchase by the defaulter, and would so defeat the object of the law.
- (j) A, who is B's Mukhtar, promises to exercise his influence, as such, with B in favour of C, and C promises to pay 1000 rupees to A. The agreement is void, because it is immoral.
- (k) A agrees to let her daughter to hire to B for concubinage. The agreement is void, because it is immoral, though the letting may not be punishable under the Indian Penal Code (XLV of 1860).

### Object and consideration

The section covers the illegality of both the object of the contract and the consideration for it. The “object” and “consideration” may in some cases be the same thing but usually they are different. For example, where money is borrowed for the purpose of the marriage of a minor, the consideration for the contract is the loan and the object, the marriage. In a case of this kind before the Madras High Court,<sup>1</sup> the court found that the marriage in question was hit by the provisions of the Child Marriage Restraint Act of 1929. “The purpose for which the guardian borrowed the money is to celebrate the marriage of a child which is an offence under the Act.” Thus, the object was to defeat the provisions of the Child Marriage restraint Act. The court relied upon the earlier decision of the Calcutta High Court in *Jaffar Meher Ali v Budge Budge Jute Mills Co*<sup>2</sup> where a debtor transferred certain property to one of his creditors, the object being to give him preference over other creditors and SALE J stated the difference between “object” and “consideration”:

The word ‘object’ in Section 23 of the Contract Act was not used in the same sense as ‘consideration’, but was used as distinguished from consideration and means ‘purpose’ or ‘design’. If then the purpose of the parties was to defeat the provisions of the Bankruptcy Law, there can be

1. *Chandra Sreenivasa Rao v Korapatti Raja Rama Mohana Rao*, AIR 1952 Mad 579. There is no presumption of illegality. Such a presumption cannot be raised except where it is warranted by rules relating to presumptions. A presumption of legality—not a presumption of illegality is the rule. The mere possibility of transgression of law is not a ground for saying that the agreement offends S. 23. The agreement must be shown to be *ex facie* illegal or capable of being performed only through illegal means. *Mathai George v Mathew Chacko*, (1987) 1 KLT 342.
2. ILR (1906) 33 Cal 702.

no doubt that the transfer would be inoperative under the provisions of Section 6 of the Transfer of Property Act.

### 1. Forbidden by law

Where the object of an agreement is forbidden by law, the agreement is void. "Law" in this connection means the law for the time being in force in India and, therefore, includes Hindu and Mohammedan laws also and also principles of unwritten law.<sup>3</sup> A simple illustration is the sale of liquor without licence. The sale is void and the price irrevocable.<sup>4</sup>

#### *Violation of licences and permits*

Cases on this point have mostly been found in agreements involving breach of laws enacted for the protection or promotion of public interest. Reference may be made to only one such case before the Madras High Court.<sup>5</sup>

The plaintiff was licensed under an Excise Act to work a liquor shop. The Act forbade the sale, transfer or sub-lease of the licence or the creation of a partnership to run the shop. The plaintiff took the defendant into partnership.

The partnership was held void as it would defeat the policy of the law if unapproved persons could find their way into working liquor shops.<sup>6</sup> An agreement indirectly defeating the provisions of an Act would be equally void.<sup>7</sup> Much, however, depends upon the object of a particular statute and the object of the agreement as interpreted by the court. If the intention of Legislature is to forbid an act in public interest, an agreement to do the forbidden act will obviously be void.<sup>8</sup> But if the intention is merely to regulate an act by prescribing certain terms and conditions and formalities, a

3. *Gherulal Parakh v Mahadeodas*, AIR 1959 SC 781, 786: (1959) 2 SCR 406, 417.

4. *Boistub Churn Naun v Wooma Churn Sen*, ILR (1889–90) 16 Cal 436. See also *Kateshwar Mittal Kamath v K. Rangappa Baliga & Co*, AIR 1959 SC 781: (1959) 2 SCA 342; *Ajit Singh v Kakbhbir Singh*, AIR 1992 P&H 193, a clog on the equity of redemption (95 yrs) violates Transfer of Property Act and is, therefore, unlawful under S. 23; *Denzyl Winston Ferries v Abdul Jaleel*, AIR 1992 AP 246: (1992) 2 An LT 144, sale of excess land without obtaining permission of competent authority under Urban Land (Ceiling and Regulation) Act, 1976, held unlawful. *Gopal Lal v Babu Lal*, (2004) 4 CLT 161 (Raj DB), a kind of compromise which is barred by Order 23, Rules 3, 3-A and S. 96(1), CPC, not allowed to be enforced.

5. *Nandlal v Thomas J. William*, 171 IC 948.

6. *Thithi Pakurdasu v Bheemudu*, ILR (1903) 26 Mad 430, involving an agreement forbidden by Madras Akkari Act (1886). A partnership for conducting business under a Government licence granted to an individual for retail sale of country spirit which was contrary to the prohibition contained in the relevant State Excise Act was held to be unlawful and void, *Biharilal Jaiswal v CIT*, (1996) 1 SCC 443.

7. *Behari Lall Shaha v Jagodish Chunder Shaha*, ILR (1904) 31 Cal 798. A restraint on sub-letting, sale or transfer does not, however, exclude the taking in of a partner. See *Gauri Shanker v Mumtaz Ali Khan*, ILR (1980) 2 All 411; *Champsey v Gordbandas*, 1917 SCC OnLine Bom 64: AIR 1917 Bom 250, which went up to the Privy Council, AIR 1921 PC 137.

8. Pollock, PRINCIPLES OF CONTRACT, adopted by Full Bench of the Hyderabad High Court in *Babiah v Mohd Abdus Subhan Khan*, AIR 1954 Hyd 156.

contract to do the act without fulfilling the statutory requirements may not itself be void, even if the parties have to pay a penalty for the breach of the statute.<sup>9</sup> A Bombay High Court decision<sup>10</sup> illustrates the point:

The plaintiff was a lessee of certain tolls under the Bombay Tolls Act, 1875. One of the conditions of the lease was that the lessee should not sublet the tolls to any other person without the permission of the Collector. A fine of Rs 200 was payable for a breach of the condition. The plaintiff contracted with the defendant to sublet the toll to him without obtaining the necessary permission.

The question was whether the sub-lease was void. The court held that it was not. The object of the statute was not to forbid such transactions. It was "an Act passed for the benefit of the revenue and not an Act for the protection of public morals". The transaction may be void as against the Collector, but between the parties it stands.<sup>11</sup>

Where an Act or Rules made thereunder prohibit sale or transfer, the licensee cannot form a partnership to work the licence as that also amounts to a transfer.<sup>12</sup> In a subsequent Full Bench decision<sup>13</sup> the Madras High Court further pointed out that "irrespective of the facts whether the contract for partnership was entered into before the licence had been granted or subsequent to the issue of the licence, the result would be the same. The partnership must be deemed to be void *ab initio*.

The decisions of the Bombay High Court, however, have struck a different note. In *Champsey v Gordhandas Kessowji*,<sup>14</sup> a licence granted under

9. See, for example, *Amritsar Rayon & Silk Mills Ltd v Amin Chand Sajdeh*, (1987) 2 PLR 253, violation of the regulatory requirements of S. 299 of the Companies Act, 1956 does not make the contract unlawful.

10. *Bhikanbhai v Hirralal*, ILR (1900) 24 Bom 622; *Waman Shrinivas Kini v Ratilal Bhagwandas & Co*, AIR 1959 SC 689: 1959 Supp (2) SCR 217, an agreement contrary to tenancy laws.

11. See also *Umacharan Shaw & Bros v CIT*, (1959) 37 ITR 271 (SC), where an agreement to take a partner for running a route permit was held valid. Followed in *Dayabhai & Co v CIT*, AIR 1967 MP 13. An agreement to lease equipment instead of selling it would be unlawful if the dominant purpose was evasion of sales tax laws. See *B-Trak Sdn Bhd v Bingkul Timber Agencies*, (1989) 1 Malaysia LJ 124 High Court of Kota Kinabalu. *Nutan Kumar v Addl District Judge*, (2002) 8 SCC 31: AIR 2002 SC 3456, an agreement of lease of land in violation of the Rent Control Act was held to be void. The lessee had no status and was ejectable. He was like a trespasser. A suit for his ejectment was not barred by S. 23.

12. So held by a Full Bench of the Madras High Court in *Chava Rammanayudu v Suryadevara Seetharamayya*, ILR (1935) 58 Mad 727. The decision was under the Madras Abkari Act, 1886. *Satchidananda Samanta v Ranjan Kumar Basu*, AIR 1992 Cal 222, cinema hall licence, partnership formed to run it, held void. *WB Cinemas (Regulations) Act*, 1954 and rules framed under it; *Moti Lal Chunni Lal v CIT*, (1987) 1 Raj LR 737, liquor licence granted jointly to two persons, admitting more into partnership, void.

13. *Velu Padayachi v Sivasooram Pillai*, ILR 1950 Mad 987.

14. AIR 1917 Bom 250. MACLEOD J relying upon Allahabad Full Bench decision in *Gauri Shanker v Mumtaz Ali Khan*, ILR (1980) 2 All 411. A Calcutta decision is to the same effect. *Gobardhan Chakraborty v Abani Mohan*, AIR 1991 Cal 195. A partnership to run a municipal stall, held illegal. *Rasamoy Chowdhury v Anil Krishna Dawn*, AIR 1988 Cal 55. But an agreement by the holder of a motor vehicle licensed under the Motor Vehicles Act to share his

the Bombay Salt Act, 1890, which also prohibited transfer of every kind and the licensee admitted his brothers into partnership with him to work the licence, the court held “that the admission of a partner to share in the profits could not be considered as a subletting or alienating a part of the privilege unless there had been a document directly transferring to the partners a part of the right to manufacture or vend”. The authorities of this kind were held by the Calcutta High Court to be not applicable to a case in which the statute or the rules made under it provided expressly that the taking in of a partner would amount to a deemed transfer of the licence.<sup>15</sup>

All such authorities were reviewed by the Calcutta High Court in *Mafizuddin Khan Chowdhury v Habibuddin Sheikh*,<sup>16</sup> where the court emphasised that decisions must rest on the definiteness of prohibition against sale etc. Here a licence was granted under the Bengal Silk Control Order, 1945, to work raw silk because at that time the Order prohibited working of raw silk without a licence. Although the licence was taken in one name, the understanding was that it would be worked with another person under partnership and that other person brought an action for accounts and dissolution. The court allowed the action, because the Order did not impose any restriction upon transfer etc. Where a party purchased a motor car in the name of a permit-holder so as to make use of his permit, the arrangement was held to be not a void one.<sup>17</sup>

Regulatory laws also give rise to the question whether a statute impliedly prohibits the making of a contract. In *Hughes v Asset Managers Plc*.<sup>18</sup>

A transaction in securities was made through the medium of a person whose firm was licensed but he himself did not hold the representative's licence as required by the Prevention of Frauds (Investments) Act, 1958 (English).

It was held that the Act did not amount to automatically invalidating such transactions because in that case public interest would suffer more instead of being protected.

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profits with another is not illegal. *Mohit Mohan Choudhury v Abdul Rouf Mia*, (1991) 1 Cal LT 361. Sale of a bus without transfer of permit is not illegal. *B. Ratnasabhapathy Chetti v M. Veerappa*, (1989) 1 An LT 588. *Balachandran v Sundara Gounder*, (2003) 2 KLT (SN) 31, the defendant was to be the licensee of a toddy shop and the agreement was that the plaintiff should conduct it, held, an independent agreement, plaintiff entitled to recover back the amount paid by him.

15. *Goutam Hazra v Pinaki Hazra*, (2005) 3 CHN 364; (2005) 3 ICC 344 (Cal).
16. AIR 1957 Cal 336. See also the observations of the Supreme Court on this distinction in *Mannalal Khetan v Kedar Nath Khetan*, (1977) 2 SCC 424: AIR 1977 SC 536. *M.G. Bros Lorry Service v Prasad Textiles*, (1983) 3 SCC 61: AIR 1984 SC 15, a condition in a carriage contract against S. 10 of the Carriers Act was held to be void.
17. *Parakkate Shankaran Keshavan v T.A. Sukumaran*, AIR 1997 Bom 381. *S. Mohammed Anwarudin v Dr Sabina Sultana*, (2005) 4 ALD 566, where the Rules and Regulations of a Housing Authority did not prohibit retransfer by house allottees, any such transfer could not be regarded as opposed to law or public policy.
18. (1995) 3 All ER 669 (CA).

Carrying on moneylending business without registration and licence under any Money-Lenders Act has been held to be contrary to the enactment and, therefore, void.<sup>19</sup>

A provision in the Foreign Exchange Regulation Act, 1973 [S. 31] (now repealed and replaced by FEMA) that a non-resident Indian selling property in India would be liable to a penalty if the sale is made without prior permission of the Reserve Bank, would not affect the validity of the sale transaction itself. The purchaser would be entitled to a valid title.<sup>20</sup>

Where a stage carriage permit was granted to a State Road Transport Corporation, it was not allowed to allot the same to a private operator for working it as a nominee.<sup>21</sup> Permission granted by a State Road Transport Corporation to private operators to operate on nationalised routes when their buses were not licensed for those routes was held to be violative of the prohibitions of the Motor Vehicles Act.<sup>22</sup>

A suit for refund of price paid in advance for the sale of a woman was held to be not maintainable.<sup>23</sup>

### *Violation of enactments*

A contract for the sale of jaggery powder (a form of gur) above control price could not be enforced because "it was tainted with all that anti-social desire against which the Control Orders attempted to fight".<sup>24</sup> Where a

19. *Haesen Banu v Syed Habeeb Sayeeduddin*, 1997 AIHC 135 (AP). Kerala High Court has differed from this opinion. See *Balakrishnan v Babu*, (1994) 1 KLT 947, where it was held that a suit for recovery of the loan amount would be maintainable even if the lender had no licence under the Money-Lenders Act.

20. *Jaswinder Singh v Sanjogta Nanda*, 1996 AIHC 4477 (P&H). *Ajit Prasad Jain v N.K. Widhani*, AIR 1990 Del 42, specific performance of a contract of the above kind was ordered. A. *Lakshmana Rao v P. Rama K. Raju*, (1993) 1 Andh WR (NOC) 5, under the bye-laws of the society, the members could alienate the house only to any other member with the permission of the board of directors. Not void. *Sebastian v Mathai*, (2006) 1 CLT 147 (Ker), property purchased in violation of FERA (New FEMA). Regulations held to be not void because the irregularity was curable. *Musliarakath Abdulla v Abdul Azeeza Naha*, (2006) 2 CCC 507 (Ker), under Foreign Exchange Rules, a car brought into the country was not allowed to be sold within two years, recovery of sale price was allowed.

21. *Brij Mohan Parihar v M.P. SRTC*, (1987) 1 SCC 13: AIR 1987 SC 29. See further *K.M. Jose v D. Anantha Bhat*, AIR 1987 Kant 173, sale of agricultural land for non-agricultural purposes, though forbidden by Karnataka Land Reforms Act (X of 1962) was held not void under S. 23 because the Act prescribed an inquiry for investigation as to the buyer's purposes and no inquiry had been undertaken up to the date of the suit. *Sunil Pannalal Bantia v City and Industrial Development Corp of Maharashtra Ltd*, (2007) 10 SCC 674, transfer of plot by original allottee approved by Corporation in accordance with Regulations. The transferee took possession and raised construction. Cancellation subsequently of the transfer on the ground of public policy was held to be not proper.

22. *Prem Chand v State of U.P.*, 1987 All LJ 1320. *G. Anabalgan v T.N. Civil Supplies Corp Ltd*, (2004) 2 CTC 135 (TN), the DM could appoint more than one transporters for lifting food-grains depending upon work load and other conditions. Two were already working. Appointment of a third transporter without explaining the need for it was struck down by the court.

23. *Nihal Singh v Ram Bai*, AIR 1987 MP 126.

24. *Sita Ram v Kunj Lal*, AIR 1963 All 206. A transfer without obtaining proper permissions of material imported on actual user's licence is illegal. *Canara Bank v Gokuldas Shenoy*, (1989)

company and its customer knowingly entered into a contract for supply of electricity in contravention of the Bihar Electricity Control Order, 1942, the customer could not recover the money paid in excess though the payment was made under protest.<sup>25</sup> The Allahabad High Court held that a contract to supply electricity on the condition that the consumer would be liable to replace the transformer if it is stolen is void, being contrary to the Electricity (Supply) Act, 1948 which provides that the Board must maintain the distribution lines and transformers are parts of it.<sup>26</sup> The Madhya Pradesh High Court held that the grounds specified by a Rent Control Act for the eviction of a tenant cannot be changed by an agreement or compromise because that would be contrary to the Act.<sup>27</sup> The High Court of Delhi refused to grant specific enforcement of a contract of lease under which a land meant for residential purposes was to be handed over to a bank for commercial purposes in violation of Section 14 of the Delhi Development Act, 1957.<sup>28</sup> An agreement to purchase an area of land beyond the statutory limit was held to be not specifically enforceable but refund of advance with interest was ordered.<sup>29</sup> Transfer of a minor's property by the guardian without taking a

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1 KLT 281. But transfer of a licensed theatre, the buyer undertaking to obtain his own licence is not unlawful. *K. Srinivasa Murthy v P. Ananda Rao*, (1985) 1 An LT 53 (NOC); *Malladi Seetharama Sastry v Naganath Kawliwar & Sons*, AIR 1968 AP 315, transfer of telephone connection in violation of S. 20-A of the Telegraph Act, hit by S. 23.

25. *Jharia Coal Field Electric Supply Co Ltd v Kaluram Agarwala*, AIR 1951 Pat 463.

26. *UPSEB v Lakshmi Devi Sehgal*, AIR 1977 All 499.

27. *Hubbilal Sadashiv v Mohd. Maqbool Ahmed Khan*, AIR 1977 MP 65. To the same effect in *Shankarlal Laxminarayan Rathi v Udaisingh Dinkarrao Rajukar*, AIR 1976 Bom 237; *Murlidhar Aggarwal v State of U.P.*, (1974) 2 SCC 472 and *Nagindas Ramdas v Dalpatram Ichharam*, (1974) 1 SCC 242: AIR 1974 SC 471. *New India Assurance Co Ltd v Kesavan Ramamurthy*, (1997) 2 ALD 446, there is nothing wrong in a vehicle insurance policy providing that no compensation would be payable if the vehicle was being driven by an unlicensed person or learning licence-holder. *Navayuga Exports Ltd v A.P. Mineral Devp Corp*, (1998) 4 An LT 505, a licence to work a mine for precious stones cannot be questioned as to its legality only on the ground that it was for too short a period of six months. *Matru Ashish Coop Housing Society Ltd v Bhavana Maternity Home*, (2004) 2 Bom CR 864, recovery of non-occupancy charges not allowed to be more than the maximum prescribed under the Rules. *Matru Ashish Coop Housing Society Ltd v Bhavana Maternity Home*, (2004) 2 Bom CR 864, realising more house tax from the owner than permitted by the applicable statute was held to be wrong irrespective that the owner had himself opted to pay more. *Namdeo Shamrao Waghamare v Ramdas Shripat Waghamare*, (2005) 2 Bom CR 829, sale of agricultural land found to be not in violation of Bombay Prevention of Fragmentation and Consolidation of Holdings Act, 1947, hence not unlawful. *A.E. Aboobacker v P.P. Vasu*, 2004 AIHC 551 (Ker), demand for paguee unlawful.

28. *SBI v Aditya Finance & Leasing Co (P) Ltd*, AIR 1999 Del 18. Unless there is prohibition of transfer of a house allotted under hire-purchases, the property is transferable, *Khair Mohd Khan v S. Eramani*, (1998) 4 An LT 66. *Netyam Venkataramanna v Mahankali Narasimhan*, AIR 1994 AP 244, purchase of land in excess of limit permitted by AP Agricultural Lands (Prohibition of Alienation) Act, 1972 which was repealed before judgment in this case, specific enforcement not refused. The only consequence would have been surrender of extra land on redetermination.

29. *Balbir Singh v Arjun Singh*, AIR 2000 All 37: 2000 AIHC 1350. *National Insurance Co Ltd v New Darjeeling Union Tea Co Ltd*, (2001) 1 Cal LT 218, S. 64 V-B of the Insurance Act, 1938 prohibits the insurer from entering into a contract unless the premium is paid in advance. It was held that such condition could be waived. *Parmanand Setia v Somlal*, AIR 2003 Raj 54,

court order was held to be in violation of Section 8 of the Hindu Minority and Guardianship Act.<sup>30</sup> A compromise between family members for distribution of the family pension which was against Pension Rules was held to be void. The state was bound to pay only in accordance with the Rules.<sup>31</sup>

A solicitor's agreement of fee sharing with a person introducing clients has been held to be void being in violation of rules [(English) Solicitors' Practice Rules, 1990, Rule 7]. The court said that the only alternative remedy of the person who introduced a client was to sue for reasonable remuneration for services if rendered in ignorance of the violation.<sup>32</sup>

#### *Assignment of copyright*

The Copyright Act, 1957 permits assignment of copyright in any present or future work. The statutory permission was held to be not violative of public policy because there are safeguards for the protection of the owner within the frame-work of the Act itself.<sup>33</sup>

#### *Stay order*

A stay order on construction which was obtained otherwise than under the allegation that the object of the contract was unlawful was held as not amounting to illegality of object. It may be that a construction under disputed circumstances may not find buyers, yet the contractor cannot get rid under the doctrine of illegality or impossibility.<sup>34</sup>

## 2. Defeat any law

Sometimes the object of, or the consideration for, an agreement is such that though not directly forbidden by law, it would, if permitted, defeat the provisions of any law. Such an agreement is also void. Easy illustrations are to be found in agreements relating to bail bonds.

An accused is required under the Criminal Procedure Code to furnish a surety in the sum of five thousand rupees for his good behaviour. He deposits the sum with the defendant and persuades him to become surety.

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relinquishment of rights which requires stamp duty and registration is a violation of law if not complied with, not enforceable. *Shirish Finance and Investment P Ltd v M. Sreenivasulu*, (2002) 1 Bom CR 419, acquisition of shares in violation of Securities and Exchange Board of India Regulations held to be void.

30. *T.S. Bellieraj v Vinodhini Krishnakumar*, (2004) 2 CTC 510.
31. *Chongtuokhawi v Union of India*, AIR 2008 Gau 6.
32. *Mohamed v Alaga & Co*, (2000) 1 WLR 1815 (CA). *Marco Shipping Agency v R Piyarelal International*, (2008) 4 CHN 520, charges of bribery could not be allowed to be considered also in an arbitration of proceedings.
33. *Prentice Hall India (P) Ltd v Prentice Hall Inc*, AIR 2003 Del 236; (2003) 1 CLT 576 (Del), Ss. 2(j), 18 and 30. The agreement was between two publishers. *Holyfaith International (P) Ltd v Shiv Kumar*, AIR 2006 AP 198; (2006) 3 An LT 216; (2006) 3 ALJ 319, editing on payment original works under an agreement with a person who declared that all rights were vested in the publisher only was held to be not violative of any body's copyright.
34. *Tenet Homes & Resorts (P) Ltd v Ernakulam*, AIR 2001 Ker 279.

After the period of suretyship is over, the accused sues the defendant for the amount.<sup>35</sup>

The Allahabad High Court held the agreement void and the amount irrecoverable. The intention in requiring a surety is that the surety shall at his own risk see to the appearance of the accused. This purpose is definitely defeated by an agreement of the above sort. A contract to indemnify the surety against his liability is illegal for the same reason.<sup>36</sup>

The debt of an agricultural borrower in respect of his agricultural land became discharged by virtue of certain statutory provisions. Subsequent to that, the same land was sold wherein the discharged debt was also treated as a part of the consideration. The transaction was held to be unlawful as it would have defeated the policy of relieving agricultural borrowers from debt burdens. The fact that only a part of the consideration had the effect of defeating law was not considered to be material because the transaction was for one inseparable consideration.<sup>37</sup>

Where a statute provides penalty for an act, it is implicit that the statute intends to forbid that act.<sup>38</sup> A transaction for exchange of properties to be performed after the compounding of a criminal case between the parties was held to be not enforceable.<sup>39</sup>

A person, who was elected as a *sarpanch* for a period of five years, made an agreement with another member that the latter would be given two year term and the elected one, the remaining three years. The agreement was held to be void as it would have defeated the purpose and provisions of the Punjab Panchayat Raj Act, 1994.<sup>40</sup> An agreement to secure votes in favour of a person to enable him to get elected to a statutory body in consideration of sharing power or quitting office after specified period was held to be violation of Section 8 of the Advocates Act which prescribes a five year term of office.<sup>41</sup>

#### *Law of friendly country*

An agreement which defeats the law of a friendly country would be equally void. An illustration is *Ragazzoni v K.C. Sethia*.<sup>42</sup>

The Government of India had, by regulations made under the Sea Customs Act, 1878, prohibited the export of goods to South Africa. The plaintiff and the defendant, being aware of the prohibition and in a bid to overcome the embargo, agreed that a larger quantity of jute bags would be shipped from India and made available in Genoa for resale to South

35. *Fateh Singh v Sanwal Singh*, ILR (1875) 1 All 751.

36. *Sunder Singh v Kishen Chand*, 1889 Punj Rec 1 p. 1.

37. *Kommineni Seetharamaiah v K. Punnaiah*, 1996 AIHC 4384 (AP).

38. *Nutan Kumar v Addl District Judge, Banda*, AIR 1994 All 298, letting of premises without allotment or release order in violation of UP Urban Buildings (Regulation of Letting, Rent and Eviction) Act, 1972.

39. *Srihari Jena v Khetramohan Jena*, AIR 2002 Ori 195: (2002) 94 CLT 201 (Ori).

40. *Mohinder Singh v State of Punjab*, AIR 2009 NOC 434 (P&H).

41. *D. Selvam v Bar Council of T.N. and Pondicherry*, (2008) 4 CTC 97.

42. (1956) 2 QB 490: (1956) 2 WLR 204.

African buyers. The defendant failed to deliver the goods and the plaintiff sued for damages.

The Court of Appeal held that while the English courts will not enforce foreign revenue or penal laws, they will not entertain an action based on a transaction which is knowingly intended to involve a breach of such laws. DENNING LJ said: "...if two people knowingly agree together to breach the laws of a friendly country or to procure someone else to break them or to assist in the doing of it, then they cannot ask this court to give its aid to the enforcement of their agreement."

Another illustration is *Foster v Driscoll*.<sup>43</sup> Here the agreement was to buy whisky in Great Britain and to smuggle it into the United States against the law of that country. The Court of Appeal held the agreement to be illegal. It involved the commission of an offence in a foreign and friendly country and so a breach of international comity. It did not matter that the parties had not succeeded in their attempt and they could have lawfully taken their goods to another country.

#### *Innocent violations*

Where the violation of a home or foreign law would not be an affront to public conscience, enforcement may be allowed. Such a possibility was recognised by the Court of Appeal in *Howard v Shirlstar Container Transport Ltd*.<sup>44</sup>

The owner of an aircraft agreed to pay the plaintiff for successfully removing his aircraft from Nigerian territorial airspace. The plaintiff did so without permission of Nigerian authorities and landed it in Ivory Coast. The plaintiff did so under the belief that there was imminent danger to life in Nigeria. The Ivory Coast Government returned the aircraft to Nigerian authorities. But the plaintiff sued for his fee.

He was allowed to recover. He had done the job of removing and safe landing and since his fee was payable on completion of the flight out of Nigeria, he had earned his fee. As for the illegality involved, the court said that although the court would not normally enforce a contract which would enable a plaintiff to benefit from his criminal conduct, since to do so would be an affront to the public conscience, there are circumstances where it would be wrong to disqualify a plaintiff from recovering, even though his claim was derived from conduct which constituted a statutory offence. One such circumstance is where the plaintiff commits a criminal act in order to escape danger to his life. Accordingly, although the plaintiff's claim would otherwise be unenforceable in English courts because his breach of Nigerian air traffic control regulations was central to the performance of his contract, the public conscience would not be affronted if the contract was enforced

43. (1929) 1 KB 470 (CA).

44. (1990) 1 WLR 1292 (CA).

against the defendant because the plaintiff's conduct was designed to free himself and his wireless operator from pressing danger.<sup>45</sup>

Where a deposit of money was taken in excess of the Post Office Monthly Income Rules, 1987 and interest paid on it, recovery of such interest amount from the depositor was not allowed. There was nothing immoral or against public policy. There was only the technical violation of a rule which it was in the hands of the Central Government to waive or to alter.<sup>46</sup> A bank was allowed to recover back money lent without knowing whether the borrower was licenced for his business or not and his guarantors were allowed to take back their title deeds from the bank.<sup>47</sup>

#### *Scope of the term "law"*

"Law" in this connection means the rules of law for the time being in force in India and includes Hindu and Muslim laws. The Bombay High Court, for example, held in a case<sup>48</sup> that according to the Mohammedan Law, it is not competent to parties contracting a marriage to enter into a separation deed by which the husband covenanted that his wife might live with her parents. Similarly, accepting a son in adoption in consideration of a sum of money is unlawful.<sup>49</sup>

#### *Money and property involved in transactions defeating law*

The Supreme Court considered this part of Section 23 in *Surasibalini Debi v Phanindra Mohan Mazumdar*.<sup>50</sup>

The plaintiff, an employee of the Court of Wards, started the business of running a boarding house. The rules of service prohibited him from engaging in any trade or business. The premises were leased nominally in the name of his father-in-law, but the management and finance was the concern of the plaintiff. The business ran for quite a few years. The plaintiff fell ill and had to leave Calcutta for some time. He transferred the business wholly to his father-in-law on the understanding that on his return, the father-in-law would hand back the business and would

45. The court applied the decisions in *Euro-Diam Ltd v Bathurst*, (1988) 2 WLR 517 (CA).

46. *Rajat Kumar Rath v Govt of India*, AIR 2000 Ori 32; *Thirumalai v Gomathi Ammal*, 2000 AIHC 1000 (Mad), gift under marriage being not void at the time, allowed to be retained. *M.A. Jabbar v LIC House Building Employees Society*, (2000) 1 An LT 385, entering into an agreement without obtaining prior approval of the Registrar of Cooperative Societies was held to be not opposed to public policy.

47. *Andhra Bank v Vattikuti Sreemannarayana*, (2004) 5 ALD 111 (DB). The court cited authorities: *Gauri Shankar v Nathu Lal*, AIR 1951 All 589, money lent under a mortgage allowed to be recovered though the mortgage was not registered as it ought to have been.

48. *Abdul Piroj Khan Nobab v Hussainbi*, (1904) 6 Bom LR 728.

49. *Narayan Laxman Chandvadkar v Gopalrao Trimbak Chandvadkar*, 1922 SCC OnLine Bom 11: ILR (1922) 46 Bom 908; *Neminath Appayya v Jamboorao Sateppa Kochtevi*, AIR 1966 Mys 154, where the court allowed specific performance of an agreement for the purchase of land beyond the ceiling fixed by an Act.

50. AIR 1965 SC 1364: (1965) 1 SCR 861.

also account for its profits. The plaintiff came back but his father-in-law refused to oblige him.

The plaintiff brought an action to recover back his business. The defendant contended that the business was illegal because it defeated the service rules and also the Income Tax Act. The Supreme Court held that the service rules were not statutory and, therefore, their violation did not render the business illegal. The only other question was the evasion of income tax. On this point, AYYANGAR J found that the law undoubtedly was that where a *benami* transaction is entered into for the evasion of taxes, the law would not give its help to either party and would leave them where they are.<sup>51</sup> In such cases, recovery is possible only if either the illegal purpose has not been carried out<sup>52</sup> or the plaintiff has not to rely upon the illegal transaction.<sup>53</sup> The plaintiff had left the business in the hands of his father-in-law on account of his illness and not because of the illegality. His action was to enforce his ownership interest and for this purpose it was not necessary for him to rely on the illegal transaction. Accordingly, he was allowed to recover the possession of his business.

Money sent from abroad through unauthorised channels has been allowed to be recovered.<sup>54</sup>

#### *Agreement to evade taxes*

An agreement between the partners of a firm to conceal income in certain respects so as to evade income tax has been held to be unlawful.<sup>55</sup> It has been held that there is subterfuge in entering into a composite works contract containing elements both of transfer of property in goods as well as labour and services.<sup>56</sup>

#### *Undercutting of statutory privileges*

A term in a contract of carriage requiring that notice of loss must be given within 30 days of the arrival of the goods has been held by the Supreme Court to be contrary to and defeating Section 10 of the Carriers Act, 1865, which prescribes a period of six months for the purpose.<sup>57</sup>

51. Apart from this, *benami* transactions are so common in India that there is no illegality in itself, see *Kedar Nath Matani v Prablad Rai*, AIR 1960 SC 213: (1960) 1 SCR 861.
52. So ruled by the Privy Council in *T. P. Petherpermal Chetty v R. Muniandi Servai*, (1907–08) 35 IA 98 and *Guru Narayan v Sheo Lal Singh*, (1918–19) 46 IA 1 (PC).
53. So held by the Privy Council in *V. Sardar Ali v Sajan Singh*, 1900 AC 167 (PC).
54. *Abdul Jabbar v Abdul Muthaliff*, AIR 1982 Mad 12. The recipient constructed a rice mill with the money; the mill was allowed to be recovered.
55. *Ram Sewak v Ram Charan*, AIR 1962 All 177.
56. *CCE and Customs v Larsen & Toubro Ltd*, (2016) 1 SCC 170.
57. *M.G. Bros Lorry Service v Prasad Textiles*, (1983) 3 SCC 61. Since the purpose of bribery is to defeat law, it would also fall under the section. *Gulabchand v Kudilal*, AIR 1966 SC 1734: (1966) 3 SCR 623. As to when certain unfair clauses in a Government contract would defeat the normal legal rights of contractors, see *V. Raghunadha Rao v State of A.P.*, (1988) 1 An LT 461. The clauses in question were an attempt to relieve the State of its liability and the court said that a State is not free to impose arbitrary or unjust clauses in a public contract.

### 3. Fraudulent

An agreement made for a “fraudulent” purpose is void. Where the parties agree to impose a fraud on a third person, their agreement is unlawful. Where, for example, a debtor agreed to pay a separate commission, or to give preference to a creditor in order to induce his consent to a composition which is proposed with other creditors, the object of the agreement is fraudulent.<sup>58</sup> In another case, there were two decree-holders against the debtor and one of them, the plaintiff, had the debtor’s property attached and brought to sale. The plaintiff agreed with the defendant, a prospective buyer, that he would not bid against the defendant and that the defendant would pay him off. The property was thus knocked down to the defendant for a very small price. It was held that the whole object of the arrangement was fraudulent as it deprived the other decree-holder of what he would have got if the sale had been competitive. Accordingly, the plaintiff could not recover anything from the defendant.<sup>59</sup> Similarly, an agreement to defraud creditors, or to give fraudulent preference to a creditor or to defraud revenue authorities,<sup>60</sup> or investors in a company,<sup>61</sup> are illegal. A compromise decree obtained by practising fraud on the court was held to be void.<sup>62</sup>

“Intention to deceive” seems to be necessary for an agreement to fall in this category. A decision of the English Court of Appeal, however, shows that the same result may follow where one of the parties had no such intention, but made himself an innocent instrument of fraud at the suggestion of the other party.<sup>63</sup>

A shipowner informed the shipper that the barrels containing the orange juice were old and frail and that some were leaking and, therefore, a clean bill of lading could not be granted. The shipowner, however, issued a clean bill after a promise of indemnity from the sender. The bill stated that the barrels were shipped in good order and condition. On

58. *Atamal Ramoomal v Deepchand Kessurmal*, AIR 1939 Sind 33; *Mallalieu v Hodgson*, (1851) 16 QB 689. *Indian Hotels Co Ltd v Bhaskar Moreshwar Karve*, 1993 Cri LJ 3370 Bom, sale of a company’s property at a throw-away price may be of fraudulent nature and, therefore, against public policy. *Munesh v Anasuyamma*, AIR 2001 Kant 355, a document containing compromise of marital proceedings on which the wife’s signature was forged was against law and, therefore, could not be the basis of any matrimonial remedy. *Laxman Lahanuji Lende v Harichand Domaji Kulharkar*, (2006) 3 Bom CR 864 (Nag Bench), deed of family partition, alleged to be fraudulent, *Karta* is a necessary party, other coparceners desirable but not necessary.

59. *Ram Nath Misra v Rajendranath Sanyal*, 142 IC 525: ILR (1933) 8 Luck 233. *Kedar Nath Matani v Prahlad Rai*, AIR 1960 SC 213, 216: (1960) 1 SCR 861.

60. *Alexander v Rayson*, (1936) 1 KB 169 (CA).

61. *Begbie v Phosphate Sewage Co Ltd*, (1876) LR 1 QBD 679 (CA).

62. *Ashis Kumar Ghosh v Gopal Chandra Ghosh*, (2004) 3 CHN 146, the plaintiffs alleged that they were never parties to the suit which ended in the compromise.

63. *Brown Jenkinson & Co v Percy Dalton (London) Ltd*, (1957) 2 QB 621: (1957) 3 WLR 403 (CA). *Naraindas v Bhagwandas*, 1993 MPLJ 1005, deliberate statement of incorrect facts resulting in exercise of jurisdiction which otherwise would not have been exercised, fraud on statute.

arrival at the destination, the contents of the barrels had suffered considerable leakage and the shipowner had to make good the loss thus caused to the buyer of the barrels. The shipowner then sought to enforce the indemnity against the sender.

It was held by a majority of two against one that the indemnity bond was not enforceable. MORRIS LJ stated the effect of the agreement thus: If you make a false representation that the goods have been received in good order when you know that they are not so and which will deceive endorsees of the bill, we will not indemnify you against consequences. Thus, the shipowner had made himself a vehicle not merely for conveyance of goods but also for carrying a false representation. This made the whole scheme unlawful disentitling him from relying upon any part of it. The argument that it was a common practice of the shipowners was shelved by the court by saying that it may explain why he did what he did, but not make an unlawful thing lawful. Where the parties to a contract conspired to defraud an insurance company by agreeing to an inflated estimate for repair work in order to claim a larger sum, it was held that the contract was vitiated by illegality. The legitimate part of the claim could not be separated from the illegal portion because it was a single indivisible arrangement, it could not be enforced.<sup>64</sup>

An agreement between two bidders not to bid against each other with an understanding that the successful bidder would convey half the property to the other, has been held to be not against public policy.<sup>65</sup>

#### 4. Injurious to person or property

An agreement between two persons to injure the person or property of another is unlawful. In the same way, if the object of an agreement is such that it involves or implies injury to the person or property of another, the agreement is unlawful and void. A person borrowed a sum of hundred rupees and executed a bond promising to work for the plaintiff without pay for a period of two years. In case of default, the borrower was to pay exorbitant interest and the principal sum at once. The court held that the contract contained in the bond was indistinguishable from slavery, which involves injury to the person and was, therefore, void.<sup>66</sup> Similarly, a bond to pay an exorbitantly high rate of interest, in case, the borrower left the lender's service, has been held to be void.<sup>67</sup> An agreement to commit a crime or a civil wrong, for example, to assault or beat a person or to deceive him<sup>68</sup> or to publish a libel against him,<sup>69</sup> all fall in this category.

64. *Taylor v Bhail, The Independent*, Nov 20, 1995 (CA).

65. *Sujan Singh Sadhana v Mohkam Chand Jain*, AIR 1983 P&H 180.

66. *Ram Sarup Bhagat v Bansi Mandar*, ILR (1915) 42 Cal 742.

67. *Ibid.*

68. *Brown Jenkinson & Co v Percy Dalton (London) Ltd*, (1957) 2 QB 621: (1957) 3 WLR 403 (CA).

69. *Clay v Yates*, (1856) 1 H&N 73: 156 ER 1123.

### *Fruits of crime*

Law does not help a person to recover anything under his own crime. The fruits of a crime are irrecoverable. No person is allowed to benefit from his own crime. It is on this principle that a person is not permitted to participate in a succession which he has brought about through murder.<sup>70</sup> An insured person committed suicide to enable his representatives to get the insurance money, but they were not allowed to recover. It was an attempt to confer a benefit through his own crime.<sup>71</sup> This brought about an undeserved punishment of the representatives. The position was, therefore, changed by the Suicide Act, 1961 [English]. The principle was again applied to prevent a person, who had taken out a policy in respect of liability for bodily injury caused by accident, from recovering anything for liability for death caused by him though involuntarily but as a result of an unlawful and violent attack.<sup>72</sup> Criticising such results, it has been observed in Cheshire and Fifoot:<sup>73</sup> “The principle that no benefit can accrue to a criminal from his own crime, however, must obviously not be pushed too far. Nowadays, there are many statutory offences, some of them involving no great degree of turpitude, which rank as crimes, and it has several times been doubted whether they are all indiscriminately affected by the rule of which the *Beresford* case is an example.”<sup>74</sup>

### **5. Immoral**

The law does not allow an agreement tainted with immorality to be enforced. Consequently, every agreement the object of or consideration for which is immoral, is unlawful. What is “immoral” depends upon the standards of morality prevailing at a particular time and as approved by the courts. But certain kinds of acts have been regarded as immoral since times immemorial and will perhaps always be so regarded.

### *Interference in marital relations*

One such act is interference with marital relations. Thus, where a married woman was given money to enable her to obtain divorce from her husband, the lender promising to marry her subsequently, it was held that the money could not be recovered.<sup>75</sup> Similarly, a promise to marry a married woman

70. *Giles v Giles*, 1972 Ch 544, a woman killing her husband.

71. *Beresford v Royal Insurance Co Ltd*, 1938 AC 586 (HL); affirmed on appeal, 1938 AC 586: (1938) 2 All ER 602. The position in India is different. Here suicide is not a crime and therefore payment under an insurance policy is not against public policy even if the claim arises by reason of suicide. *Scottish Union & National Insurance Co v N. Roushan Jahan Begam*, AIR 1945 Oudh 152; ILR (1945) 20 Luck 194.

72. *Gray v Barr Prudential Assurance Co Ltd*, (1971) 2 QB 554: (1971) 2 WLR 1334..

73. LAW OF CONTRACT (9th Edn by Furmston, 1976) 335.

74. Recovery would, for example, be allowed to the victim of a motor accident even if intentionally induced.

75. *Baiwijli v Nansa Nagar*, ILR (1885) 10 Bom 152; *Roshun v Muhammad*, 1887 Punj Rec No. 46.

after the death of her husband or after she obtains divorce from him is immoral. In the same way, a promise by a married man to marry a woman after the death of his wife or after obtaining divorce from her is illegal. But if she does not know the man to be married, she can bring an action for breach.<sup>76</sup> In *Fender v John Mildmay*<sup>77</sup> the House of Lords had to face a difficult case on this point.

The defendant, who was a married man at the time, met the plaintiff at a nursing home where she was a nurse. He told her that he was unhappy with his wife and later asked her whether, if his wife divorced him, she would marry him after the divorce. She consented and thereupon sexual relations took place between them. The wife petitioned for a divorce on the ground of this adultery and a decree *nisi* was pronounced.<sup>78</sup> The defendant then promised to marry the plaintiff as soon as the decree was made absolute. But he committed breach of this promise by marrying another woman. The plaintiff sued him.

The claim was resisted on the ground of immorality, but she was held entitled to recover. What is immoral is interference with marital status, whereas, in the present case, “after decree *nisi* the bottom has dropped out of marriage: nothing but a shell is left”. Accordingly, the circumstances which lead to mischief were absent here.

#### *Dealings with prostitutes*

Dealings with prostitutes have always been regarded as immoral. “If articles are sold or something is hired to a prostitute for the purpose of enabling her to carry on her profession, neither the price of the articles sold nor the rent of the thing hired can be recovered.”<sup>79</sup> “If a woman takes a house in order to live in it as the mistress of a man and to use it for that purpose, and the landlord at the time when the lease is executed knows that it is taken for that purpose, the landlord cannot recover the rent.”<sup>80</sup>

#### *Illegal cohabitation*

A promise to pay for past sexual immorality or illegal cohabitation has been held in England to be enforceable if under seal. If it is not under seal, it cannot be enforced as past consideration is no consideration.<sup>81</sup> The

76. *Shaw v Shaw*, (1954) 2 QB 429; (1954) 3 WLR 265 (CA); *Wilson v Carnley*, (1908) 1 KB 729 (CA).

77. 1938 AC 1, 723 (HL).

78. Decree *nisi* is made absolute after six months and then final divorce takes place. In the meantime the marital status continues.

79. *Pearce v Brookes*, (1866) LR 1 Exch 213; *Bholi Baksh v Gulia*, (1876) Punj Rec No 64; *Gangamma v Cudapah Kupammal*, AIR 1939 Mad 139.

80. BUCKNILL J in *Upfill v Wright*, (1911) 1 KB 506; *Chogalal v Piyari*, ILR (1908–10) 31 All 58. The landlord may, however, recover if he did not know the purpose. *Sultan v Naner*, 1877 Punj Rec No 64.

81. *Beaumont v Reeves*, (1846) 8 QB 483.

Allahabad High Court allowed a woman to recover arrears of allowance promised to her for past cohabitation.<sup>82</sup> But in a subsequent decision, the same High Court has held that where cohabitation is adulterous, that is to say, where either party is married, whether past or future, it will not support a promise. Adultery is not merely immoral, but is also illegal.<sup>83</sup> Contrary views have also been expressed. “In *Hussainali Casan v Dinbai*,<sup>84</sup> MACLEOD CJ and CRUMP J held that a contract which was immoral at the time, and, therefore, could not support an immediate promise to pay, did not become innocent by merely being past consideration. There can be no difference whether A says to B: ‘I will give you Rs 1000 a month if you live with me for a year,’ or ‘I will give you Rs 1200 because you have lived with me for a year.’” The consideration, therefore, for past cohabitation is unlawful as being immoral or opposed to public policy.<sup>85</sup>

A promise to pay for future cohabitation is unenforceable. A promise to pay for past cohabitation for the purpose of securing the continuance of the cohabitation is also unenforceable. Where a promise was given for past cohabitation “with a view that she may continue in my service”, it was held to be opposed to public policy.<sup>86</sup> But a promise to pay for past cohabitation only is enforceable even if the circumstances do not rule out the continuance of the cohabitation.<sup>87</sup>

The principles which have thus crystallised from the various High Court decisions have been approved by the Supreme Court in *Dwarampudi Nagaratnamba v Kunuku Ramayya*.<sup>88</sup> Certain properties were gifted in consideration of past cohabitation. The Supreme Court found that the properties belonged to the joint family, which the *Karta* had no power to gift and, therefore, the gift was void. But apart from this, BACHAWAT J recognised past cohabitation as a good consideration. The Rajasthan High Court has put the same thing on more rational basis.<sup>89</sup> A gift deed was executed by a person in favour of a woman with whom he had adulterous cohabitation. Holding the gift deed to be enforceable, the court said that the word “object” as used in Section 23 means purpose or design. Past cohabitation, even if adulterous, is no longer the object of the gift. It only supplies a motive. Gift is a transfer without consideration. Hence, no question of unlawful consideration can arise.

82. *Dhiraj-Kuar v Bikramjit Singh*, ILR (1831) 3 All 787.

83. *Alice Mary Hill v William Clarke*, ILR (1905) 27 All 266. Patna High Court has expressed a similar view. See *Godfrey v Parbati*, AIR 1938 Pat 308.

84. AIR 1924 Bom 135. See also *Kisendas v Dhondu*, ILR (1920) 44 Bom 542.

85. Per ANANTANARAYAN CJ in *Manicka Gounder v Muniammal*, AIR 1968 Mad 392; *Subhashchandra v Narbadabai*, AIR 1982 MP 236 (past cohabitation).

86. *Alice Mary Hill v William Clarke*, ILR (1905) 27 All 266.

87. So held in *B. V. Rama Rao v Jayamma*, AIR 1953 Mys 33.

88. AIR 1968 SC 253: (1968) 1 SCR 43.

89. *Pyare Mohan v Narayani*, AIR 1982 Raj 43. *Sandhya Chatterjee v Salil Chandra Chatterjee*, AIR 1980 Cal 244, there is nothing immoral in the agreement of a husband to provide separate residence to his wife. *A.E. Thirumal Naidu v Rajammal*, AIR 1968 Mad 201.

### *Dancing girls*

Help given or promised to a dancing girl is not tainted with immorality.<sup>90</sup>

### *"Immorality" to be limited to sex outside marriage*

The scope of the word "immoral" has been explained by the Supreme Court in *Gherulal Parakh v Mahadeodas*<sup>91</sup> SUBBA RAO J (afterwards CJ) said:

The case-law both in England and India confines the operation of the doctrine to sexual immorality. To cite only some instances: settlements in consideration of concubinage, contracts of sale or hire of things to be used in a brothel or by a prostitute for purposes incidental to her profession, agreements to pay money for future illicit cohabitations, promises in regard to marriage for consideration or contracts facilitating divorce are held to be void on the ground that the object is immoral.

The learned judge pointed out that the word "immoral", being a very comprehensive one, must be given restricted meaning and it has been restricted to mean sexual immorality. Accordingly, the court held that a wagering, agreement could not be regarded as immoral.

## 6. Public policy

An agreement is unlawful if the court regards it as opposed to public policy. The term "public policy"<sup>92</sup> in its broadest sense means that sometimes the courts will, on considerations of public interest, refuse to enforce a contract.<sup>93</sup> The normal function of the courts is to enforce contracts; but considerations of public interest may require the courts to depart from their primary function and to refuse to enforce a contract.<sup>94</sup> Interpretation of the concept of public policy is the function of the court and not that of the executive. A State Amendment of the Registration Act, 1908 empowered the Registrar to refuse registration of a power of attorney authorising the attorney to transfer specified immovable properties because the registration of such documents was opposed to public policy.<sup>95</sup>

### *Observations in English Law about public policy*

The circumstances in which a contract is likely to be struck down as one opposed to public policy are fairly well-established in England. "... So a contract of marriage brokerage, the creation of a perpetuity, a contract in restraint of trade, a gaming or wagering contract, or the assisting of the

90. *Khubchand v Beram*, ILR (1888) 13 Bom 150.

91. AIR 1959 SC 781; (1959) 2 SCR 406.

92. The subject of public policy has been considered in a number of learned articles and essays. See generally Lord Wright, *LEGAL ESSAYS AND ADDRESSES*; Winfield, *Public Policy in the English Common Law*, (1928) 42 Har L Rev 76–102.

93. *Thomson-CSF v National Airport Authority of India*, AIR 1993 Del 252, grant of Government contracts, national interest demands that national contractors should be preferred if they are equally equipped.

94. See Lord WRIGHT in *Fender v John Mildmay*, 1938 AC 1, 723 (HL).

95. *State of Rajasthan v Basant Nahata*, (2005) 12 SCC 77: AIR 2005 SC 3401.

King's enemies, are all unlawful things" on the ground of public policy.<sup>96</sup> The ordinary function of the courts is to rely on the well-settled heads of public policy and to apply them to varying situations.<sup>97</sup> If the contract in question fits into one or the other of these pigeon-holes, it may be declared void.<sup>98</sup> The courts may, however, mould the well-settled categories of public policy to suit new conditions of a changing world.<sup>99</sup> But may a court invent a new head of public policy?

According to Lord HALSBURY, the categories of public policy are closed.<sup>100</sup> "I deny", he said, "that any court can invent a new head of public policy". "From time to time judges of the highest reputation have uttered warning notes as to the danger of permitting judicial tribunals to roam unchecked in this field."<sup>101</sup> For example, a judge protesting against public policy in an early case, said, "it is a very unruly horse, and when once you get astride it, you never know where it will carry you".<sup>102</sup> A few other opinions may be cited. " 'Public policy' is a vague and unsatisfactory term."<sup>103</sup> "Certain kinds of contracts have been held void at common law on this ground—a branch of the law, however, which certainly should not be extended, as judges are more to be trusted as interpreters of the law than as expounders of what is called public policy."<sup>104</sup> " 'Public policy' is always an unsafe and treacherous ground for legal decisions, and in the present case it would not be easy to say on which side the balance of convenience would incline."<sup>105</sup> Yet the rule exists. In the words of Lord ATKIN, "the doctrine should only be invoked in clear cases in which the harm to the public is substantially incontestable, and does not depend upon the idiosyncratic inference of a few judicial minds".<sup>106</sup>

#### *Indian cases adopting English view*

"The Indian cases also adopt the same view."<sup>107</sup> The following words of SUBBA RAO J (afterwards CJ) in *Gherulal Parakh v Mahadeodas*<sup>108</sup> enshrine the present position of the doctrine of public policy in India:

96. Earl of HALSBURY LC in *Janson v Driefontein Consolidated Mines Ltd*, 1902 AC 484.

97. See SUBBA RAO J (as he then was) in *Gherulal Parakh v Mahadeodas*, (1959) 2 SCR 406.

98. ASQUITH J in *Monkland v Jack Barclay Ltd*, (1951) 2 KB 252.

99. Lord WRIGHT in *Fender v John Mildmay*, 1938 AC 1, 723 (HL).

100. See PARKE B in *Egerton v Brownlow*, 10 ER 359, 408; (1853) 4 HLC 1, 123.

101. Lord ATKIN in *Fender v John Mildmay*, 1938 AC 1, 723 (HL).

102. BOROUGH J in *Richardson v Mellish*, (1824) 2 Bing 229, 252; 130 ER 294.

103. PARKE B in *Egerton v Brownlow*, (1853) 4 HLC 1, 123.

104. CAVE J in *Mirams, re*, (1891) 1 QB 594, 595.

105. Lord DAVY in *Janson v Driefontein Consolidated Mines Ltd*, 1902 AC 484, 500.

106. In *Fender v John Mildmay*, 1938 AC 1, 723 (HL).

107. Per SUBBA RAO J (as he then was) in the *Gherulal* case, AIR 1959 SC 781. *Indian Oil Corp v Raj Unocal Lubricants Ltd*, (1997) 2 Mah LJ 281, public policy connotes some matter which concerns public good and public interest. See also *Transocean Shipping Agency (P) Ltd v Black Sea Shipping*, (1998) 2 SCC 281; AIR 1998 SC 707, appointment of a foreign arbitrator and application of foreign laws, but enforcement of the award in India was held to be not *ipso facto* opposed to public policy of India. The matter was under the Foreign Awards (Recognition and Enforcement) Act, 1961 (now repealed by the Arbitration and Conciliation Act, 1996).

108. AIR 1959 SC 781: (1959) 2 SCR 406.

"The doctrine of public policy may be summarised thus: Public policy or the policy of the law is an illusive concept; it has been described as an "untrustworthy guide", "variable quality", "unruly horse", etc.; the primary duty of a court of law is to enforce a promise which the parties have made and to uphold the sanctity of contract which forms the basis of society; but in certain cases, the Court may relieve them of their duty on a rule founded on what is called the public policy; for want of better words Lord ATKIN describes that something done contrary to public policy is a harmful thing; but the doctrine is extended not only to harmful cases but also to harmful tendencies; this doctrine of public policy is only a branch of common law, and just like any other branch of common law, it is governed by precedents; the principles have been crystallised under different heads and though it is permissible for courts to expound and apply them to different situations, it should only be invoked in clear and incontestable cases of harm to the public; though the heads are not closed and though theoretically it may be permissible to evolve a new head under exceptional circumstances of a changing world, it is advisable in the interest of stability of society not to make any attempt to discover new heads in these days."

Explaining the scope of the expression "public policy" and the role of the judge, C. REDDY J of the Andhra Pradesh High Court observed:<sup>109</sup> The twin touchstones of public policy are advancement of the public good and prevention of public mischief and these questions have to be decided by judges not as men of legal learning but as experienced and enlightened members of the community representing the highest common factor of public sentiment and intelligence.

Endorsing this view, the Supreme Court added that going by prevailing social values, an agreement having tendency to injure public interest or public welfare is opposed to public policy.<sup>110</sup>

### *Surrender of rights*

A wife who is entitled to maintenance can give up her right in consideration of a lump sum payment, but the surrender of the right to claim revision of the amount in the context of rising prices would be opposed to public policy.<sup>111</sup>

109. *Ratanchand Hirachand v Askar Nawaz Jung*, AIR 1976 AP 112.

110. *Rattan Chand Hira Chand v Askar Nawaz Jung*, (1991) 3 SCC 67. Refund of sales tax money already collected under various sales transactions would be a breach of trust with the people and a violation of public policy and, therefore, cannot be allowed as an article of incentive to new industry. *Amrit Banaspati Co Ltd v State of Punjab*, (1992) 2 SCC 411: AIR 1992 SC 1075. There is nothing wrong essentially in providing for the appointment of an arbitrator from among employees of the department. *Vijay Singh Amar Singh v Hindustan Zinc Ltd*, AIR 1992 Raj 82; *M.K. Usman Koya v C.S. Santha*, AIR 2003 Ker 191, the term "public policy" has an entirely different and more extensive meaning than the meaning of the term "policy of law". It does not remain static. Judges have to interpret it taking a substantial guidance from precedent.

111. *Muniammal v Raja*, AIR 1978 Mad 103. *Bhaskar Tanhaji Dhokrat v Parvatbai Bhaskar Dhokrat*, (1996) 1 Bom CR 311, a custom to the effect that legal right to maintenance would

Giving effect to an agreement which overrides Section 125 CrPC would tantamount to not only giving recognition to something which is opposed to public policy but would also amount to negation of the statutory provisions. The court said that public policy can broadly be equated with policy of law.<sup>112</sup> A marriage was dissolved on consent terms, one of which was that the wife would not claim alimony or maintenance. It was held that such consent terms could not prevent the court from granting maintenance on the application of the wife made subsequently. Such rights are the larger parts of the right to life. It is against public policy to snatch them.<sup>113</sup>

An agreement to give up one's legal right is not hit by Section 23. The agreement in question was between the landlord and tenant. It was entered into during the pendency of eviction proceedings and stipulated that even if an eviction order was passed, the landlord would not evict the tenant. This was held to be not illegal or against public policy.<sup>114</sup> The court followed the Supreme Court ruling to the effect that what makes an otherwise legal agreement to be void is that its performance is impossible except by disobedience of law.<sup>115</sup>

The Employees' State Insurance Act, 1948 has been enacted for benefit of all the workers covered by it. Its provisions are meant to protect employees from employers. It is a matter of underlying public policy. Such beneficial rights cannot be contracted out either by employers or employees' union. Such contracts are void and unenforceable. Waiver of advantages conferred by law is opposed to public policy.<sup>116</sup>

### *Marriage of minor girl*

Where the consideration for a contract of sale was the expenses of the marriage of a minor girl, the arrangement was held to be opposed to public policy, being in violation of the Child Marriage Restraint Act.

### *Payment out of black money*

The Delhi High Court has held that a contract for the sale of goods whose tenor shows that the price was intended to be paid out of black money is not opposed to public policy and is, therefore, valid and enforceable.<sup>117</sup> The contract involved transfer of goods and payment of price and neither is opposed

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become surrendered would be contrary to law if it is destructive of those rights without alternative security.

112. *Hanamant Basappa Choudhari v Laxmawwa*, (2002) 5 Kant LJ 405.
113. *Geeta Satish Gokarna v Satish Shankerrao Gokarna*, AIR 2004 Bom 345. *Hanamant Basappa Choudhari v Laxmawwa*, (2002) 5 Kant LJ 405, surrender of rights under S. 125 CrPC, against public policy. *Vinita Devangan v Rakesh Kumar Devangan*, AIR 2010 NOC 117 Chh; *Mahesh Chandra Dwivedi v State of UP*, AIR 2009 NOC 205 (All), consent divorce, right to maintenance remains. It is lost only on remarriage or becoming self-sufficient.
114. *M.K. Usman Koya v C.S. Santha*, AIR 2003 Ker 191: (2003) 3 CLT 12.
115. *BOI Finance Ltd v Custodian*, (1997) 10 SCC 488: AIR 1997 SC 1952.
116. *RCC (Sales) (P) Ltd v ESI Corpn*, AIR 2015 Hyd 134.
117. *Anand Prakash Om Prakash v Oswal Trading Agency*, AIR 1976 Del 24.



to public policy, nor can it be said to be designed to hoodwink the revenue. And even if it could be so said, the seller who had delivered his goods, could always call for payment out of the innocent money of the buyer. An agreement to exclude the land of a company from notified urban areas has been held to be not against public policy.<sup>118</sup>

### *Grabbing of privileges by extraneous influences*

A sale of seats in a public institution, e.g., a medical college, is equally opposed to public policy. The Supreme Court has held that charging of capitation fee in consideration of admission to educational institutions is illegal and impermissible as it amounts to denial of citizen's right to education and is arbitrary and violative of Article 14 of the Constitution.<sup>119</sup> The Madras High Court did not permit the recovery of a sum of money paid to a person to enable him to procure a seat in a medical college. Any attempt to pervert selection by merit is highly injurious to public interest.<sup>120</sup> Money promised to a person to get the promisor declared as the heir of a wealthy *Nawab* has been held to be not recoverable.<sup>121</sup> The fulfilment of the promise involved influencing statesmen for private gain, which is the same thing as corruption. Money promised to be paid to a person for using his influence for obtaining a Government order in favour of a manufacturer for supply of spare parts, or to secure a mining right are in the same category.<sup>122</sup> A contract between *A* and *B* for wielding influence with the Government authorities to secure a decision in favour of *B* has been held by the Supreme Court to be opposed to public policy.<sup>123</sup> Money paid under such a contract is not allowed to be recovered.<sup>124</sup>

### *Price escalation and interest clauses*

On account of price instabilities, it has become usual to allow suppliers and project contractors the benefit of price adjustment where the market price increases to such an extent that it would be unreasonable to ask anybody to go on performing at the originally reserved prices. The Development Authorities can make such adjustments according as the market of selling plots or houses fluctuates. If an Authority is forced under a court order to pay more compensation for acquisition, it can recoup from allottees with whom the deal is still not finalised. The Authority can also categorise the beneficiaries of its services, for example, into auction-purchasers and

118. *Associated Cement Companies Ltd v State of Rajasthan*, AIR 1981 Raj 133. *T.T. Augustine v Changanacherry Municipality*, AIR 1982 Ker 307, raffles are not opposed to public policy.

119. *Mohini Jain v State of Karnataka*, (1992) 3 SCC 666: AIR 1992 SC 1858.

120. *N.V.P. Pandian v M.M. Roy*, AIR 1979 Mad 42.

121. *Ratanchand Hirachand v Askar Nawaz Jung*, AIR 1976 AP 112.

122. *Kuju Collieries Ltd v Jharkhand Mines Ltd*, (1974) 2 SCC 533: AIR 1974 SC 1892; *Sita Ram v Radha Bai*, AIR 1968 SC 534: (1968) 1 SCR 805.

123. *Rattan Chand Hira Chand v Askar Nawaz Jung*, (1991) 3 SCC 67.

124. *Montefiore v Menday Motor Components Co Ltd*, (1918) 2 KB 241.

allottees. Demanding more price from allottees only does not constitute a discrimination. The allottees may be further categorised into economically stronger or weaker sections. Lesser prices from weaker sections does not in itself violate the constitutional guarantee of equality.<sup>125</sup>

### *Agreements contrary to public policy of friendly foreign state*

The public policy of a friendly foreign country where the agreement in question has to be performed can be taken into account while enforcing the agreement in England. This principle was laid down by the court of Queen's Bench Division in *Lemenda Trading Co Ltd v African Middle East Petroleum Co Ltd*.<sup>126</sup> An oil company in England wanted renewal of a supply contract with the Qatar National Oil Company. For this purpose, it entered into an agreement with the plaintiff company which undertook to bring about the renewal by using their influence with the officers of Qatar and this, in return, for a commission on oil supplies. Such commission was against public policy under the law of Qatar. The supply was renewed and an action was commenced in England to recover the agreed commission. The court said that recovery would not be allowed. The public policy of a friendly foreign State cannot, of course, of itself prevent the enforcement of a contract in England, but even so, an English court would not enforce a contract related to a transaction which is contrary to English public policy founded on general principles of morality and the same public policy is applicable in the friendly foreign country where the contract was to be performed so that the contract would not be enforceable under the law of that country, because in such circumstances the international comity combined with the English domestic public policy would militate against enforcement. Since a contract for the use of personal influence in return for money in circumstances where the person to be influenced is likely to be unaware of the pecuniary motive involved is contrary to public policy in both England and Qatar, such contract would not be enforced in England.<sup>127</sup> The court cited the following passage from the judgment of HALSBURY LC:<sup>128</sup> "Where a

125. *Vipul Rai Sharma v Ludhiana Improvement Trust*, AIR 1992 P&H 42.

126. 1988 QB 448.

127. The court noted *Norman v Cole*, (1800) 3 ESP 253: 170 ER 606, money paid for using the influence of the recipient for securing pardon for murder not allowed to be recovered back; *Montefiore v Menday Motor Components Co Ltd*, (1918) 2 KB 241, a claim for commission for procuring from the Government a loan to be used for manufacturing aircraft components, not allowed.

128. *Missouri SS Co, re*, (1889) LR 42 Ch D 321, 336 (CA). The court also cited *Kaufman v Gerson*, (1904) 1 KB 591 (CA). In that case: "A Frenchman coerced a Frenchwoman into signing a contract in France by the threat that if she refused to sign he would prosecute her husband for a crime of which he was accused." The contract was valid by French law, but an action brought for its breach in England was dismissed on the ground that to enforce it "would contravene what by the law of this country is deemed an essential moral interest". Presumably, therefore, an English court would apply the rule that has been laid down in the United States of America and would refuse to enforce any contract which tended to promote

contract is void on the ground of immorality, or is contrary to such positive law as would prohibit the making of such a contract at all, then the contract would be void all over the world, and no civilised country would be called on to enforce it."

### *Alienation of land by member of depressed class*

A portion of land was assigned by the Government to a depressed class member in fulfilment of its Constitutional obligation under Article 39(b). The grant was subject to the specific condition that the land would not be alienated. Because of the violation of this condition and because of the public policy implication, the alienation of the land was held to be of no effect.<sup>129</sup> A land allotted on the basis of Scheduled Caste was put under 20 year restriction on disposal. This was held to be valid. A transfer in violation of the applicable Rules was naturally invalid. The Rules permitted mortgage in favour of banking companies and recognised financial institutions for raising a loan.<sup>130</sup>

Such restrictions are in the interest of the assignees of lands and are based upon public policy to meet guaranteed social needs. They do not operate as a clog. They are intended to make assignees full owners.<sup>131</sup> Any such restriction which is not in the interest of the class to which the assignee belongs is likely to be declared void.<sup>132</sup>

### *Chitty*

The conduct of a *chitty* in violation of Acts enacted in the interest of uniformity of practices was held to be not opposed to public policy within the meaning of Section 23. The cheques issued under the scheme were found to be issued for payment of legally enforceable debts. The dishonour of such cheques amounted to an offence under Section 138 of the Negotiable Instruments Act, 1881.<sup>133</sup>

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corruption in the public affairs of a foreign country, however irreproachable such conduct might be in the view of the foreign law as noted in Cheshire, Fifoot and Furmston, *LAW OF CONTRACT*, pp. 370–71.

129. *Papaiah v State of Karnataka*, (1996) 10 SCC 533: AIR 1997 SC 2676. In *Paresar v Municipal Board, Mt. Abu*, 1997 AIHC 1897 Raj, regularisation of encroachment colonies for 10 years with restriction on alienation, not against public policy. Presumption that State decisions are in public interest and for public good. *Jaipur Development Authority v Daulat Mal Jain*, (1997) 1 SCC 35, allottee of land after acquisition, subsequent sale of that land to others described as sub-awardees or nominees was held to be opposed to public policy.
130. *Jit Singh v Piara*, (2003) 4 ICC 275 (P&H). *Jayamma v Maria Bai*, (2004) 7 SCC 459: AIR 2004 SC 3957, transfer by will also falls within the spell of prohibition.
131. *Land Acquisition Officer v Mekala Pandu*, (2004) 3 CTC 19 (Larger Bench).
132. *Bhavani Amma Kanakadevi v CSI Dekshina Kerala Maha Idavaka*, AIR 2008 Ker 38, a sale deed contained a provision that the assignee would return the land if he failed to build a college and not otherwise transfer it, hold against public policy, not enforceable, free right of transferring property is protected by S. 10 of the Transfer of Property Act.
133. *Nadarajan v Nadarajan*, (1999) 2 KLT 512.

### *Arbitration award induced by fraud or corruption*

An arbitration award induced by fraud or corruption has been held to be against public policy. It is therefore liable to be set aside under Section 34(2) (b)(11), Explanation of the Arbitration and Conciliation Act, 1996.<sup>134</sup>

### *Things done under statutory provisions*

Banking business includes recovery. The assignment of a debt and a non-performing asset by SBI to a banking company under the provisions of an Act with right to recover the debt was held to be a valid transaction. The transaction in question was neither prohibited under the Transfer of Property Act nor it was violative of public policy.<sup>135</sup> Things expressly permitted by law cannot be held as opposed to public policy. In this case there was a transaction in derivatives, which is a financial instrument used to transfer or hedge the risk. This was permitted by Master Circulars issued by the Reserve Bank from time to time and Regulations framed under FEMA, 1999.<sup>136</sup>

**Divorce by mutual consent.**—The parties to a marriage entered into a compromise over their marriage which had already suffered irretrievable breakdown with no chance of reunion between them. According to the terms of the settlement, the husband had already deposited the entire amount of permanent alimony and returned all articles of *streedhan* to the wife. The compromise was voluntary and without any coercion or undue influence. The court granted divorce.<sup>137</sup>

### *Heads of public policy*

#### 1. TRADING WITH ENEMY

“The King’s subjects cannot trade with an alien enemy, i.e. a person owing allegiance to a Government at war with the King, without the King’s licence.”<sup>138</sup> “It is now fully established that the presumed object of war being as much to cripple the enemy’s commerce as to capture his property, a declaration of war imparts a prohibition of commercial intercourse and correspondence with the inhabitants of the enemy’s country, and that such intercourse, except with the licence of Crown, is illegal”.<sup>139</sup> “The doctrine applies to all contracts which involve intercourse with the enemy or tend to assist the enemy, even though no enemy be a party to the contract.”<sup>140</sup>

134. *Venture Global v Satyam Computer Services Ltd*, (2010) 8 SCC 660: AIR 2010 SC 3371.

135. *Kotak Mahindra Bank Ltd v Chopra Fabricator & Mfr. P Ltd*, AIR 2011 All 19. The transfer was under the Securitisation and Enforcement of Security Interest Act, 2002.

136. *Rajshree Sugars and Chemicals Ltd v Axis Bank Ltd*, AIR 2011 Mad 144.

137. *Bipin Kumar Samal v Minarva Swain*, AIR 2016 Ori 41.

138. Lord MACNAGHTEN in *Janson v Driefontein Consolidated Mines Ltd*, 1902 AC 484, 499.

139. *Espostio v Bowden*, 110 RR 822, 823.

140. *Badische Co, re*, (1921) 2 Ch 331, 373. For Indian authorities see: *Banghy Abdul Razak v Khandi Rao*, 40 IC 851, 852; *R.K. Motishaw v Mercantile Bank of India*, 37 IC 258; *Wolf & Sons v Dadybha Khimji & Co*, ILR (1919) 44 Bom 631.

## 2. TRAFFICKING IN PUBLIC OFFICES

An agreement by which it is intended to induce a public officer to act corruptly is contrary to public policy. An agreement, for example, by which a sum of money was provided to a charity on the condition that latter would procure a knighthood for the plaintiff was held void and the money irrecoverable.<sup>141</sup> Similarly, an agreement to provide money to a member of Parliament to influence his judgment is void.<sup>142</sup> Sale of public offices, that is, appointments in consideration of money, are also against public policy. The sale of the office of a Shebait has been held invalid.<sup>143</sup> Charging of capitation fee for admission to prestigious educational institutions is contrary to public policy. The Supreme Court has described it as unreasonable, unjust and unfair.<sup>144</sup>

## 3. INTERFERENCE WITH ADMINISTRATION OF JUSTICE

A contract, the object of which is to interfere with the administration of justice, is obviously opposed to public policy. It may take any of the following forms:

(a) *INTERFERENCE WITH THE COURSE OF JUSTICE.*—Any agreement which obstructs the ordinary process of justice is void.<sup>145</sup> An agreement to delay the execution of a decree,<sup>146</sup> and a promise to give money to induce a person to give false evidence,<sup>147</sup> have been held void. An extreme illustration is an agreement to perform “puja” to secure success to the defendant in a litigation, which was held void.<sup>148</sup>

(b) *STIFLING PROSECUTION.*—It is in public interest that criminals should be prosecuted and punished. Hence, an agreement not to prosecute an offender or to withdraw a pending prosecution is void if the offence is of public

141. *Parkinson v College of Ambulance Ltd*, (1925) 2 KB 1.

142. *Marshall v Baltimore & Ohio Railroad Co*, 14 L Ed 953: 57 US (16 How) 314 (1853). There should be a clear proof of illegal intention. See *Manindra Chandra Nandi v Aswini Kumar Achariya*, AIR 1921 Cal 185 and *Shivsaran Lal v Keshav Prasad*, AIR 1917 Pat 92.

143. *Narasimma Thattha Acharya v Anantha Bhatta*, ILR (1881) 4 Mad 391; cf. *Mancharan v Pran Shanker*, ILR (1882) 6 Bom 298. See also *Ruppa Gurkul v Dorasami*, ILR (1882) 6 Mad 76; *Wahid Ali v Ashraf Hussain*, ILR (1882) 8 Cal 732 and *Anjaneyalu v Venuegopala Rice Mills Ltd*, ILR (1922) 45 Mad 620; in all of which sale of religious offices was disapproved. For other illustrations of sale of public appointments see *Ranjitsingh Murlisingh v Ramlal Shivalal*, AIR 1951 MB 113; *Ledu Coachman v Hiralal Bose*, (1914–15) 19 CWN 919: (1915) 29 IC 625; *Samintha Aiyar v Mathusami Pillai*, ILR (1907) 30 Mad 530, where an agreement to induce a public servant to retire was struck down. Where managing agents were induced to take a partner by bribe the agreement was held void. *Gulabchand v Kudilal*, AIR 1966 SC 1734: (1966) 3 SCR 623.

144. *Mohini Jain v State of Karnataka*, (1992) 3 SCC 666: AIR 1992 SC 1858.

145. FRY LJ remarked in *Windhill Local Board of Health v Vint*, (1890) LR 45 Ch D 351, 366 that “we cannot give effect to the agreement, the consideration of which is diverting the course of justice”.

146. *Nand Kishore v Kunj Behari Lal*, AIR 1933 All 303.

147. *Ko Pa Tu v Azimulla*, AIR 1940 Rang 73; *Abhiraja Shatty v Vittal Bhatta*, AIR 1914 Mad 366.

148. *Bhagwan Das Shastri v Raja Ram*, AIR 1927 All 406.

nature. Such agreements are called agreements to stifle prosecution. "You shall not make a trade of a felony."<sup>149</sup> "No court of law can countenance or give effect to an agreement which attempts to take the administration of law out of the hands of the judges and put it in the hands of the private individuals."<sup>150</sup> However, the law allows compromise agreements in respect of compoundable offences.<sup>151</sup> But the compromise of a non-compoundable offence is not allowed. An illustration is to be found in the decision of the Supreme Court in *Narasimharaju v Gurumurthy Raju*.<sup>152</sup>

In the dissolution and settlement of accounts of a partnership firm, one of the partners filed criminal complaints against his co-partners alleging forgery in and manipulation of accounts by taking in a fake partner. Subsequently, the partners entered into an agreement to refer the matter to arbitration in pursuance of which the complainant did not offer any evidence and his complaint was accordingly rejected. When the question of enforcement of the arbitrator's award arose, it was alleged that the reference to arbitration was the result of an agreement to stifle prosecution.

GAJENDRAGADKAR J (afterwards CJ) held the agreement to be opposed to public policy. He said: "If a person sets the machinery of criminal law into action on the allegation that the opponent has committed a non-compoundable offence and by the use of the coercive criminal process, he compels the opponent to enter into an agreement, that agreement would be treated as invalid for the reason that its consideration is opposed to public policy". The learned judge referred to the decision of the Privy Council in *Bhowanipur Banking Corpn Ltd v Durgesh Nandini Dassi*,<sup>153</sup> where a mortgage was executed by the respondent as a part of the consideration for a promise by the bank to withdraw criminal proceedings instituted by it against the mortgagor's husband and the bond was held invalid, notwithstanding that the debt itself was real and valid. Lord ATKIN observed:

149. Lord WESTBURY in *Williams v Bayley*, (1866) LR 1 HL 200, 220. See also *Keir v Leeman*, (1846) 9 QB 371, 392; (1844) 6 QB 308, where at pp. 316 and 322 Lord DENMAN LC cited the principle laid down by WILMOT CJ in *Collins v Blantern*, (1767) 2 Wils 341 that a contract to withdraw a prosecution for perjury, and consent to give no evidence against the accused is founded on an unlawful consideration. *Newar Marble Industries (P) Ltd v Rajasthan SEB*, 1993 Cri LJ 1191 (Raj), compounding the offence of theft of energy, held to be against public policy.

150. MUKHERJI J in *Sudhindra Kumar v Ganesh Chandra*, ILR (1939) 1 Cal 241, 250.

151. See S. 345, CrPC and Ss. 213–14, IPC.

152. AIR 1963 SC 107: (1963) 3 SCR 687. See also *Marai Packiam v Vallaimmal*, 1989 SCC OnLine Mad 301: (1990) 1 LW 449, criminal proceedings which cannot be compromised without court permission; *John Jacob v Joseph Joseph*, (1990) 1 KLT 75 where the court observed that a document executed by parties to settle the disputes between them and thereby to bring peace and good neighbourly relations can, under no stretch of imagination, be considered as an agreement to stifle litigation. *Sribari Jena v Khetramohan Jena*, AIR 2002 Ori 195: (2002) 94 CLT 201 (Ori), a deed executed with the intention of compromising some criminal cases between the parties pending before courts, hit by provisions of S. 23.

153. (1941) 54 LW 529: AIR 1941 PC 95.

To insist on reparation as a consideration for promise to abandon criminal proceedings is a serious abuse of the right of private prosecution. The citizen who proposes to vindicate the criminal law must do so whole-heartedly in the interest of justice, and must not seek his own advantage.<sup>154</sup>

Where a compromise agreement is made before any complaint is filed, it would not amount to stifling prosecution, even if it is implemented after the filing of a complaint which is then withdrawn. This was pointed out by the Supreme Court in *Ouseph Poulo v Catholic Union Bank Ltd.*<sup>155</sup>

A bank found that the goods in a godown, which was pledged to it against a loan, were either fraudulently overvalued or withdrawn in collusion with bank officials. The borrowers agreed to make up for the deficiency by hypothecating more property. Some delay having taken place in the hypothecation, the bank filed a complaint which was withdrawn after the hypothecation was completed.

GAJENDRAGADKAR CJ did not agree with the contention that the agreement involved any idea of stifling prosecution. The agreement was entered into before the complaint was filed, and so, it would be unreasonable to suggest merely from the sequence of subsequent events that the documents in question was executed with the object of stifling the criminal prosecution.

Approving cases of this kind in its decision in *Union Carbide Corp v Union of India*,<sup>156</sup> the Supreme Court pointed out the distinction between “motive” and “consideration” for withdrawing a prosecution. “Where dropping of the criminal proceedings is a motive for entering into the agreement—and not its consideration—the doctrine of stifling of prosecution is not attracted. Where there is also a pre-existing civil liability, the dropping of criminal proceedings need not necessarily be a consideration for the agreement to satisfy that liability.”<sup>157</sup> Where withdrawal of a prosecution is the motive but not the object or consideration of the contract, public policy is not affronted. The settlement of the Bhopal gas disaster was, therefore, valid.”

An agreement not to appear as a witness is void.<sup>158</sup>

(c) MAINTENANCE AND CHAMPERTY.—Explaining “maintenance” Lord HALDANE says: “It is unlawful for a stranger to render officious by money

154. *Elamma v Fr Joseph Arnachani Olikkan*, (2003) 2 KLT 536: (2003) 4 ICC 279, the falsity was known to both parties, threat of filing a false suit is really a form of blackmail and cannot be regarded as good consideration for an agreement to abstain from doing so.

155. AIR 1965 SC 166: (1964) 7 SCR 745. To the same effect is *R. Sivaram v T.A. John*, AIR 1975 Ker 101, where price was accepted from an employee who committed theft of articles.

156. (1991) 4 SCC 584: AIR 1992 SC 317, 288.

157. Citing *Adhikanda Sahu v Jogy Sahu*, AIR 1922 Pat 502; *Deb Kumar Ray Choudhury v Anath Bandhu Sen*, AIR 1931 Cal 421 where it was held that a contract for payment of money in respect of a criminal prosecution was permissible, was not by itself opposed to public policy; *Babu Harnarian Kapur v Babu Ram Swarup Nigam*, AIR 1941 Oudh 593.

158. *State of U.P. v Kapil Deo Shukla*, (1972) 3 SCC 504: AIR 1973 SC 494.

or otherwise to another person in a suit in which that third person has himself no legal interest, for its prosecution or defence.”<sup>159</sup> “Champerty” in its essence means “a bargain whereby one party is to assist the other in recovering property, and is to share in the proceeds of the action”.<sup>160</sup> “Agreements by which a stranger advances money for maintenance of litigation with a view to obtaining an unconscionable gain are called champertous agreements.”<sup>161</sup> The MP High Court observed that in India there is no law prohibiting champertous agreements as that in England. But a number of High Courts in India have been of the view that the English principle is applicable.<sup>162</sup> In *Harilal Nathalal Talati v Bhailal Pranlal Shah*<sup>163</sup> the Division Bench of the Bombay High Court dealt with an agreement in which a person had agreed to give half share of the property to the financier, valued at Rs 30,000 from such property as he might get whether by a suit or by private settlement or in any other manner from his father’s estate. The court held that the agreement was extortionate and unconscionable and opposed to public policy. An agreement which provided that the financier should get  $\frac{3}{4}$  of the property was not regarded as reasonable or fair.<sup>164</sup> A fair agreement to assist a person in the enforcement of his legal rights may be held valid even if the person providing the assistance is to be reimbursed out of the proceeds of the action.<sup>165</sup> Much, however, depends upon the quantum of share which the financier has stipulated to get in the fruits of the action. A stipulation for  $\frac{3}{4}$ th share in the property, if recovered, has been held to make the agreement champertous.<sup>166</sup> On the other hand, in *Ram Swarup v Court of Wards*,<sup>167</sup> which went up to the Privy Council, the agreement provided that the financier should bear all the expenses of the case and in return therefore get a three-anna share of the immovable property recovered provided that it should be increased to four annas, should the case go to the

159. *Neville v London Express*, 1919 AC 368.

160. *Hutley v Hutley*, (1873) LR 8 QB 112, per BLACKBURN J. *Kamrunnisa v Pramod Kumar Gupta*, AIR 1997 MP 106, agreement to finance litigation on the condition that the entire share of the decretal property would go to the financier, held, extortionate and against equity and justice, could not be enforced specifically. *Vatsavaya Venkata Subhadeayyamma Jagapati Bahadur Guru v Poosapati Venkatapati Raju Garu*, (1924–25) 52 IA 1: (1924) 20 LW 298: AIR 1924 PC 162 to the effect that champerty by itself does not make the agreement unlawful. *Rajah Mokham Singh v Rajah Rup Singh*, (1892–93) 20 IA 127, champerty becomes opposed to public policy if the agreement is not just and equitable.

161. *Khaja Moinuddin Khan v S.P. Ranga Rao*, AIR 2000 AP 344 at p. 346.

162. *Gayabai v Shriram*, (2005) 3 Civ LT 420 (MP).

163. AIR 1940 Bom 143.

164. *Nuthaki Venkataswami v Katta Nagi Reddy*, AIR 1962 AP 457, The Allahabad High Court in *Babu Ram v Ram Charan Lal*, AIR 1934 All 1023 dealt with an agreement which provided for 50 per cent share for the financier and held that the suit was opposed to public policy. In *Vatsavaya Venkata Jagapati v Poosapati Venkatapati*, (1924–25) 52 IA 1, where the agreement was found to be champertous but the amount actually spent by the financier was allowed to be recovered by creating a charge in his favour on the proceeds.

165. *Fischer v Kamala Nicker*, (1860) 8 MIA 170; *Bhagwat Dayal Singh v Devi Dayal Sabu*, (1907–08) 35 IA 48. *Banwarilal v Deenathan*, ILR 1954 MP 337.

166. *Nuthaki Venkataswami v Katta Nagi Reddy*, AIR 1962 AP 457.

167. ILR 1940 Lah 1 (PC).

Privy Council, the agreement was held to be valid. Similarly, agreements to pay 3/6th share;<sup>168</sup> 1/4th share<sup>169</sup> and 1/8th share<sup>170</sup> have been upheld. But an agreement to pay 1/6th part of the property to be inherited has been held to be unlawful. The estate being very vast, even 1/6th would net Rs 3 lakhs for the promisee and this is exorbitant.<sup>171</sup> Principles that ensure justice, fair play, transparency, objectivity and probity in discharging public functions are facets of public policy, *i.e.* any rule, contract or arrangement that is in public good and public interest.<sup>172</sup> An agreement to pay to the financier 40 per cent of the value of the property in question or its sale proceeds was held to be of champertous nature.<sup>173</sup> Where the property forming the subject-matter of litigation is agreed to be sold to the financier, the mere fact that the consideration for the sale is inadequate, may not render the agreement champertous.<sup>174</sup>

An agreement by a client to pay his lawyer according to the result of the case is against public policy. "It is professional misconduct for an advocate to stipulate for or agree with his client to accept as his fee or remuneration a share of the property sued or other matter in litigation upon the successful issue thereof."<sup>175</sup> An agreement for solicitor retainership on the basis that the solicitors' standard remuneration would be paid on successful cases and there would be 20 per cent reduction of their fee for lost cases has been held to be champertous. Neither the amount not paid, could be recovered, nor the fee amounts already paid could be claimed back. The court said that a contingency fee which is contrary to public policy is not confined to a direct or indirect share of the spoils but it includes a differential fee dependent on the outcome of the litigation.<sup>176</sup>

#### 4. MARRIAGE BROKAGE CONTRACTS

An agreement to procure the marriage of a person in consideration of a sum of money is called marriage brokerage contract. Such agreements are void. A typical illustration would be an agreement for the sale of a girl.<sup>177</sup> The custom of paying bride price to the parents of a girl is well-known in India. According to decisions of the Punjab,<sup>178</sup> Calcutta<sup>179</sup> and Madras<sup>180</sup>

168. *Vatsavaya Venkata Subhadeayyamma Jagapati Bahadur Guru v Poosapati Venkatapati Raju Garu*, (1924-25) 52 IA 1: (1924) 20 LW 298: AIR 1924 PC 162.

169. *Valluri Ramanamma v Marina Viranna*, (1931) 33 MLW 757: AIR 1931 PC 100.

170. *Rajah Mokham Singh v Rajah Rup Singh*, (1892-93) 20 IA 127.

171. *Ratanchand Hirachand v Askar Nawaz Jung*, AIR 1976 AP 112.

172. *BCCI v Cricket Assn of Bihar*, (2015) 3 SCC 251, members of a deciding committee cannot have personal interest.

173. *Khaja Moinuddin Khan v S.P. Ranga Rao*, AIR 2000 AP 344.

174. *Unnao Commercial Bank v Kailash Nath*, AIR 1955 All 393.

175. *Kathu Jairam Gujjar v Vishvanath Ganesh Javadekar*, AIR 1925 Bom 470.

176. *Aratra Potato Co Ltd v Taylor Joynson Garrett*, (1995) 4 All ER 695.

177. *Girdhari Singh v Neeladhar Singh*, (1972) 10 All LJ 159.

178. *Wazarimal v Rallia*, 1889 Punj Rec No. 128.

179. *Baldeo Das Agarwalla v Mohamaya Persad*, (1911) 15 CWN 447.

180. *Kalavagunta Venkata Kristnayya v Kalvagunta Lakshmi Narayana*, ILR (1909) 32 Mad 185.

High Courts, an agreement to pay money to the parent of a minor to induce him to give the minor in marriage is void. Where, however, the money has already been paid, but the marriage fails to go through, it has been held in a few cases that the money may be taken back.<sup>181</sup>

An attempt to make gain of material nature out of a marriage would be equally opposed to public policy. When a father or other guardian of a boy or girl has to betroth his ward, his primary and only consideration ought to be happiness and welfare of the child. The stipulating for a monetary payment for himself is an incentive to the parent or other guardian to have regard to other considerations than the child's happiness in marrying him or her into another family. Such an agreement would clearly be invalid.<sup>182</sup>

A decision of the Orissa High Court provides a suitable illustration:<sup>183</sup>

The defendant proposed the marriage of his widowed niece to the plaintiff and offered to give her gold and jewels and land. The marriage took place, but the defendant refused to fulfil the rest of his promise.

The court observed: We would like to make it clear at the outset that if gifts or presents to the groom or the bride are made voluntarily it cannot be attacked as anything immoral or opposed to public policy. But if pecuniary gain is made the consideration of marriage, it is bound to be condemned as reprehensible to all sense of decent morals. In the present case, monetary gain was the sole consideration for the marriage between the two.<sup>184</sup>

Inter-caste marriage arrangements have been held to be valid.<sup>185</sup>

## 5. UNFAIR, UNREASONABLE OR UNCONSCIONABLE DEALINGS

[*Dealings with employees*]

Where the parties are not economically on equal footing and there is a wide gap in the bargaining power of the parties, where one of them is in a position to exploit and the other is vulnerable and the contract made with that other is apparently unfair, it can in circumstances be also regarded as opposed to public policy. For example, the Supreme Court laid down in *Central Inland Water Transport Corpn v Brojo Nath Ganguly*<sup>186</sup> that



CASE PILOT

181. *Ganpat v Lahana*, AIR 1928 Nag 89; *Gopi Krishna Prasad v Janak Prasad*, AIR 1951 Pat 519.

182. *Per FARRAN CJ in Dholidas v Fulchand Chhagan*, ILR 22 Bom 658.

183. *A. Suryanarayan Murthi v P. Krishna Murthy*, AIR 1957 Ori 125.

184. MOHPATRA J who relied upon *Kalavagunta Venkata Kristnayya v Kalavagunta Lakshmi Narayana*, ILR (1909) 32 Mad 185. For a reappraisal of the concept of public policy as it affects insurance claims and the principle that no one should benefit from his own wrong, see John Shand, *Unblinking the Unruly Horse; Public Policy in the Law of Contract*, (1972-A) Camb LJ 144. See also Goodhart, *ENGLISH LAW AND THE MORAL LAW*, p. 10 and Devlin, *THE ENFORCEMENT OF MORALS*, pp. 43–44.

185. *Amirchand v Ram Rattanchand*, 1903 Punj Rec No. 50.

186. (1986) 3 SCC 156: AIR 1986 SC 1571. In its judgment in *Sethani v Bhana*, 1993 Supp (4) SCC 639: AIR 1993 SC 956, the Supreme Court held that where a sale deed of her property was executed by an old, illiterate and blind tribal woman in favour of the person on whom she was dependent till death, the donee would have to prove bona fides of the transaction. *Gujarat Water Supply & Sewerage Board v Pagi Malabhai Andarbhai*, (2004) 2 GCD 923

a Government corporation imposing upon a needy employee a term that he can be removed just by three months' notice or pay in lieu of notice and without any ground is an exploitation and every ruthless exploitation is against public policy.<sup>187</sup> The Allahabad High Court distinguished this case in *Jagat Bahadur v District Supply Officer, Allahabad*<sup>188</sup> where the contract was for the allotment of a fair price shop for distribution of foodgrains and it contained a clause for termination of the agreement and withdrawal of the privilege without assigning any reasons. The same was held to be neither opposed to public policy nor violative of Article 14 of the Constitution. A person aspiring for the grant of a fair price shop is perfectly free not to enter into such a contract because he has all the opportunities of trading in the free foodgrain market. His position cannot be compared with that of an employee.<sup>189</sup>

A rule permitting administrators of Board of Control for Cricket in India (BCCI) to have commercial interest in events conducted by BCCI was held to be capable of defeating high ideals of fairness and objectivity in discharge of a public function and therefore opposed to public policy. It is liable to be struck down. The court said that principles that ensure justice, fair play, transparency, objectivity and probity in discharge of public functions are facets of public policy. A rule, contract or arrangement which is in public good and interest cannot be regarded as opposed to public policy.<sup>190</sup>

#### *Surreptitious transfer of shares*

In reference to the conduct of public financial institutions holding shares in companies, it has been held by the Supreme Court that a surreptitious transfer of a bulk of shares in one company without caring to see whether it would result in the creation of a monopoly adverse to public interest, if it is done with a mala fide intention, the deal would be illegal.<sup>191</sup>

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(Guj), the courts would strike down and refuse to enforce contracts which are unfair and unreasonable and employee is not in apposition of an equal bargaining power. A term which prevents an employee from enforcing his legal rights is taken to be contrary to public policy. *K. Madhu v Dugar Finance India Ltd*, (2006) 3 MLJ 713, finance for vehicle, reserving power of seizure of vehicle, against public policy.

187. See also *BCPP Mazdoor Sangh v NTPC*, (2007) 14 SCC 234: AIR 2008 SC 336, agreement under which service conditions of employees were altered and they were transferred from a public sector undertaking to a private concern was held to be opposed to public policy. *Bharti Airtel Ltd v Union of India*, (2015) 12 SCC 1, licence to provide a telecom service is a contract between the licensee and government.

188. AIR 1990 All 113.

189. See further, *DTC v Mazdoor Congress*, 1991 Supp (1) SCC 600: AIR 1991 SC 101, where a term in a contract of employment that a permanent worker was removable without inquiry was held to be opposed to public policy. *Hindustan Times v State of U.P.*, (2003) 1 SCC 591: AIR 2003 SC 250, deduction of 5 per cent amount from advertisement bill of newspapers imposed by the State Government which amount to form part of pension fund of working journalists, held arbitrary and violative of Art. 14.

190. *BCCI v Cricket Assn of Bihar*, (2015) 3 SCC 251.

191. *N. Parthasarathi v Controller of Capital Issues*, (1991) 3 SCC 153, arising out of the L&T mega issue.



### *Parties with matching bargaining powers*

As between parties whose bargaining power is fairly matched and the standard contract with all its clauses has not only been duly signed but also is one which has been widely used over the years, this will create a presumption of fairness.<sup>192</sup> Where experienced businessmen are involved in a commercial contract and there is no inequality of bargaining power, the agreed terms must ordinarily be respected as the parties must be taken to have had regard to the matters known to them. The sellers and buyers in this case were businessmen and they had agreed on all the terms on the basis that they were in conformity with international trade and commerce. The clause for reimbursement for or repayment of the price if the seller could not deliver the goods within the specified time was neither unreasonable nor unjust. It was also not extravagant. The Supreme Court said that the arbitration award on its basis could not be regarded as contrary to public policy.<sup>193</sup>

A clause enabling the contracting authority to vary the quantum of work upwards or downwards to be computed by adding up all variations both upwards and downwards has been held to be based on good reasons and there is nothing unconscionable if the power is exercised for legitimate causes.<sup>194</sup> A clause in a contract of hiring of three vessels for a period of three years entitled the hirer to terminate the agreement after one year without assigning any reason. The clause was held to be not unconscionable or opposed to public policy. It was also covered by Section 14(1)(c) and (e) of the Specific Relief Act, 1963.<sup>195</sup>

In the opinion of the Karnataka High Court<sup>196</sup> in order to attract Section 23 of the Act, it is not necessary that the contract should be tainted with illegality. It would be enough if it contains terms which are so unfair and unreasonable that they shock the conscience of the court. But this general observation has been held to be not applicable where a guarantor agrees not to claim the benefit of Sections 133, 134, 135, 139 and 141 of the Act which give to the guarantor certain protective rights. Such rights being variable with the consent of the surety, there is no violation of the Act if he agrees not to claim any of those rights.<sup>197</sup>

192. *Bihar State Electricity Board v Green Rubber Industries*, (1990) 1 SCC 731, 740: AIR 1990 SC 699.

193. *Phulchand Exports (P) Ltd v O.O.O. Patriot*, (2011) 10 SCC 300.

194. *National Fertilizers v Puran Chand Nangia*, (2000) 8 SCC 343: AIR 2001 SC 53. *Societe Pepper Grenolde v Union of India*, AIR 2004 Del 376, a clause that only one party will appoint arbitrator has been held to be valid.

195. *ONGC Ltd v Streamline Shipping Co (P) Ltd*, AIR 2002 Bom 420.

196. *City Municipal Council v C. Ramu*, ILR 1989 KAR 2138 and *Suresh Mahajan v Myveneers*, ILR 1990 Kant 2910.

197. *T. Raju Setty v Bank of Baroda*, AIR 1992 Kant 108, not agreeing with *Union of India v Pearl Hosiery Mills*, AIR 1961 Punj 281 where it was held that the operation of S. 133 could not be ousted. Followed in *Central Bank of India v Multi Block (P) Ltd*, AIR 1997 Bom 109, where it was held that waiver of surety's rights under Ss. 133, 134, 135, 139 and 141 was not against public policy. *Prentice Hall India (P) Ltd v Prentice Hall Inc*, AIR 2003 Del

A clause in a loan agreement permitting the financier to seize the financed vehicle in the event of default in payment was held to be void.<sup>198</sup> A clause in a bank loan agreement that in the event of pre-payment an extra interest would be charged was held to be arbitrary and unreasonable.<sup>199</sup>

An agreement for selling the recognition and no-objection certificate is opposed to public policy as the educational institution is granted recognition for the benefit of the public and if such right is sold like a tradable commodity without approval of the competent authority, it would be an act opposed to public policy and forbidden under Section 23 of the Contract Act.<sup>200</sup>

### VOID AGREEMENTS

Giving the meaning of a void agreement, the Act says in Section 2(g):

An agreement not enforceable by law is said to be void.

The following types of agreement are declared to be void:

- (1) Agreements of which consideration and objects are unlawful in part, [S. 24]
- (2) Agreements without consideration, [S. 25]
- (3) Agreements in restraint of marriage, [S. 26]
- (4) Agreements in restraint of trade, [S. 27]
- (5) Agreements in restraint of legal proceedings, [S. 28]
- (6) Unmeaning agreements, [S. 29]
- (7) Wagering agreements, [S. 30] and
- (8) Agreements to do impossible acts. [S. 56]

#### Agreements in which a part of consideration or object is unlawful

**S.24. Agreements void, if considerations and objects unlawful in part.**—If any part of a single consideration for one or more objects, or any one or any part of any one of several considerations for a single object, is unlawful, the agreement is void.

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236, assignment of copyright is permissible even under the Copyright Act and, therefore, there was nothing contrary to public policy in such assignments. *Thakar Kanaiyalal Rasiklal v State of Gujarat*, AIR 2003 Guj 14, under a settlement, the plaintiffs were allowed to perform *pooja* for 20 years in a temple. They enjoyed that right but after the expiry of 20 years, they claimed a hereditary right to continue *pooja*. The court said that the claim was barred by Order 23, Rule 1, CPC and was also against the principles of public policy. *K.E. Aboobacker v Vasu P.P.*, 2004 AIHC 551 (Ker): AIR 2004 NOC 262 (Ker) demand of premium (*pakidi*) by landlord for giving premises was held to be not only penal but also against morals and public policy. *Robit Dhawan v G.K. Malhotra*, AIR 2002 Del 151, doctrine of perpetuity could not be applied to an agency, because otherwise one party may completely ruin the business of the other.

198. *Tarun Bhargava v State of Haryana*, AIR 2003 P&H 98: ILR (2003) 1 P&H 26.

199. *Mahavir Ice & Cold Storage Ltd v Small Industries Development Bank of India*, AIR 2009 NOC 1218 (Ori DB).

200. *Evva Memorial Teacher Training Institute v National Council for Teacher Education*, (2008) 1 CTC 625.

*Illustration*

A promises to superintend, on behalf of B, a legal manufacturer of Indigo, and an illegal traffic in other articles. B promises to pay A, a salary of 10,000 rupees a year. The agreement is void, the object of A's promise, and the consideration for B's promise, being in part unlawful.

The working philosophy behind the provision was stated by WILLES J in these words:<sup>201</sup> Where you cannot sever the illegal from the legal part of a covenant the contract is altogether void, but where you can sever them whether the illegality be created by statute or by common law, you may reject the bad part and retain the good.

The section comes into play when a part of the consideration for an object or more than one objects of an agreement is unlawful. The whole of the agreement would be void unless unlawful portion can be severed without damaging the lawful portion. A promises to pay a fixed sum of money on monthly basis to a married woman for living in adultery with the promisor, which is unlawful, and for keeping his house, which is lawful, the whole agreement was held to be void because it was impossible to apportion the single lump sum between the lawful object and the unlawful one.<sup>202</sup> A licence was granted to a person for sale of opium and *ganja* with this restriction that he would not take any partner in the *ganja* business without the permission of the collector. Without such permission he admitted a partner into the whole business on receiving from him a fixed sum as his share of capital. Differences arose between them. The new entrant filed a case for dissolution and refund of his money. His claim was not allowed. The court said that "it is impossible to separate the contract or to say how much capital was advanced for the opium and how much for the *ganja*".<sup>203</sup> A Municipal Corporation granted to a contractor for a lump sum the licence to collect toll from pilgrims and vehicles and animals. It had no power to authorise collection of fees from pilgrims. The whole transaction was held to be void.<sup>204</sup>

Where the legal part of an agreement is severable from the illegal, the former would be enforced. A Muslim husband agreed by a registered deed to handover to his wife the totality of his earnings and not to do anything without her permission and, if he did so, she would be at liberty to divorce him. The latter part of the agreement was unlawful. It was severed from that part under which he promised to handover all earnings and this part was enforced giving it this meaning that he was bound to give only maintenance amount and not every bit that he might earn.<sup>205</sup> Transactions arising out of an agreement to do an illegal act, if they are such that when taken

201. *Pickering v Illfracombe Rly Co*, (1868) LR 3 CP 235, 250.

202. *Alice Mary Hill v William Clarke*, ILR (1905) 27 All 266.

203. *Gopalrao v Kallappa*, (1901) 3 Bom LR 164.

204. *Saundatti Yellama Municipality v Shripad bhat Seshbhat Joshi*, AIR 1933 Bom 132; ILR (1933) 57 Bom 278. See also *Tong Kheng Bros v Anuarul Aini*, (1990) 2 CLJ 715 High Court, Penang, an agreement to lease a licensed forest contract and its sawmill, held to be unlawful, such transfer being possible only with prior written approval.

205. *Poonoo Bibi v Fyaz Buksh*, 1874 SCC OnLine Cal 59: (1874) 15 L Beng LR App 5.

separately from the illegal act, they would be valid, they would remain valid and enforceable notwithstanding the illegality of the agreement.<sup>206</sup>

A prohibition of forward transactions in securities was held to be not applicable upon that part of the transaction which was for ready delivery (spot delivery), this part being separable from the other part.<sup>207</sup> If a contract is, on the face of it, capable of legal performance, the fact that one party was entertaining an undisclosed intention of performing it unlawfully or of using it as a part of an unlawful scheme, would not disentitle the other party from enforcing it. If there is any doubt about the real nature or purport of the agreement, that construction should be preferred which admits of lawful performance. The fact that one party entertains the motive of defeating the execution of the decree which may be passed against him is immaterial.<sup>208</sup>

### Agreements without consideration [S. 25]

Section 25 declares that an agreement without consideration is void. This is, of course, subject to a few exceptions, which have already been considered along with "consideration".

### Restraint of marriage [S. 26]

**S. 26. Agreement in restraint of marriage void.**—Every agreement in restraint of the marriage of any person, other than a minor, is void.

It is the policy of law to discourage agreements which restrain freedom of marriage. The restraint may be general or partial, that is to say, the party may be restrained from marrying at all, or from marrying for a fixed period, or from marrying a particular person, or a class of persons, the agreement is void. The only exception is in favour of a minor.<sup>209</sup>

A penalty upon remarriage may not be construed as a restraint of marriage. Thus, an agreement between two co-widows that if any of them remarried, she should forfeit her right to her share in the deceased husband's property has been upheld, the court pointing out that no restraint was imposed upon either of the two widows for remarriage. "All that was provided was that if a widow elected to remarry, she would be deprived of her rights."<sup>210</sup> Similarly, agreements that upon remarriage, the widow would lose the right to maintenance<sup>211</sup> and upon the husband marrying a second wife, the first would get the right to divorce him, have been upheld.<sup>212</sup>

206. *BOI Finance Ltd v Custodian*, (1997) 10 SCC 488; AIR 1997 SC 1952. *Canbank Financial Services Ltd v Custodian*, (2004) 8 SCC 355; AIR 2001 SC 2601.

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209. *Lowe v Peers*, (1768) 4 Burr 2225; *Maharam Ali v Aysha Khatun*, (1914–15) 19 CWN 1226, where a condition in a marriage arrangement that if the husband married another woman, the first wife would divorce him was upheld.

210. *Rao Rani v Gulab Rani*, ILR 1942 All 810.

211. *Latafatunnissa v Shaharbanu Begam*, AIR 1932 Oudh 108.

212. *Badu v Badarnessa*, (1919) 29 CLJ 230.

*Illustration*

A promises to superintend, on behalf of B, a legal manufacturer of Indigo, and an illegal traffic in other articles. B promises to pay A, a salary of 10,000 rupees a year. The agreement is void, the object of A's promise, and the consideration for B's promise, being in part unlawful.

The working philosophy behind the provision was stated by WILLES J in these words:<sup>201</sup> Where you cannot sever the illegal from the legal part of a covenant the contract is altogether void, but where you can sever them whether the illegality be created by statute or by common law, you may reject the bad part and retain the good.

The section comes into play when a part of the consideration for an object or more than one objects of an agreement is unlawful. The whole of the agreement would be void unless unlawful portion can be severed without damaging the lawful portion. A promises to pay a fixed sum of money on monthly basis to a married woman for living in adultery with the promisor, which is unlawful, and for keeping his house, which is lawful, the whole agreement was held to be void because it was impossible to apportion the single lump sum between the lawful object and the unlawful one.<sup>202</sup> A licence was granted to a person for sale of opium and *ganja* with this restriction that he would not take any partner in the *ganja* business without the permission of the collector. Without such permission he admitted a partner into the whole business on receiving from him a fixed sum as his share of capital. Differences arose between them. The new entrant filed a case for dissolution and refund of his money. His claim was not allowed. The court said that "it is impossible to separate the contract or to say how much capital was advanced for the opium and how much for the *ganja*".<sup>203</sup> A Municipal Corporation granted to a contractor for a lump sum the licence to collect toll from pilgrims and vehicles and animals. It had no power to authorise collection of fees from pilgrims. The whole transaction was held to be void.<sup>204</sup>

Where the legal part of an agreement is severable from the illegal, the former would be enforced. A Muslim husband agreed by a registered deed to handover to his wife the totality of his earnings and not to do anything without her permission and, if he did so, she would be at liberty to divorce him. The latter part of the agreement was unlawful. It was severed from that part under which he promised to handover all earnings and this part was enforced giving it this meaning that he was bound to give only maintenance amount and not every bit that he might earn.<sup>205</sup> Transactions arising out of an agreement to do an illegal act, if they are such that when taken

201. *Pickering v Illfracombe Rly Co*, (1868) LR 3 CP 235, 250.

202. *Alice Mary Hill v William Clarke*, ILR (1905) 27 All 266.

203. *Gopalrao v Kallappa*, (1901) 3 Bom LR 164.

204. *Saundatti Yellama Municipality v Shripadbhat Seshbhat Joshi*, AIR 1933 Bom 132: ILR (1933) 57 Bom 278. See also *Tong Kheng Bros v Anuarul Aini*, (1990) 2 CLJ 715 High Court, Penang, an agreement to lease a licensed forest contract and its sawmill, held to be unlawful, such transfer being possible only with prior written approval.

205. *Poonoo Bibi v Fyaz Buksh*, 1874 SCC OnLine Cal 59: (1874) 15 L Beng LR App 5.

separately from the illegal act, they would be valid, they would remain valid and enforceable notwithstanding the illegality of the agreement.<sup>206</sup>

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206. *BOI Finance Ltd v Custodian*, (1997) 10 SCC 488: AIR 1997 SC 1952. *Canbank Financial Services Ltd v Custodian*, (2004) 8 SCC 355: AIR 2001 SC 2601.

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211. *Latafatunnissa v Shaharbanu Begam*, AIR 1932 Oudh 108.

212. *Badu v Badarnessa*, (1919) 29 CLJ 230.

### RESTRAINT OF TRADE [S. 27]

**S. 27. Agreement in restraint of trade void.**—Every agreement by which any one is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void.

**Exception 1.—Saving of agreement not to carry on business of which goodwill is sold.**—One who sells the goodwill of a business may agree with the buyer to refrain from carrying on a similar business, within specified local limits, so long as the buyer, or any person deriving title to the goodwill from him, carries on a like business therein:

Provided that such limits appear to the Court reasonable, regard being had to the nature of the business.

### Protection of freedom of trade and commerce

Freedom of trade and commerce is a right protected by the Constitution of India. Just as the Legislature cannot take away individual freedom of trade, so also the individual cannot barter it away by agreement. “The principle of law is this: Public policy requires that every man shall be at liberty to work for himself, and shall not be at liberty to deprive himself or the State of his labour, skill or talent, by any contract that he enters into.”<sup>213</sup> “Every man should have unfettered liberty to exercise his powers and capacities for his own and the community’s benefit.”<sup>214</sup> Section 27, therefore, declares in plain terms that: Every agreement by which any one is restrained from exercising a lawful profession, trade or business of any kind, is, to that extent, void.<sup>215</sup>

### All restraints covered whether partial or general

*Madhub Chander v Raj Coomar*<sup>216</sup> is the first case in which the scope of the section came up for consideration before the Calcutta High Court.

The plaintiff and the defendant were rival shopkeepers in a locality in Calcutta. The defendant agreed to pay a sum of money to the plaintiff if he would close his business in that locality. The plaintiff accordingly did so, but the defendant refused to pay.

The plaintiff sued him for the money contending that the restraint in question was only partial as he was restrained from exercising his profession only in one locality and that such restraints had been upheld in English law. COUCH J, however, held the agreement to be void and laid down: The words “restrained from exercising a lawful profession, trade or business”, do not

213. *Per* JAMES VC in *Leather Cloth Co v Lorsont*, (1869) LR 9 Eq 345, 354: 39 LJ Ch 86.

214. *Vancouver Malt & Sake Brewing Co Ltd v Vancouver Breweries Ltd*, (1934) 39 LW 618: AIR 1934 PC 101.

215. *Electrosteel Castings Ltd v Saw Pipes Ltd*, (2005) 1 CHN 612, the words “lawful profession” in S. 27 include both an independent professional and a salaried professional. Self employment and all modes of economic survival or of earning one’s livelihood are covered.

216. (1874) 14 Beng LR 76.

mean an absolute restriction, and are intended to apply to a partial restriction, a restriction limited to some place.<sup>217</sup>

The learned judge drew support from the use of the word “absolutely” in Section 28, which deals with restraint of legal proceedings. As this word is absent from Section 27, therefore, he concluded, that it was intended to prevent not merely a total restraint but also a partial restraint. This interpretation of the section has been generally accepted. “The section has abolished the distinction between partial and total restraints of trade. Whether the restraint is general or partial, unqualified or qualified, if the agreement is in the nature of a restraint of trade, it is void.” Thus, an agreement to close a mill for 3 months in a year,<sup>218</sup> and an agreement that one party would sell beef for 14 days in a month and the other for the rest of the month,<sup>219</sup> have been held void.

### Developments in English Law

In England the law relating to restraint of trade was elaborately considered by the House of Lords in *Nordenfelt v Maxim Nordenfelt Guns & Ammunition Co.*<sup>220</sup>

The case involved a sale of goodwill by an inventor and a manufacturer of guns and ammunition who agreed with the buyer company: (1) not to practise the same trade for 25 years, and (2) not to engage in any business competing or liable to compete in any way with the business for the time being carried on by the company. He afterwards entered into agreement with another manufacturer of guns and ammunition and the company brought an action to restrain him.

It was held that first part of the agreement was valid being reasonably necessary for the protection of the purchaser's interest. But the rest of the covenant by which he was prohibited from competing with the company in any business that the company might carry on was held as unreasonable and, therefore, void. Lord MACNAGHTEN laid down: “The public have an interest in every person's carrying on his trade freely: so has the individual. All interference with individual liberty of action in trading, and all restraints of trade of themselves, if there is nothing more, are contrary to public policy and, therefore, void. That is the general rule. But there are exceptions. Restraint of trade... may be justified by the special circumstances of a particular case. The only justification is that the restriction should be reasonable—reasonable in reference to the interest of the parties and reasonable in reference to the public interest. The restriction should be so framed and

217. *Per Mookerjee and Candler JJ* in *Shaikh Kalu v Ram Saran Bhagat*, (1908–09) 13 CWN 388: 1 IC 94.

218. *Khemchand Manekchand v Dayaldas Bassarmal*, AIR 1942 Sind 114.

219. *Mohammad v Ona Mohd Ebrahim*, AIR 1922 Upper Burma 9.

220. 1894 AC 535.

guarded as to afford adequate protection to the party in whose favour it is imposed while at the same time it is in no way injurious to the public.”

### General principle in India and England same

Thus both in England and in India the general principle is the same, namely, that all restraints of trade whether partial or total, are void.<sup>221</sup> The only difference is that in England a restriction will be valid if it is reasonable. In India it will be valid if it falls within any of the statutory, or judicially created exceptions. To the extent to which these exceptions are an embodiment of the situations in which restraints have been found reasonable in England, the two laws are identical and not “widely dissimilar”.<sup>222</sup> The English law may be a little more flexible as the word “reasonable” enables the courts to adapt it to changing conditions. As Lord WILBERFORCE remarked in *Esso Petroleum Co Ltd v Harper's Garage (Stourport) Ltd*<sup>223</sup> “the classification (of agreements in restraint of trade) must remain fluid and the categories can never be closed”. The following passage in a judgment of the Supreme Court<sup>224</sup> shows the effect of absence of the test of “reasonableness”: “The question of reasonableness of restraint is outside the purview of Section 27 of the Contract Act and need not be gone into. Therefore, the present case has to be proceeded on the basis that an enquiry into reasonableness of the restraint is not envisaged by Section 27. On that view, instead of being required to consider two questions<sup>225</sup> as in England, the courts in India have

221. See, for example, Chitty on CONTRACT (GENERAL PRINCIPLES) (21st Edn) 481–82, where the learned writer says that “all contracts in restraint of trade are *prima facie* void, unless they are reasonable.” For Indian authority see PIGOT and MCPHELSON JJ in *Nur Ali Dubash v Abdul Ali*, ILR (1892) 19 Cal 765, 773, “S. 27 does away with the distinction between partial and total restraints of trade.”

222. MOOKERJEE and CARNDUFF JJ in *Sk Kalu v Ram Saran Bhagat*, (1909) 8 CWN 388, 392. The learned Judges said that as a result of the decision in the *Nordenfelt* case “the rule as embodied in S. 27 presents an almost startling dissimilarity to the most modern phase of the English rule on the subject”.

223. 1968 AC 269: (1967) 2 WLR 871 (HL).

224. *Gujarat Bottling Co Ltd v Coca Cola Co*, (1995) 5 SCC 545; AIR 1995 SC 2372: (1995) 84 Comp Cas 618.

225. The following passage in the judgment of the Supreme Court (*ibid.*) explains the position of two questions under English law: “Under the common law in England traditionally the doctrine of restraint of trade applied to covenants whereby an employee undertakes not to compete with his employer after leaving the employer’s service and covenants by which a trader who has sold his business agrees not thereafter to compete with the purchaser of the business. The doctrine is, however, not confined in its application to these two categories but covenants falling in these two categories are always subjected to the test of reasonableness. The general principle once applicable to agreements in restraint of trade has consequently been considerably modified by later decisions in England. The rule now is that restraints, whether general or partial, may be good if they are reasonable and any restraint on the freedom of contract must be shown to be reasonably necessary for the purpose of freedom of trade. A covenant in restraint of trade must be reasonable with reference to the public policy and it must also be reasonably necessary for the protection of the interest of the covenantee and regard must be had to the interests of the covenantor. Contracts in restraint of trade are *prima facie* void and the onus of proof is on the party supporting the contract to show that the restraint goes no further than is reasonably necessary to protect the interest of the

only to consider the question whether the contract is or is not in restraint of trade.”

### “Profession, trade or business”

But the Indian courts have not been rendered entirely sterile in the matter.<sup>226</sup> Thus, for example, where it was necessary to do so, the High Court of Kutch regarded an agreement to monopolise the privilege of performing religious services in a village as being opposed to public policy and void under Section 27,<sup>227</sup> though it may be doubted whether the words “profession, trade or business” as used in the section were intended to cover the religious services of a priest. On the other hand, the Allahabad High Court in *Pothi Ram v Islam Fatima*<sup>228</sup> upheld as valid a restrictive covenant on the ground that the activity restrained was not in the nature of “profession, trade or business”.

Two landlords in the same neighbourhood, in order to avoid competition, agreed that a market for sale of cattle shall not be held on the same day on the lands of both of them.

The High Court said: “It seems to us that a landlord who in return for tolls or fees, allows a cattle market to be conducted on his land is not thereby exercising trade or business of selling cattle. He is only a landholder and an agreement on his part not to use the land on a certain day for a certain purpose does not amount to restraint of ‘profession, trade or business’.”

The strange contrast in these two cases is that while letting out land for commercial purposes is not a “profession, trade or business”, the performance of religious services is.

The Madras High Court took the lead provided by the Allahabad High Court and came to the conclusion that submission of tenders for the purpose of obtaining a contract is not “a trade or calling”.<sup>229</sup>

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covenantee and if this onus is discharged the onus of showing that the restraint is nevertheless injurious to the public is on the party attacking the contract. The court has to decide, as a matter of law, (i) whether a contract is or is not in restraint of trade, and (ii) whether, if in restraint of trade, it is reasonable. Instead of segregating two questions, (i) whether the contract is in restraint of trade, (ii) whether, if so, is it ‘reasonable’, the courts have often fused the two by asking whether the contract is in ‘undue restraint of trade’ or by a compound finding that it is not satisfied that this contract is really in restraint of trade at all but, if it is, is it reasonable.” Another aspect of this case was, that one of the terms of the agreement with the company was that its shareholders would not transfer their shares during the currency of the agreement. This was held to be not hit by S. 27 because shareholders were not parties to the agreement and the company had no means to prevent them from selling their shares.

226. See, *Sandhya Organic Chemicals P Ltd v United Phosphorus Ltd*, AIR 1997 Guj 177, where the court observed that the principles of English common law can be used where the statutory provisions cannot be understood without the aid of English law, but not beyond that.

227. *Revashanker Shamji v Velji Jagiwan Kukama*, AIR 1951 Kutch 56.

228. AIR 1915 All 94 (2). *Zaheer Khan v Percept D'mark India (P) Ltd*, AIR 2004 Bom 362, a contract restricting the party's future freedom to carry on his affairs in a manner he likes and with persons of his choice, held, unreasonable restraint of trade.

229. *Mohd Isack v Daddapaneni*, AIR 1946 Mad 289.

A postal authority invited tenders for licence for carrying mails. The plaintiff, a bus owner, abstained from tendering on the promise of the defendant, another bus owner, to pay him some money. The latter obtained the contract but refused to pay the money.

The court said that tendering to obtain a contract is not in the nature of a trade or calling. The court compared the case with an agreement between intending bidders and said that such an agreement was considered as being not opposed to public policy in a few previous cases.<sup>230</sup> Special stress was laid upon a decision of the Privy Council where it was held that a court sale by public auction does not become void if a person had deterred others from bidding.<sup>231</sup> But, it is submitted with respect, that the decision is not an authority for the proposition that the collusion agreement between the bidders is itself valid and enforceable. In the United States such agreements have been held illegal.<sup>232</sup>

When the Madras High Court faced a problem of this kind again in a subsequent case,<sup>233</sup> it reluctantly held that "the precedents are far too numerous to be got over, even if one should be disposed to disagree with the underlying reasoning therein". The facts were that on an auction sale of fishery, the villagers colluded that only one of them shall bid for all of them and thereby the public authority was misguided as to the real value of the fishery. The agreement between the villagers was held to be valid.<sup>234</sup>

All these matters had subsequently to be taken in the light of the provision in Section 33(1)(jb) of the Monopolies and Restrictive Trade Practices Act, 1969 [now repealed] to the effect that an agreement as to making of bids, or excluding a person from bidding, at an auction for sale of goods, shall be a restrictive trade practice and, therefore, void unless it was necessary in public interest as spelled out in Section 38 of that Act. Now by the virtue of this clause, such collusive agreements can be held to be void unless they are necessary in public interest within the meaning of Section 38. The clause is wide enough to cover cases of secret agreements as to participation

230. *Hari Balkrishna Joglekar v Naro Moreshwar Joglekar*, ILR (1893) 18 Bom 342 and by the Privy Council in *Mohd Mira Rowther v Savvasi Vijya Roghunanda*, ILR (1900) 23 Mad 227.

231. *Ibid.* (Privy Council decision)

232. See *RESTATEMENT OF THE LAW OF CONTRACT*, Ch. 18, p. 1002, where the rule is thus stated: "A bargain not to bid at an auction, or any public competition for a sale or contract, having as its primary object to stifle competition, is illegal". Illustration 1 given in the Restatement is as follows: "A and B attending an auction of curios, make mutual promises by which each agrees to refrain from bidding for specified articles in order that the other may acquire them too cheaply. The agreement is illegal." Illustration 4 comes very close to the facts of the Madras case: "A advertises for bids for the construction of a building. B, a contractor, promises \$ 1000 each to C and D if they will refrain from bidding. They do so. The bargains are illegal."

233. *Pattipati Ramalingaiah v Nagulagunta Subbarami*, AIR 1951 Mad 390.

234. Following this, it has been held by the P&H High Court in *Sujan Singh Sadhana v Mohkam Chand Jain*, AIR 1983 P&H 180, that an agreement between two bidders not to bid against each other with an understanding that the successful bidder would convey half the property to the others is not against public policy.

in an auction according to pre-planned terms. Though collusive tendering has not been specifically included in the clause, it is likely to be covered by the wide ambit of the clause because it is often difficult to distinguish an auction from a tender when secret bids are invited in the shape of tenders. For example, in the *Perfect Circle Victor Ltd* case<sup>235</sup> the MRTP Commission issued cease and desist orders against three respondents manufacturing gaskets who were acting in concert by quoting the same or identical prices against tenders floated by the Director General of Supplies and Disposals.

Though the MRTP Act has been repealed, these decisions are likely to remain valid because of the parallel provisions in Sections 3 to 6 of the Competition Act, 2002 which is a replacement of its predecessor MRTP Act.

### **Knock-out agreements**

In United Kingdom, the “knock-out” agreements are covered by the Auctions (Bidding Agreements) Act, 1927. The Act provides that if any dealer agrees to give or gives or offers any gift or consideration to any other person as an inducement or reward for abstaining or having abstained from bidding at a sale by auction, either generally or for any particular lot or if any person agrees to accept or accepts or attempts to obtain from any dealer any such gift or consideration as aforesaid, he shall be guilty of offence under the Act. There is no special provision relating to collusive tendering or bidding in the Restrictive Trade Practices Act, 1976. But it seems clear that such bid agreements fall within Sections 6(1)(a) and 11(2)(a) of the Restrictive Trade Practices Act, 1976, as relating to the prices to be quoted for goods or services.<sup>236</sup> The agreement by which parties confer authority upon an association, or an individual, to adjust prices which they are to quote are also within these provisions.

In a case of this kind, P&H High Court stated thus:<sup>237</sup>

“An agreement between ‘A’ and ‘B’ to purchase certain property at an auction sale jointly and not to bid against each other at the auction is perfectly lawful, though the object may be to avoid competition between the two. However, if there is an agreement among all the competing bidders at the auction and they formed a ring to peg down price and to purchase the Government largess at knock-out price, the purpose or design of the agreement is to defraud the Government and then it can be said that there

235. RTP Enquiry, 120 of 1984, 24-4-1988. Similarly, in *Excel Industries Ltd*, (1988) 1 Comp LJ 53, three respondents who were major manufacturers of aluminium phosphide quoted identical rates in response to tenders floated by Food Corporation of India and reduced the rates by an identical amount during negotiations, the Commission passed cease and desist orders.
236. The report of the UK Monopolies Commission noted that any communication of prices between competitors and still more any adjustment of the amounts of tenders by arrangement between bidders would frustrate the purpose of the system of tendering. Since such tenders cease to be independent offers as they are held out to be, the practices are *prima facie* contrary to public interest.
237. *Anti-Corruption and Social Welfare Organisation v State of Punjab*, (1997) 1 BC 262 (P&H DB).

is an implied injury to the Government. The public policy is not static. It is variable with the changing times and the needs of the society. The march of law must match with the fact situation. A contract which does not cause any loss to the Government or the public authority, nor there is anything to infer that the bidders had formed a ring to peg down the price at an auction sale, the auction cannot be invalidated or cannot be said to be injurious to public interest or public welfare or fraudulent to defeat the rights of the Government or the local authority.”

In the US the practice of collusive tendering attracts the general provision of Section 1 of the Sherman Act which provides that every contract, combination or conspiracy in restraint of trade or commerce is illegal.

### Restrictions for long period

The principle of the *Nordenfelt* case was applied by the House of Lords in *McEllistrim v Ballymacelligott Coop Agricultural & Diary Society*<sup>238</sup> where an agreement contained in the rules of a society by which a former member agreed that for an unlimited time he would sell all the milk he produced to a creamery run by the society was held to be invalid. The doctrine of restraint of trade has been reconsidered by the House of Lords in *Esso Petroleum Co Ltd v Harper's Garage (Stourport) Ltd.*<sup>239</sup> In this case, their Lordships struck down an exclusive dealing agreement because it extended to a period of 21 years, which was unreasonable. A five-year period would have been held to be reasonable. In holding that the doctrine applied to exclusive dealing agreements they opened up the possibility that it might be extended to every sort of contract because all contracts must need involve a restraint of some sort. They said that the doctrine applied only if a man contracted to give up some existing freedom which he had.<sup>240</sup>

### Restriction upon use of trade mark

A restraint upon the use of a trade mark does not attract Section 27, it being not a restriction upon carrying on any trade or business. The trade mark was the subject-matter of the dispute.<sup>241</sup>

### Restrictions in lease

Restrictions contained in a lease agreement as to the uses to which the premises can be put and what business would be done and in what name and style have been held to be not violative of Section 27.<sup>242</sup>

238. 1919 AC 548 (HL).

239. 1968 AC 269: (1967) 2 WLR 871 (HL).

240. See J.D. HEYDON, *The Restraint of Trade Doctrine reviewed*, 89 LQR 292. Alec Lobb (*Garages*) Ltd v Total Oil Great Britain Ltd, (1983) 1 WLR 87 (Ch D), exclusive dealing agreement for an extended period of 21 years was held void as unreasonable restraint of trade however great the justification for the rest of the transaction which was found to be valid.

241. *Suresh Dhanuka v Sunita Mohapatra*, (2012) 1 SCC 578.

242. *Vidya Wati v Hans Raj*, AIR 1993 Del 187.

## EXCEPTIONS

There are two kinds of exceptions to the rule, those created by statutes and those arising from judicial interpretation of Section 27.

### Statutory exceptions

#### 1. *Sale of goodwill*

The only exception mentioned in the proviso to Section 27 of the Contract Act is that relating to sale of goodwill. It is thus stated:

One who sells the goodwill of a business may agree with the buyer to refrain from carrying on a similar business, within specified local limits, so long as the buyer, or any person deriving title to the goodwill from him, carries on a like business therein:

Provided that such limits appear to the court reasonable, regard being had to the nature of the business.

Apparently the object is to protect the interest of a purchaser of goodwill.

“It is difficult to imagine that when the goodwill and trade of a retail shop were sold, the vendor might the next day set up a shop within a few doors and draw off all customers.”<sup>243</sup> Therefore, some restriction on the liberty of the seller becomes necessary. Indeed, the restriction is the only “means by which a saleable value is given to the goodwill of a business”.<sup>244</sup> Far from being adverse to public interest, the restriction, by giving a real marketable value to the goodwill of a business, operates as an additional inducement to individuals to employ their skills and capital in trade and thus tend to the advantage of public interest.

**MEANING OF GOODWILL.**—There should be a real goodwill to be sold. “Goodwill” being an abstract property, is not easy to define. In the words of Lord ELDON:

The goodwill which has been the subject of sale is nothing more than the probability that the old customer will resort to old place.<sup>245</sup>

But in the opinion of Lord MACNAGHTEN, as expressed in a subsequent case, goodwill means much more than this: Often it happens that goodwill is the very sap and life of the business, without which the business would yield little or no profits. It is the whole advantage, whatever it may be, of the reputation and connection of firm, which may have been built up by years of honest work or gained by lavish expenditure of money.<sup>246</sup>

243. Lord MACNAGHTEN in *Ann Trego v George Stratford Hunt*, 1896 AC 7, 23 citing PLUMBER VC in *Harrison v W. Gardner*, 369 F 2d 172.

244. D.W. Auchterlonie v Charles Bell, (1868) 4 Mad HCR 77, 79.

245. *Cruttwell v Lye*, (1810) 17 Ves Jun 335: 34 ER 129, cited by Lord HERSCHELL in *Ann Trego v George Stratford Hunt*, 1896 AC 7, 16.

246. *Ann Trego v George Stratford Hunt*, 1896 AC 7, 23–24.

These opinions were adopted by the Judicial Committee in an appeal from a decision of the Calcutta High Court.<sup>247</sup>

The plaintiff and the defendant were carrying on business as carriers of passengers by boats. The plaintiff sold his business to the defendant for a sum of money and agreed to abstain from carrying on a boat business there for a period of three years.

The suit was brought to recover the promised sum. Allowing the plaintiff's action Lord HALDANE said: "Their Lordships entertain no doubt that what took place was the sale of goodwill within the meaning put on the expression in such cases as *Trego v Hunt*."

Where the aim of an agreement is prevention of competition, it will be void even if its nakedness is concealed behind the "imposing facade of a sale" of goodwill. An attempt of this kind was in evidence in *Vancouver Malt & Sake Brewing Co Ltd v Vancouver Breweries Ltd*.<sup>248</sup>

A company was licensed to manufacture liquor and beer but it confined its business to produce only 'sake', a Japanese liquor made from rice. Its only customer was the Government. It entered into an agreement with another wine and beer manufacturing company by which it sold its business and goodwill of manufacturing wine and beer, but not the right to produce sake.

The agreement was held to be devoid of any content. "The only business in which it was engaged was the brewing of sake, and the goodwill of its licence so far as relating to sake was expressly excluded from sale. It had no goodwill to sell so far as regards the brewing of beer. Nothing has been sold. It is simply a case of the appellant undertaking to the respondent in consideration of a sum of money that it will not for 15 years carry on a particular branch of business. If there was any sale, it was a sale by the appellant of its liberty to brew beer and a purchase by the respondent of protection against the possible competition of the appellant in the brewing of beer." Lord MACMILLAN then referred to the judgment of Lord Chancellor BIRKENHEAD in *McEllistrim v Ballymacelligott Coop Agricultural & Dairy Society*,<sup>249</sup> that "the respondents were not entitled to be protected against mere competition", and continued to say that "covenants restrictive of competition which have been sustained have all been ancillary to some main transaction, and have been found justified because they were reasonably necessary to render that transaction effective.

**LIMITS OF RESTRAINT.**—The agreement has to specify the local limits of the restraint. The seller can be restrained within certain territorial or geographical limits and the limits must be reasonable. Reasonableness of

247. *Parasullah Mullik v Chandra Kanta Das*, (1916–17) 21 CWN 979. On appeal *Chandra Kanta Das v Parasullah Mullick*, ILR (1921) 48 Cal 1030 (PC).

248. (1934) 39 LW 618: AIR 1934 PC 101.

249. 1919 AC 548, 563 (HL).

restrictions will depend upon many factors, for example, the area in which the goodwill is effectively enjoyed and the price paid for it.<sup>250</sup>

The seller can only be restrained from carrying on a similar business and also only for such period for which the business sold is actually carried on either by the buyer or by any person deriving title to the goodwill from him.

## 2. Partnership Act

There are four provisions in the Partnership Act which validate agreements in restraint of trade. Section 11 enables partners during the continuance of the firm to restrict their mutual liberty by agreeing that none of them shall carry on any business other than that of the firm.<sup>251</sup> Section 36 enables them to restrain an outgoing partner from carrying on a similar business within a specified period or within specified local limits. Such agreement shall be valid if the restrictions imposed are reasonable. A similar agreement may be made by partners upon or in anticipation of dissolution by which they may restrain each other from carrying on a business similar to that of the firm.<sup>252</sup>

It is necessary for the validity of a restraint under Section 36 or 54 that—

- (1) the agreement should specify the *local limits or the period of restraint*, and
- (2) the restriction imposed must be reasonable.<sup>253</sup>

An agreement by a retiring partner not to carry on similar business on the land belonging to him and adjoining the factory of the firm, has been held to be reasonable and binding on the persons buying the land from him.<sup>254</sup>

## Under judicial interpretation

### 1. Trade combinations

It is now almost a universal practice for traders or manufacturers in the same line of business to carry on their trade in an organised way.<sup>255</sup> Thus, there are combinations of ice manufacturers,<sup>256</sup> grain merchants, sugar producers,<sup>257</sup> etc. The primary object of such associations is to regulate business and not to restrain it. Combinations of this kind are often desirable in the interest of trade itself and also for the promotion of public interest.

250. See *Damodar Laxman Lele v Kashinath Waman Lele*, (1906) 9 Bom LR 312; *Deva Sharma v Laxmi Narain*, AIR 1956 Punj 49.

251. See *Firm Daulat Ram v Firm Dharm Chand*, AIR 1934 Lah 110, where two ice factory owners constituting a partnership agreed that only one factory will be worked at a time and its profits distributed among them. The restraint was held to be justified.

252. S. 54 of the Partnership Act.

253. See *Krishnarao v Shankar*, 1954 SCC OnLine Bom 61: ILR 1954 Bom 1409, where DESAI J, explained the rules as to reasonableness of restrictions at pp. 978–79.

254. *Hukmi Chand v Jaipur Ice and Oil Mills*, AIR 1980 Raj 155.

255. *Bom Ice Co v S.B. Fraser & Co*, (1904) 6 Bom LR 23.

256. *Bhola Nath Shankar Das v Lachmi Narain*, (1931) 29 All LJ 84.

257. *Carew & Co Ltd v North Bengal Sugar Mills*, ILR (1951) 2 Cal 386.

They bring about standardised goods, fixed prices and eliminate ruinous competition. Thus, "regulations as to the opening and closing of business in the market, licensing of traders, supervision and control of dealers and the mode of dealing are not illegal,"<sup>258</sup> even if there is incidental deprivation of trade liberty. But the courts would not allow a restraint to be imposed disguised as trade regulations. Thus, an agreement between certain persons to carry on business with the members of their caste only,<sup>259</sup> and an agreement to restrict the business of a sugar mill within a zone allotted to it, have been held void.<sup>260</sup> An agreement between two companies that one would not employ the former employees of the other has been held to be void by reason of its generality. This was the situation in *Kores Mfg Co Ltd v Kolok Mfg Co Ltd.*<sup>261</sup>

Both companies were engaged in manufacturing similar products involving technical processes in which the employees were likely to acquire knowledge of trade secrets and confidential information. The companies agreed that neither would employ, without the written consent of the other, any person who had been the employee of the other for any time during the previous five years.

Though the agreement was between two employers who were dealing at arm's length and on equal terms, it was held to be void. It prohibited the appointment of any person by any one company or the other who had been in the service of one or the other for any period, however short, and in any capacity, however humble. The ban was applicable as much to an unskilled manual labourer who might have been employed even for a single day as to a highly skilled and long-term employee, as much to a dismissed servant as to one who might have resigned; as much to a lay employee as to one who might have acquired confidential knowledge.

Agreements as to regulation of prices and output are generally upheld as valid. Thus in a Bombay case:<sup>262</sup>

Four ginning factories entered into an agreement fixing uniform rate for ginning cotton, and pooling their earnings to be divided between them in certain proportions.

The action was for division of profits and there being nothing in the agreement against Section 27, it was allowed.

Referring to the other part of the agreement, which fixed uniform rates, FARREN CJ said that an agreement of this description whereby traders agree amongst themselves to sell their wares at a fixed price, or labourers so agree to labour only at the stipulated wage have in the English courts usually been

258. *Municipal Committee, Khurai v Firm Kaluram Hiralal*, AIR 1944 Nag 73.

259. *Vaithealinga v Saminada*, ILR (1872) 2 Mad 44.

260. *Carew & Co Ltd v North Bengal Sugar Mills*, ILR (1951) 2 Cal 386.

261. 1959 Ch 108: (1958) 2 WLR 858 (CA).

262. *Haribhai v Sharafali*, ILR (1897) 22 Bom 861.

held void. But CANDY J disagreed with him. He believed that the apparent object was to prevent competition.<sup>263</sup>

The question again arose in *S.B. Fraser & Co v Bombay Ice Mfg Co.*<sup>264</sup>

An agreement between certain ice manufacturers fixed the minimum price for sale of ice, the proportion of the manufacture which each was to bear and of profits which each was to receive, some of them were restrained from selling at Poona and some others at steamers.

RUSSEL J held that the agreement was not within the terms of Section 27, the whole object being to regulate business and not to restrain it.<sup>265</sup>

The Allahabad High Court faced the problem in *Bhola Nath Shankar Das v Lachmi Narain.*<sup>266</sup>

The rules of an association of traders and weighmen provided that members shall not deal with outsiders, the penalty for breach being fine and expulsion. The legality of the association was attacked on the ground that its objects and methods were unlawful as it aimed at the creation of a monopoly by shutting out all competition and was a defiance of the spirit of Sections 23 and 27.

Rejecting this contention, SEN J quoted Baron ALDERSON in *Hilton v Eckersley*<sup>267</sup> as saying: “*prima facie* it is the privilege of a trader in a free country in all matters not contrary to law, to regulate his own mode of carrying it on according to his own discretion and choice.”<sup>268</sup>

## 2. *Solus or exclusive dealing agreements*

Another business practice in vogue is that a producer or manufacturer likes to market his goods through a sole agent or distributor and the latter agrees in turn not to deal with the goods of any other manufacturer. A producer may, for example, agree to sell all his output to one consumer who, in turn, agrees not to buy his requirements from any other source. As long as the negative stipulation is nothing but an ordinary incident of or ancillary to the positive covenant, there is hardly anything obnoxious to Section 27.

263. At p. 868. The learned Judge quoted that speech of Lord COLERIDGE in *Mogul SS Co Ltd v McGregor Gow & Co*, (1889) LR 23 QBD 598 (CA), “it seems it was no more in restraint of trade than if two tailors in a village agreed to give their customers five per cent in their bills on Christmas on condition of their customers dealing with them and them only”. Followed by the Allahabad High Court in *Kubernath v Mohate Ram*, ILR (1912) 26 ILR All 587. Now this has to be taken in the light of the provisions of the Monopolies and Restrictive Trade Practices Act, 1969, [now repealed] which provide in S. 33(1)(d) that price fixation for goods or service is deemed to be a restrictive trade practice unless it was saved by S. 38 of that Act which permits certain restrictions in public interest. MRTP Act has now been superseded by the Competition Act, 2002. Ss. 3 to 6 are now the relevant provisions.

264. ILR (1904) 29 Bom 107.

265. The learned Judge cited a number of decisions from the United States in which it has been held that competition is not always a public benefaction. See at pp. 30–31 of 6 Bom LR 1904.

266. (1931) 29 All LJ 84.

267. (1855) 6 E&B 47.

268. (1931) 29 All LJ 84 at p. 87.

Indeed “in one sense, every agreement for sale of goods whether *in esse* or *in posse* is a contract in restraint of trade for, if AB agrees to sell goods to CD, he precludes himself from selling them to anybody else”.<sup>269</sup> Thus, an agreement by a manufacturer of *dhotis* to supply 1,36,000 pairs of certain description to the defendant and not to sell goods of that kind to any other person for a fixed period;<sup>270</sup> an agreement by a person to sell all the salt manufactured by him to a firm for five years;<sup>271</sup> an agreement by a person to send all the mica produced by him to the plaintiffs, and not to send them to any other firm, nor to keep any in stock<sup>272</sup> and an agreement by a buyer of goods for Calcutta market, not to sell them in Madras, have all been held to be outside the scope of Section 27 and therefore valid. Such negative stipulations do not have the effect of restraining the manufacturer. “On the contrary, he is encouraged to exercise his business because he is assured of a certain market for the products of his labour.”<sup>273</sup>

But where a manufacturer or supplier, after meeting all the requirements of a buyer, has surplus to sell to others, he cannot be restrained from doing so.<sup>274</sup> The buyer cannot restrain the seller from dealing with others unless he can acquire the whole stock during the period of the agreement. The court may not countenance the agreement particularly where the buyer intends to corner or monopolise the commodity so that he may resell at his own price or where he binds the seller for an unreasonable period of time. Thus, in *Shaikh Kalu v Ram Saran Bhagat*.<sup>275</sup>

A seller of combs entered into an agreement with all the manufacturers of combs in the city of Patna whereby the latter undertook during their lifetime to sell all their products to R.S., and to his heirs and not to sell the same to any one else.

Holding the agreement void under Section 27, the court said: “It bound the manufacturers from generation to generation; it was unrestricted both as to time and place; it was oppressive; it was intended to create a monopoly.”<sup>276</sup>

The House of Lords has held that 21-year period of exclusive dealing would be unreasonably long. The case before their Lordships was *Esso Petroleum Co Ltd v Harper's Garage (Stourport) Ltd*.<sup>277</sup>

Esso Co had an agreement with two garages which was to bind one for about four and a half years and the other for 21 years. During this period

269. *HANDLEY J in Mackenzie v Striramiah*, ILR (1890) 8 Mad 472, 474. *Percept D'Mark (India) (P) Ltd v Zabeer Khan*, (2004) 2 Bom CR 47, negative covenant in a contract that the covenantee would not sell a similar product of a competitor was held not necessarily in restraint of trade, it could also be in furtherance of trade.

270. *Carliles Nephews & Co v Ricknauth Bucktermull*, ILR (1882) 8 Cal 809.

271. *Mackenzie v Striramiah*, ILR (1890) 8 Mad 472.

272. *Subba Naidu v Haji Badsha Sahib*, ILR (1902) 26 Mad 168.

273. *Abdul Karim v Sk. Dubar*, AIR 1937 Oudh 445.

274. *Har Bilas v Mahadeo Prasad*, AIR 1931 All 539.

275. (1908–09) 13 CWN 388: 1 IC 94.

276. *Ibid* at p. 396. See also *Abdul Karim v Sk. Dubar*, AIR 1937 Oudh 445.

277. 1968 AC 269: (1967) 2 WLR 871 (HL).

they had to buy the whole of their requirements from Esso and to operate the garages in accordance with Esso co-operation plan. The garage which was bound for 21 years was also mortgaged to Esso against a loan which was repayable in instalments lasting for 21 years and not earlier.

The House of Lords unanimously held that the agreement fell within the sphere to which the doctrine of restraint applies and the period of 21 years being not reasonable, it was void, but the tie with the other garage for four years and five months was reasonable. Lord PEARCE laid down: "The doctrine does not apply to ordinary commercial contracts for the regulation and promotion of trade during the existence of the contract provided that any prevention of work outside the contract viewed as a whole is directed towards absorption of the parties' services and not their sterilisation. Sole agencies are a normal and necessary incident of commerce, and those who desire the benefit of a sole agency must deprive themselves the opportunities of other agencies. So too, in the case of a film star who may tie himself to a company in order to obtain from them the benefits of stardom."<sup>278</sup>

Where a contract is reasonable and fair at the beginning, but circumstances have arisen which show that it is being enforced by one party in a manner which is prejudicial to the interest of the other, the courts will hold the agreement to be unenforceable, though not void or invalid. This opinion has been expressed by the Court of Appeal in *Shell U.K. Ltd v Lostock Garages Ltd*.<sup>279</sup>

A petrol pump was tied to Shell for a period which the court found to be reasonable. Subsequently, on account of a sharp rise in petrol prices sales suffered and in order to counteract this, some of the petroleum companies encouraged their pumps to cut prices. The Shell Company did not do so, but instead adopted a support plan to compensate their pumps for losses suffered by them in selling at competitive prices. This support plan did not apply to Lostock because his sales had not suffered to the extent contemplated by the support plan. Lostock attempted to get supplies from other companies and an injunction was sought against him. No injunction was, however, granted.

Lord DENNING MR first remarked that "it is now settled beyond doubt that a solus agreement is a contract in restraint of trade. As such it comes within that special class in which the courts can investigate the terms of the contract and see whether they are fair and reasonable. If they are unfair and unreasonable, the courts may refuse to enforce them". His Lordship found that there was nothing unreasonable in the contract, it being only for five years. "At that time the parties did not anticipate that circumstances would arise in which Shell would subsidise neighbouring garages to such an extent

278. *Gaumont British Picture Corpn Ltd v Alexander*, (1936) 2 All ER 1686. See *Restrictive Trade Practices*, 87 LQR 481; (1937) 35 Mod LR 651; Rudolf Graupner, *Sole Distributorship Agreements*, (1969) 18 ICLQ 879.

279. (1976) 1 WLR 1187 (CA).

as to force Lostock to trade at a loss. That contingency was so improbable and extravagant that it would not invalidate the tie at the time it was made.” His Lordship then laid down that the court should not enforce a covenant in restraint of trade if circumstances afterwards arise in which it would be unreasonable or unfair to enforce it.

An agency for sale of the goods of a German company in India which carried a term restraining the Indian company from selling goods for five years after the termination of the contract was held to be not enforceable.<sup>280</sup> An agreement of this kind was okayed by the Supreme Court where it was confined to the currency of the agreement. The case before the court was *Gujarat Bottling Co Ltd v Coca Cola Co*.<sup>281</sup>

An agreement for grant of franchise by Coca Cola Co to Gujarat Bottling Co to manufacture, bottle, sell and distribute beverages under trade marks held by the franchiser contained the negative stipulation restraining the franchisee to “manufacture, bottle, sell, deal or otherwise be concerned with the products, beverages of any other brands or trade marks/trade names during subsistence of this agreement including the period of one year’s notice”. It was held that the negative stipulation was intended to promote the trade. Moreover, operation of the stipulation was confined only to subsistence of the agreement and not after termination thereof. Hence stipulation could not be regarded as in restraint of trade.

The court proceeded as follows:

“A stipulation in a contract which is intended for advancement of trade shall not be regarded as being in restraint of trade. Similarly, except in cases where the contract is wholly one-sided, normally the doctrine of restraint of trade is not attracted in cases where the restriction is to operate during the period the contract is subsisting and it applies in respect of a restriction which operates after the termination of the contract.”

“There is a growing trend to regulate distribution of goods and services through franchise agreements providing for grant of franchise by the franchiser on certain terms and conditions to the franchisee. Such agreements often incorporate a condition that the franchisee shall not deal with competing goods. Such a condition restricting the right of the franchisee to deal with competing goods is for facilitating the distribution of the goods of the franchiser and it cannot be regarded as in restraint of trade.

The agreement in question in this case was an agreement for grant of franchise by Coca Cola to GBC to manufacture, bottle, sell and distribute the various beverages for which the trade marks were acquired by Coca Cola. It was thus, a commercial agreement whereunder both the parties have undertaken obligations for promoting the trade in beverages for

280. *Taprogge Gesellschaft MBH v IAEC India Ltd*, AIR 1988 Bom 157.

281. (1995) 5 SCC 545: AIR 1995 SC 2372: (1995) 84 Comp Cas 618.

their mutual benefit. The purpose of the negative stipulation contained in the agreement was that GBC will work vigorously and diligently to promote and solicit the sale of the products/beverages produced under the trade marks of Coca Cola. This would not be possible if GBC were to manufacture, bottle, sell, deal or otherwise be concerned with the products, beverages or any other brands or trade marks/trade names. Thus, the purpose of the said agreement is to promote the trade and the negative stipulation seeks to achieve the said purpose by requiring GBC to wholeheartedly apply to promote the sale of the products of Coca Cola. Moreover, since the negative stipulation is confined in its application to the period of subsistence of the agreement and the restriction imposed therein is operative only during the period the agreement is subsisting, the said stipulation cannot be held to be in restraint of trade so as to attract the bar of Section 27 of the Contract Act.”

### 3. Restraints upon employees

*RESTRAINTS DURING EMPLOYMENT.*—Agreements of service often contain negative covenants preventing the employee from working elsewhere during the period covered by the agreement. “Trade secrets, the names of customers, all such things which in sound philosophical language are denominated as objective knowledge—these may not be given away by a servant; they are his master’s property, and there is no rule of public interest which prevents a transfer of them against the master’s will being restrained.”<sup>282</sup> A servant may, therefore, be restrained from taking part in any business in direct competition with that of his employer.<sup>283</sup> Thus, in *Charlesworth v MacDonald*:<sup>284</sup>

A agreed to become assistant for three years to B who was a physician and surgeon practising at Zanzibar. The appointment was subject to the clause against practising. A left the service within a year and began to practise there on his own account.

282. *Herbert Morris Ltd v Saxelby*, (1916) 1 AC 688, 714 (HL), *per Lord SHAW*.

283. *Electrosteel Castings Ltd v Saw Pipes Ltd*, (2005) 1 CHN 612, where an employee agrees with his employer, e.g. to work with him faithfully for five years and not to work with any competitor during that period. The court said: The clause is a good one, because it is not in restraint of any profession, trade or business. The restriction against working with a competitor during the period of one’s parent employment is not a restriction against profession but it is a restriction against breach of faith and loyalty. A whole-time employee, if he is to be diligent and loyal, can obviously serve only one master. The clause only enforces this condition of employment and is not in reality restrictive. *VFS Global Services (P) Ltd v Suprit Roy*, 2007 SCC OnLine Bom 1083: (2008) 3 Mah LJ 266, a clause prohibiting an employee from disclosing commercial or trade secrets is not in restraint of trade because the employee is not thereby restrained from carrying on any lawful profession, trade or business.

284. ILR (1898) 23 Bom 103. See further *Sociedade De Fomento Industrial Ltd v Ravindranath Subraya Kamat*, (2000) 1 Mah LJ 148, a contract of retainership contained a clause that up to the currency of the engagement the employee would not undertake directly or indirectly by himself or by family members or by any person as his agent any activity competing with the business of the plaintiff companies; this was held to be not void.

But he was restrained from doing so during the period of three years. FARRAN CJ explained the principle thus: "An agreement of this class does not fall within Section 27. If it did, all contracts of personal service for a fixed period would be void. An agreement to serve exclusively for a week, a day, or even for an hour, necessarily prevents the person so agreeing to serve from exercising his calling during that period for anyone else than the person with whom he so agrees."<sup>285</sup>

The principle was applied by KANIA AG CJ (as he then was) of the Bombay High Court in *V.N. Deshpande v Arvind Mills Co Ltd.*<sup>286</sup>

The defendant took employment as a weaving master in a mill and agreed not to serve in that capacity for three years for anyone else in any part of India. An injunction was granted to restrain him in terms of the agreement.<sup>287</sup>

Agreements for protection of confidentiality and trade secrets are not one-sided or unfair or unreasonable. Any breach of such clauses on the part of the employee can also be treated as a misconduct. The petitioner was in this case, after resignation, working for a competitor. The possibility of using the client lists and confidential information just cannot be ruled out. Though, there is no direct evidence on record but in view of the admitted breach and facts and circumstances the petitioner is liable to pay lump sum damages/compensation. It is clear breach of the agreed clauses as confidential information/data must have traversed out of the private domain to the competitor's domain through the petitioner. The sufferer needs to be compensated in view of the admitted breach itself. The element of breach relating

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285. *India Charlesworth v Mac Donald*, ILR (1899) 23 Bom 103. See for further study: J. Finch, *Restraint Clauses in General Medical Practitioner's Partnership*, 132 New LJ 27.

286. AIR 1946 Bom 423. See also *Lalbhai Dalpatbhai & Co v Chittaranjan Chandulal Pandya*, AIR 1966 Guj 189.

287. The Ag. Chief Justice reviews at pp. 425–28 all the leading English cases on the subject. For other illustrations see *Pragji v Pranjivan*, (1903) 5 Bom LR 878; *Madras Rly Co v Rust*, ILR (1890) 4 Mad 18; *Subba Naidu v Haji Badsha Sahib*, ILR (1902) 26 Mad 168; *Burn & Co v McDonald*, ILR (1909) 36 Cal 354: 9 Cal LJ 190. In this case an engineer Macdonald was brought by the company from England to work for them for five years. In case of his leaving employment earlier he was to pay damages of £ 100. He left employment and refused to pay damages. The Court did not permit him to continue his work with the new employer. The Court opined that the employee, could not act in such an overbearing manner. The Court proceeded on the illustrations (c) and (d) of S. 57 of the earlier Specific Relief Act, 1877. It did not advert to S. 27 at all. *Niranjan Shankar Golikari v Century Spg & Mfg Co Ltd*, AIR 1967 SC 1098: (1967) 2 SCR 378, a restraint during five years' term of service, held reasonable. *Numeric Power Systems Ltd v Mohd. Muzaffar*, 2006 SCC OnLine Mad 697: (2006) 4 LLN 385, a negative covenant can be enforced during the continuance of the employment and it continues for this purpose till the employee is released. The stipulation in the contract that the negative covenant was to bind the employee for one year after termination of employment was not enforced. *Nazir Maricar v Marshalls Sons & Co (India) Ltd*, (2005) 2 CTC 478, section comes into play even when there is only a partial restriction. Justifiable restrictions are permissible. Training expenses were incurred, employee put on five year term, Rs 30,000 payable if he left earlier. He worked for 18 months. Rs 30,000 would have to be reduced proportionally.

to confidential information with other elements of loss of profit, etc., just cannot be overlooked. As there is legal injury, it should be compensated.<sup>288</sup>

**RESTRAINTS AFTER TERMINATION OF EMPLOYMENT.**—But an agreement to restrain a servant from competing with his employer after the termination of employment may not be allowed by the courts. Thus, in *Brahmaputra Tea Co Ltd v E. Scarth*,<sup>289</sup> where an attempt was made to restrain a servant from competing for five years after the period of service, the court observed: “Contracts by which persons are restrained from competing, after the term of their agreement is over, with their former employers within reasonable limits, are well known in English law, and the omission to make any such contract an exception to the general prohibition contained in Section 27 indicates that it was not intended to give them legal effect in this country.”

The principles thus established have been approved by the Supreme Court in *Niranjan Shankar Golikari v Century Spg & Mfg Co Ltd*.<sup>290</sup>



CASE PILOT

A company manufacturing tyre cord yarn was offered collaboration by a foreign producer on the condition that the company shall maintain secrecy of all the technical information and that it should obtain corresponding secrecy arrangements from its employees. The defendant was appointed for a period of five years, the condition being that during this period he shall not serve anywhere else even if he left the service earlier.

SHELAT J held the agreement to be valid. The defendant was accordingly restrained from serving anywhere else during the currency of the agreement. “The evidence is clear that the appellant has torn the agreement to pieces only because he has been offered a high remuneration. Obviously he cannot be heard to say that no injunction should be granted against him to enforce the negative covenant which is not opposed to public policy. The injunction issued against him is restricted as to time, the nature of employment and as to area and cannot therefore be said to be too wide or unreasonable or unnecessary for the protection of the interest of the respondent company.”

The learned judge distinguished the case from the decision of A.N. RAY J (as he then was) of the Calcutta High Court in *Gopal Paper Mills Ltd v Surendra K. Ganeshdas Malhotra*<sup>291</sup> where an injunction to enforce a negative covenant during the period of employment was refused as the agreement

288. *Anindya Mukherjee v Clean Coats (P) Ltd*, (2011) 1 Mah LJ 573.

289. ILR (1885) 11 Cal 545.

290. AIR 1967 SC 1098: (1967) 2 SCR 378. Further followed in *R. Babu v TTK Lig Ltd*, (2004) 2 CTC 684: (2004) 2 CCC 565, so as to hold that such injunctions are allowable. The court said in this case that no injunction could be granted against an employee after termination of his employment restraining him from carrying on competitive trade. The order restraining him from joining the new employer could not be sustained, his termination being the result of a breach of agreement. *Ambiance India (P) Ltd v Naveen Jain*, (2005) 81 DRJ 538: (2005) 122 DLJ 421 (Short Notes, Case 70), the employment being determinable, the employee left, the prohibition on taking employment elsewhere not enforced, an irreparable loss would be caused to the young employee whereas the employer could be compensated for breach, if any, in terms of money.

291. AIR 1962 Cal 61.

was for a period of twenty years and its terms were also unconscionable. SHELAT J said:

The period of contract there was as much as 20 years and the contract gave the employer an arbitrary power to terminate the service without notice ... such a contract would clearly be held void as being one-sided.

A service contract carried a clause to the effect that the employee was not to disclose confidential information to any person after cessation of employment with the employer (applicant) and was not to take up any employment or involve himself with any other person a body corporate in similar field of activity which was of competitive nature. This was held to be contrary to the provisions of Section 27. An order of injunction could not be granted to enforce it at the interim stage itself.<sup>292</sup>

In England the position of such restrictive covenants has been described to be "still an uncertain field". Lord WILBERFORCE observed in the *Esso Petroleum* case:

Certain contracts of employment, with restrictions appropriate to their character against undertaking other work during their currency may be acceptable. Here too, however, if it is found that the restriction is purely limitative or sterilising, it may be subject to examination.

#### *Recovery of training expenses*

The agreement was that the employee would put in service for a period of five years after returning from training abroad at the cost of the employer. An indemnity clause quantified damages at Rs 30,000 if the service was left earlier. The employee left after 18 months. The trial court awarded to the employer the whole amount of Rs 30,000. The High Court reduced the amount to Rs 20,000 keeping in mind the proportionate recovery already effected during the actual period of service. Such agreements, the court said, are for the benefit of employees because training provided to them increases their acceptability in the job market. There is no restraint also because the employee is free to go away after paying unrecovered portion of expenses of training.<sup>293</sup>

**PROTECTION OF TRADE SECRETS.**—One of the principles is that a master is not entitled to restrain his servant after the termination of employment from offering competition, but he is entitled to reasonable protection against exploitation of trade secrets.<sup>294</sup> In *Mason v Provident Clothing and Supply Co Ltd*<sup>295</sup> the House of Lords did not allow an employer to restrain his

292. *Sanmar Speciality Chemicals Ltd v Biswajit Roy*, AIR 2007 Mad 237.

293. *Nazir Maricar v Marshalls Sons & Co (India) Ltd*, (2005) 2 CTC 478.

294. YOUNGER LJ in *Attwood v Lamont*, (1920) 3 KB 571.

295. 1913 AC 724 (HL). See also *Marshall v N.M. Financial Management Ltd*, (1995) 1 WLR 1461. In this case, a sales agent was working on the condition that for one-year period after the termination of employment he would not become an independent intermediary or become employed in any direct or indirect competitor. This was held to be an invalid restraint of

canvasser for a period of three years after the termination of his service. Viscount HALDANE LC pointed out that capacity for canvassing is a natural gift and not due to special training provided by the employer. "Had they been content with asking him to bind himself not to canvass within the area where he had actually assisted in building up the goodwill of their business, or in an area restricted to places where the knowledge which he had acquired in his employment could obviously have been used to their prejudice, they might have secured a right to restrain him within these limits."

On the other hand, in *Fitch v Dewes*<sup>296</sup> the House of Lords allowed a covenant by which a solicitor's clerk was restrained from practising within 7 miles of the city, it being reasonably necessary for protecting the interest of both parties. But in no case the court would allow covenants against competition. In *Attwood v Lamont*<sup>297</sup> the employer was running several departments in connection with tailoring etc. and the employee was the superintendent only of the tailoring department. The agreement with him was that after ceasing to be an employee he would not engage himself within 10 miles in any of the business being run by the employer in addition to tailoring. The Court of Appeal held the agreement not only to be unnaturally wide but also in restraint of competition. YOUNGER LJ cited the following passage from the speech of Lord PARKER in *Morris v Saxelby*:<sup>298</sup> "The reason and the only reason for upholding such a restraint on the part of an employee is that the employer has some proprietary right, whether in the nature of the trade connection or in the nature of trade secrets, for the protection of which such a restraint, is, having regard to the duties of an employee, reasonably necessary. Such a restraint has never been upheld, if directed only to the prevention of competition or against the use of the personal skill and knowledge acquired by the employee in his employer's business."

In a subsequent case:<sup>299</sup>

The defendants were employed by the plaintiffs as agents for debt collection for the city of Birmingham. A clause of the agreement provided: "For a period of six months after the determination of employment the

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trade. It was far wider than was really necessary for protecting the employer's clientage. The restriction was preventive of competition over a much wider range than was necessary. The employer was permitted to forfeit his arrears of commission. *Sandhya Organic Chemicals P Ltd v United Phosphorus Ltd*, AIR 1997 Guj 177, an employee was under covenant not to divulge any confidential and secret information, the court said that it would not go beyond the term of employment; injunction refused. *Certact Ptc Ltd v Tang Stew Choy*, (1991) 3 CLJ 2269 High Court, Singapore, list of suppliers and customers is property of employer, employee can be restrained from using such trade secrets and confidential information.

296. (1921) 2 AC 158 (HL). A restraint upon a ladies hairdresser that she should not work after the termination of her employment at a competitive place for 12 months and within half a mile of the place, was held to be reasonable. *White (Marion) Ltd v Francis*, (1972) 1 WLR 1423.

297. (1920) 3 KB 571.

298. (1916) 1 AC 688, 710.

299. *Financial Collection Agencies Ltd v Batey*, The Times, May 1973: 1973 New LJ 469.

defendants would not solicit business from any person, firm or companies who shall at any time have been a client." The defendants left and started a debt collection agency of their own. The plaintiff prayed for an injunction.

It was held that the injunction would not be granted, for the covenant was far too wide and was an unreasonable restraint of trade, since it extended to the whole area of the plaintiffs' operation whereas the defendants were employed in Birmingham alone.

A restraint upon a ladies' hair dresser that she should not work after the termination of her employment at a competitive place for 12 months and within half a mile of the place, was held to be reasonable.<sup>300</sup>

In a Canadian case:<sup>301</sup>

The defendants were employees of a company which carried on a topographical survey business. During their service they attempted to obtain a valuable contract for the plaintiff company, but failed to do so. Thereafter, the defendants resigned and obtained the contract for themselves, but without using any confidential information of the plaintiff.

The court held that there is an implied term in a contract of employment that a former employee may not make use of his former employer's trade secrets, but with this exception, he is entitled to compete and that even if the contract of employment had contained a covenant not to compete in respect of possible future contracts, such covenant would have been an unreasonable restraint of trade and void.<sup>302</sup>

300. *Marion White Ltd v Francis*, (1972) 1 WLR 1423; *Hi-Tech Systems and Services Ltd v Suprabhat Ray*, 2015 SCC On Line Cal 1192: AIR 2015 Cal 261, employees resigned in quick succession one after the other, formed a partnership, shared information with third parties with the clear object of causing diversion of the business of former employer, an injunction was granted against them to restrain breach of contract terms.

301. *Canadian Aero Service Ltd v O'Malley*, (1971) 23 DLR (3rd) 632, Ontario Court of Appeal.

302. For a discussion of the subject and case see Poonuswami, *Public Interest and Restrictive Trade Practices in India*, (1963) Indian Yearbook Int'l. Affairs 256-280. *Merit Scada Automation (P) Ltd v Sanmar Industrial Systems Ltd*, (2004) 5 CTC 81 (Mad), senior engineer signed secrecy agreement with plaintiff company, he promoted a new company while still in his employment and the new company was to compete with his employer company. Held, he and his company could be prevented from competitive bidding in the same line of work. *Commercial Plastics Ltd v Vincent*, (1965) 1 QB 623 (CA) "the use of mere general technical knowledge, acquired in the course of employment, must be carefully distinguished from confidential information and it is not a valid interest which the employer can claim to protect by a restraining covenant." *Ambiance India (P) Ltd v Naveen Jain*, (2005) 81 DRJ 538: (2005) 122 DLJ 421: routine day-to-day affairs of employer which are in the knowledge of many and are commonly known to others cannot be called trade secrets. A trade secret can be a formulae, technical know-how or a peculiar mode or.... In a business house, the employees discharging their duties come across so many matters, but all these matters are not trade secrets or confidential matters or formulae, the divulgence of which may be injurious to the employer. If the defendant on account of his employment with the plaintiff has learnt some business acumen or ways of dealing with the customers or clients, the same do not constitute trade secrets or confidential informations, the divulgence or use of which should be prohibited. *American Express Bank Ltd v Priya Puri*, 2006 SCC OnLine Del 638: (2006) 110 FLR 1061 cited in *Numeric Power Systems Ltd v Mohd. Muzaffar*, 2006 SCC OnLine

A restriction, even when otherwise justified, for a period of five years was held to be unreasonable in the case of an employee who earned only a modest wage.<sup>303</sup> A rule in the terms of employment providing that in case a servant took employment with a competitor his pension benefits would be forfeited has been held to be void.<sup>304</sup> Within three months of leaving employment, the defendant joined the competitor. The court said that the right of employees to seek employment and right of livelihood must prevail. The agreement was to restrain employment with an employer dealing in competitive business for a period of two years. Such restraint was not allowed. There could be injunction only to restrain the defendant from approaching the plaintiff's suppliers and customers for soliciting their business.<sup>305</sup>

Negative covenants tied up with positive covenants during the subsistence of the contract, be it of employment, partnership, commerce, agency or like, are not normally regarded as being in restraint of trade, business or profession unless the same are unconscionable or wholly one-sided. No employee can be put in a situation where he has either to stay with the present employer or face idleness.<sup>306</sup>

The principle envisaged under the section is applicable to all types of contracts or transactions and not merely to contracts of employment.<sup>307</sup> The court further said that in construing such covenants or restrictions neither the test of reasonableness nor the fact of partial restriction is applicable. The case should fall within the exception engrafted in Section 27.

**AGREEMENT BETWEEN EMPLOYERS.**—An agreement between two employers that neither would employ any person who had been the other's employee within a period of five years has been held to be void as it imposed too wide and unreasonable restriction upon freedom of employment.<sup>308</sup> An agreement between two employers that on cessation of their relationship, neither

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Mad 697: (2006) 4 LLN 385, one Bank cannot restrain another bank from dealing with its customers. The court said: Information will only be protected if it can properly be classified as a trade secret or as material which, while not properly to be described as a trade secret, is in all the circumstances of such a highly confidential nature as to require the same protection as a trade secret. *Electrosteel Castings Ltd v Saw Pipes Ltd*, (2005) 1 CHN 612 that the restriction against working with a competitor during the period of one's parent employment is not a restriction against profession, it is a restriction against breach of faith and loyalty.

303. *M & S Drapers (firm) v Reynolds*, (1957) 1 WLR 9.

304. *Bull v Pitney-Bowes Ltd*, (1967) 1 WLR 273. *Provident Financial Group plc v Hayward*, (1989) 3 All ER 298 (CA), an injunction was not to be granted where the defendant did not have any relevant confidential information of the plaintiffs which would be of use to the rival company and there was no real prospect of serious or significant damage to the plaintiffs from the defendant working as financial controller for the rival company for the short period which remained of his contract.

305. *Desiccant Rotors International (P) Ltd v Bappaditya Sarkar*, (2009) 112 DRJ 14 (Del).

306. *Wipro Ltd v Beckman Coulter International SA*, (2006) 131 DLT 681; *VFS Global Services (P) Ltd v Suprit Roy*, 2007 SCC OnLine Bom 1083: (2008) 3 Mah LJ 266, a garden leave clause which prohibits the employee from taking up any employment during the period of three months on the cessation of the employment has been held to be in restraint of trade.

307. *Percept D'Mark (India) (P) Ltd v Zaheer Khan*, (2006) 4 SCC 227.

308. *Kores Mfg Co Ltd v Kolok Mfg Co Ltd*, 1959 Ch 108: (1958) 2 WLR 858 (CA).

would induce or solicit the employees of the other to leave jobs and join pre-offered jobs in other competing firms was held to be not falling within the scope of Section 27 as it did not envisage any restriction on employers. The employees were free to move out of their jobs and join rivals and no injunction could be issued against the other party restraining it from taking in such turn-away employees. If the employees can leave here and go there without solicitation, how can there be an injunction when they do so on solicitation.<sup>309</sup>

*EFFECT OF PREMATURE REMOVAL.*—A restriction of this kind will cease to be effective against an employee who has been prematurely removed without his fault.<sup>310</sup> The Supreme Court also pointed out that a restraint beyond the term of service would be *prima facie* void and that the only ground on which it could be justified is by bringing it within the scope of the exception, that is, by showing that it is necessary for the protection of the employer's goodwill. The court further said that even if such a restraint is valid, it will only apply after the expiry of the term in its natural course, and not when the employee is wrongfully dismissed earlier. It could also apply if the employee left his service earlier. But leaving a service is different from premature termination. The restraint clause became inapplicable.<sup>311</sup>

No restriction was allowed to be imposed upon an employee when his term of employment was not for a specified period and he had left the job.<sup>312</sup> An employee of Star TV wanted to resign, but his resignation was not being accepted. On the contrary, a case was filed against him for a declaration that he had no right to resign or to join a rival firm. The court refused to issue an injunction for enforcing a negative covenant. The court said that the question whether the employee had gained knowledge of some trade secrets, whether he was imparted special training and was in possession of confidential information were matters which could be determined at the trial and till all this was sorted out, a negative covenant in matters of personal service could not be enforced. Freedom of contract includes freedom of occupation. There was nothing to suggest that the employer was likely to suffer irreparable loss without the injunction. Merely because the employer could face

309. *Wipro Ltd v Beckman Coulter International SA*, (2006) 131 DLT 681; *V.V. Sivaram v FOSECO India Ltd*, 2005 SCC Online Kar 595: (2006) 1 AIR Kant R 120, the employee had access to confidential information pertaining to several products including the patent "Turbostop". He left under voluntary retirement scheme. Injunction restraining him from manufacturing and marketing a product similar to "Turbostop" was held to be not violating S. 27.

310. *Superintendence Co of India v Krishan Murgai*, (1981) 2 SCC 246: AIR 1980 SC 1717. *Sanmar Speciality Chemicals Ltd v Biswajit Roy*, AIR 2007 Mad 237, clause against disclosure of confidential information after cessation of employment and taking any competitive job, injunction against employee not issued at the initial stage of the case for enforcing the clause. *VFS Global Services (P) Ltd v Suprit Roy*, 2007 SCC OnLine Bom 1083: (2008) 3 Mah LJ 266, another similar agreement.

311. A parallel English authority is *General Billposting Co Ltd v Atkinson*, 1909 AC 118 (HL).

312. *Weiler International Electronics (P) Ltd v Punita Velu Somasundaram*, (2003) 3 Bom CR 59.

some inconvenience or competition was not a ground for enforcing a negative covenant. It is not in public interest to restrain healthy competition.<sup>313</sup>

### Restraint of legal proceedings [S. 28]

It is a well-known rule of English law that “an agreement purporting to oust the jurisdiction of the courts is illegal and void on grounds of public policy”.<sup>314</sup> Thus, any clause in an agreement providing that neither party shall have the right to enforce the agreement by legal proceedings is void.<sup>315</sup> An arrangement may, however, stipulate that there is no intention to contract, or that it is only a gentleman’s agreement. In such a case, no action is possible under the agreement.<sup>316</sup>

Section 28 of the Indian Contract Act renders void two kinds of agreement, namely:

- (1) An agreement by which a party is restricted absolutely from enforcing his legal rights arising under a contract, by the usual legal proceedings in the ordinary tribunals.
- (2) An agreement which limits the time within which the contract rights may be enforced.

**S. 28. Agreements in restraint of legal proceedings void.—**<sup>317</sup> [Every agreement,—

- (a) by which any party thereto is restricted absolutely from enforcing his rights under or in respect of any contract, by the usual legal proceedings in the ordinary tribunals, or which limits the time within which he may thus enforce his rights; or
  - (b) which extinguishes the rights of any party thereto, or discharges any party thereto from any liability, under or in respect of any contract on the expiry of a specified period so as to restrict any party from enforcing his rights,
- is void to that extent.]

**Exception 1.—Saving of contract to refer to arbitration dispute that may arise.**—This section shall not render illegal a contract, by which two or more persons agree that any dispute which may arise between them in respect of any subject or class of subjects shall be referred to arbitration, and that only the amount awarded in such arbitration shall be recoverable in respect of the dispute so referred.

**Suits barred by such contracts.**—<sup>318</sup> When such a contract has been made, a suit may be brought for its specific performance; and if a suit, other than for such

313. *Star India (P) Ltd v Laxmiraj Setharam Nayak*, (2003) 3 Bom CR 563: (2003) 3 Mah LJ 726.

314. *Halsbury's Laws of England*, Vol 9, 352.

315. See *Baker v Jones*, (1954) 1 WLR 1005.

316. *Rose & Frank Co v J.R. Crompton & Bros Ltd*, (1923) 2 KB 261 (CA).

317. Subs. by Act 1 of 1997, S. 2.

318. The second clause of Exception 1 to S. 28 was *repealed* by the Specific Relief Act, 1877 (1 of 1877), S. 2 and Sch. I. The clause is, however, printed here in italics, because the Contract Act is in force in certain Scheduled Districts to which the Specific Relief Act does not apply.

*specific performance, or for the recovery of the amount so awarded, is brought by one party to such contract against any other such party, in respect of any subject which they have so agreed to refer, the existence of such contract shall be a bar to the suit.*

**Exception 2.—Saving of contract to refer questions that have already arisen.**—Nor shall this section render illegal any contract in writing, by which two or more persons agree to refer to arbitration any question between them which has already arisen, or affect any provision of any law in force for the time being as to references to arbitration.

<sup>319</sup>**[Exception 3.—Saving of a guarantee agreement of a bank or a financial institution.]**—This section shall not render illegal a contract in writing by which any bank or financial institution stipulate a term in a guarantee or any agreement making a provision for guarantee for extinguishment of the rights or discharge of any party thereto from any liability under or in respect of such guarantee or agreement on the expiry of a specified period which is not less than one year from the date of occurring or non-occurring of a specified event for extinguishment or discharge of such party from the said liability.

*Explanation.*—(i) In Exception 3, the expression “bank” means—

- (a) a “banking company” as defined in clause (c) of Section 5 of the Banking Regulation Act, 1949 (10 of 1949);
- (b) “a corresponding new bank” as defined in clause (da) of Section 5 of the Banking Regulation Act, 1949 (10 of 1949);
- (c) “State Bank of India” constituted under Section 3 of the State Bank of India Act, 1955 (23 of 1955);
- (d) “a subsidiary bank” as defined in clause (k) of Section 2 of the State Bank of India (Subsidiary Banks) Act, 1959 (38 of 1959)
- (e) “a Regional Rural Bank” established under Section 3 of the Regional Rural Bank Act, 1976 (21 of 1976);
- (f) “a Co-operative Bank” as defined in clause (cci) of Section 5 of the Banking Regulation Act, 1949 (10 of 1949);
- (g) “a multi-State co-operative bank” as defined in clause (cciiia) of Section 5 of the Banking Regulation Act, 1949 (10 of 1949); and

(ii) In Exception 3, the expression “a financial institution” means any public financial institution within the meaning of Section 4-A of the Companies Act, 1956 (1 of 1956).]

### Restriction on legal proceedings

Explaining the section, GARTH CJ of the Calcutta High Court observed in *Koegler v Coringa Oil Co Ltd*:<sup>320</sup> “This section applies to agreements which wholly or partially prohibit the parties from having recourse to a court of law. If, for instance, a contract were to contain a stipulation that no

319 . Ins. by Act 4 of 2013, S. 17 and Sch. (w.e.f. 18-1-2013).

320. ILR (1876) 1 Cal 466, 468–69.

action should be brought upon it, that stipulation would ... be void, because it would restrict both parties from enforcing their rights under the contract in the ordinary legal tribunals."

The right to appeal does not come within the purview of the section. A party to a suit may agree not to appeal against the decision.<sup>321</sup>

#### *Compromise outside court*

The claim in question was under the Recovery of Debts due to Banks and Financial Institutions Act, 1993. The parties entered into a compromise outside the court regarding withdrawal of proceedings. The court said that it was not hit by Sections 28, 57 and 59 of the Contract Act because no restraint was being placed upon institution of proceedings.<sup>322</sup>

#### *Limitation of time*

Another kind of agreement rendered void by the section is where an attempt is made by the parties to restrict the time within which an action may be brought so as to make it shorter than that prescribed by the law of limitation. According to the Limitation Act, 1963, for example, an action for breach of contract may be brought within three years from the date of breach. If a clause in an agreement provides that no action should be brought after two years, the clause is void. Thus, a clause in a policy of life insurance declaring that "no suit to recover under this policy of life insurance shall be brought after one year from the death of the assured" was held void.<sup>323</sup> Similarly, clauses in the standard fire insurance policy of the insurer curtailing limitation to 12 months of the occurrence of the event or 3 months of the rejection of the claim by the insurer were not permitted to be invoked to bar the claim filed within three years.<sup>324</sup> However, in a similar case before the Bombay High Court, a clause providing that "no suit shall be brought against the company in connection with the said policy later than one year after the time when the cause of action accrues was held valid, the court saying that the effect of the agreement was not to limit the time but to provide for the surrender of rights if no action was brought within that

321. See *Munshi Amir Ali v Inderjit Koer*, (1871) 9 Ben LR 460, a decision of the Privy Council before the Contract Act was passed. It has been followed by the Allahabad High Court in *Ashburner & Co v Anant Das*, ILR (1876) 1 All 267.

322. *Sashi Agarwal v Debtr Recovery Appellate Tribunal*, AIR 2010 All 24: (2009) 76 ALR 372.

323. *Ma Ywest v Chin Mutual Life Insurance Co Ltd*, 91 IC 622, but cf. *Hirabhai Narotamdas v Manufacturers Life Insurance Co*, 16 IC 1001: (1912) 14 Bom LR 791.

324. As contemplated by Art. 44(b) of the Limitation Act, 1963. See *Harsud Coop Mktg Society Ltd v United India Fire and General Insurance Co Ltd*, AIR 1992 Bom 341. *New India Assurance Co v Food Corporation of India*, 1996 SCC OnLine Mad 38: (1996) 1 CTC 375, notice issued within six months as required, filing of suit within three years thereafter, held, within time.

time.<sup>325</sup> The case has been adversely criticised.<sup>326</sup> But that view seems to have been affirmed by the Supreme Court in *Vulcan Insurance Co Ltd v Maharaj Singh*,<sup>327</sup> where the court observed that "it has been repeatedly held that such a clause is not hit by Section 28 and is valid". This was further affirmed in *National Insurance Co Ltd v Sujir Ganesh Nayak & Co*.<sup>328</sup> The clause in question provided that "in no case whatsoever shall the company be liable for any loss or damage after the expiration of 12 months from the happening of loss or damage unless the claim is the subject of pending action or arbitration". The claimant notified the insurer regarding the strike which caused the loss, but did not commence proceedings within the stipulated time. The court reversed the decision of the Kerala High Court and held that the clause was valid and its operation had ended the plaintiff's claim.<sup>329</sup>

A suit was filed for recovery of the amount due under an insurance policy. A clause in the policy provided that suits must be filed within 12 months from the date of disclaimer. The clause was held to be not valid. A suit filed within three years from that date was held to be maintainable.<sup>330</sup>

### Effect of amendment

The amendment of the section in 1997 has brought about this change that all clauses which reduced the normal period of limitation would be void to that extent. Thus, the artificial distinction between a clause cutting short the period of limitation and a clause providing for extinction of rights after a specified period has been eliminated.<sup>331</sup>

325. *Hirabhai Narotamdas v Manufacturers Life Insurance Co*, 16 IC 1001: (1912) 14 Bom LR 791.
326. See *Baroda Spg & Wvg Co Ltd v Satyanarayan Marine & Fire Insurance Co Ltd*, AIR 1914 Bom 25 (2): ILR (1914) 38 Bom 344. See also *New Asiatic Insurance Co v Bihar State Coop Bank*, AIR 1966 Pat 69, a clause requiring notice of loss within ten days was upheld.
327. (1976) 1 SCC 943; AIR 1976 SC 287; *Baroda Spg & Wvg Co Ltd v Satyanarayan Marine & Fire Insurance Co Ltd*, AIR 1914 Bom 25 (2): ILR (1914) 38 Bom 344.
328. (1997) 4 SCC 366: AIR 1997 SC 2049: (1997) 89 Comp Cas 131. See also *Food Corporation of India v New India Assurance Co Ltd*, (1994) 3 SCC 324, where the nature of the restriction in S. 28 was considered in the context of the restrictive clauses. The SC decision was relied upon in *Reliance Industries Ltd v P&O Containers Ltd*, 2006 AIHC 793: AIR 2006 Bom 65, suit against carrier in a transaction for import of goods, limitation clause of Hague Rules was made applicable providing one year period of limitation. Port of shipment was outside India, hence the Indian Carriage of Goods by Sea Act, 1925 was not applicable. The clause valid.
329. The Kerala decision is reported in *Sujir Ganesh Nayak & Co v National Insurance Co Ltd*, AIR 1996 Ker 49.
330. *State of A.P. v United India Insurance Co Ltd*, (1998) 2 An LT 74. *Muni Lal v Oriental Fire & General Insurance Co Ltd*, (1996) 1 SCC 90: AIR 1996 SC 642, prohibiting prescription of shorter limitation than prescribed by the Limitation Act, 1963.
331. *Continental Construction Ltd v Food Corporation of India*, AIR 2003 Del 32, a contract made before the amendment under which the work was also executed before the amendment, was to be governed by the unamended section and was not to be declared void under the new provision. *Rajesh Kumar Midda v State of Punjab*, (2004) 2 Cal LT 362, the condition of limitation in the arbitration agreement reduced the period of limitation from three years to six months. The arbitrator's refusal to entertain the claim after expiry of six months held to be wrongful. The condition was contrary to law and, therefore, not effective.

### *Forfeiture and surrender of rights*

Cases of this sort have been distinguished from those which provide for surrender or forfeiture of rights if no action is brought within the stipulated time. A clause in a policy of life insurance provided:

If a claim be made and rejected and an action or suit be not commenced within three months after such rejection ... all benefits under the policy shall be forfeited.<sup>332</sup>

The clause was held valid. Similarly, a clause that the company shall not be liable if no suit were brought within 12 months after the occurrence of the loss,<sup>333</sup> and a clause in a bill of lading providing that "in any event the carrier and the ship shall be discharged from all liability in respect of loss or damage unless a suit is brought within one year after the delivery of the goods,"<sup>334</sup> have been upheld. The reason why clauses of this kind have been allowed is that the extent of loss or damage can be measured with a certain amount of accuracy when the matters are fresh. "Lapse of time in such cases may result in all kinds of claims which are not capable of determination with any amount of exactitude and when memories of men may become rather hazy."<sup>335</sup>

The Jammu and Kashmir High Court extended the same principle to Government contracts. In a case before it:<sup>336</sup>

A clause in a Government contract provided that the President of India shall be discharged from all liability under the contract unless an arbitration or a suit is commenced within six months from the expiration of the period.

The clause was held to be valid. Explaining the distinction between extinction of rights and limitation of time, the court said:<sup>337</sup> "The distinction may be a fine one but it is nonetheless a fundamental distinction. The

332. *Girdharilal Hanumanbux v Eagle Star & British Dominions Insurance Co Ltd*, (1923) 27 CWN 955; *DDA v Bhardwaj Bros*, 2014 SCC OnLine Del 1581: AIR 2014 Del 147, an agreement providing for forfeiture or waiver of right if no action is commenced within the period stipulated in the agreement has been held to be not void.

333. *A. N. Ghose v Reliance Insurance Co*, ILR 11 Rang 475; *Ruby General Insurance Co Ltd v Bharat Bank Ltd*, AIR 1950 EP 352; *Pearl Insurance Co v Atma Ram*, AIR 1960 Punj 236.

334. *Haji Shakoor Gany v H. E. Hinde & Co Ltd*, AIR 1932 Bom 330.

335. *KAPUR J in Ruby General Insurance Co Ltd v Bharat Bank Ltd*, AIR 1950 EP 352.

336. *Prithvi Nath Malla v Union of India*, AIR 1962 J&K 15.

337. Followed, *Kasim Ali v New India Insurance Co*, AIR 1968 J&K 3. See also *Governor General in Council v Firm Badri Das Gauri Dutt*, AIR 1951 All 702. A clause in bank guarantee that action should be filed within six months of expiry of the guarantee, held, it was not available after the expiry of six months. *Kerala Electric and Allied Engg Co Ltd v Canara Bank*, AIR 1980 Ker 151, following *State of Maharashtra v M.N. Kaul*, AIR 1967 SC 1634. The arbitration clause in an agreement provided that all disputes in connection with the contract shall be submitted to arbitration not later than 28 days after the architect's final certificate. Held, that the right to refer ceased after 28 days. But in *Rajasthan Handicrafts Emporium v Pan American World Airways*, AIR 1984 Del 396, a clause in an airway bill that "no action shall be commenced" after certain time was held to be void. It was not a mere forfeiture clause.

arrangement in the one case takes it for granted that the right as well as the liability exists, but the time for enforcing it is sought to be limited. While in the other case, the parties agree that the right as well as liability shall stand extinguished if a specified event occurs."

"What Section 28 forbids, is not extinguishment of the rights or liabilities of a party to a contract on the happening of a specified event, but the limiting of the time within which a party may enforce his rights. It is obvious that a party will have no right to enforce, if the rights have already been extinguished under the contract. In such a case, there can be no question of the time for the enforcement of the rights being limited. What happens is that the right itself ceases to exist."

Where the need for reduction of time to sue has already been taken care of by a statute, there cannot be further reduction. Under Section 10 of the Carriers Act, 1865 notice of loss or damage must be given within six months, otherwise the right to sue is lost. A contract provided that such notice must be given within 30 days of the arrival of the goods. This being contrary to statutory provisions was held to be void.<sup>338</sup>

#### *"Absolutely": partial restriction as to jurisdiction*

Section 28 will come into play when the restriction imposed upon the right to sue is "absolute" in the sense that the parties are wholly precluded from pursuing their legal remedies in the ordinary tribunals.<sup>339</sup> A partial restriction will be valid.<sup>340</sup> An illustration of partial restriction is the decision of the Calcutta High Court in *Continental Drug & Co Ltd v Chemoids & Industries Ltd*.<sup>341</sup>

The contract in question fell under the concurrent jurisdiction of both the Bombay and Alipore courts, but the contract provided that "any dispute arising between the parties, settlement of the same legally or otherwise, will be decided in Bombay.

Holding the clause to be valid and binding, LAHIRI J said: "If there are two courts which are equally competent to try the suit, an agreement

338. *M.G. Bros Lorry Service v Prasad Textiles*, (1983) 1 SCC 61: AIR 1984 SC 15.

339. *Emmsons International Ltd v Metal Distributors (UK)*, 2005 AIHC 1190 (Del): (2005) 116 DLT 559, a unilateral covenant depriving the party of the right to sue under the contract either through ordinary tribunals or through alternative dispute resolution mechanism, void. *Tapash Majumdar v Pranab Dasgupta*, AIR 2006 Cal 55, the rule of a club authorised the executive committee to take action against any member who approached the court to challenge the election process, held void.

340. *Raigarh Jute and Textile Mills Ltd v New Haryana Transport Co*, 1994 MPLJ 626, parties by mutual agreement choosing one out of several courts having jurisdiction to try the suit, is not against public policy. *Dilip Kumar Ray v Tata Finance Ltd*, AIR 2002 Ori 29, hire purchase agreement specifying place of suit which was valid. Suit at any other place was held to be not maintainable.

341. AIR 1955 Cal 161. Where the selection of the forum is valid, that forum cannot be excluded from entertaining the suit only because the amount involved is paltry six hundred rupees. *East India Hat Co v Prakash Roadlines (P) Ltd*, (1986) 10 DRJ 133: (1986) 2 PLR 39 (Del).

between the parties that the suit should be instituted in one of those two courts cannot be said to be an absolute restriction on the right of taking legal proceedings. It has been established by a long line of judicial decisions that such an agreement does not contravene the provisions of Section 28 if the chosen court has jurisdiction to try the suit under ordinary law.”<sup>342</sup>

This has been affirmed by the Supreme Court in *Hakam Singh v Gammon (India) Ltd.*<sup>343</sup> The court laid down:<sup>344</sup> “It is not open to the parties by

342. The learned Judge cited: *Acharatnal Kesaval Mehta & Co v Vijaram & Co*, AIR 1925 Mad 1145; *Kondepu Elukkoru Raghavayya v Vasudevayya*, AIR 1944 Mad 47; *Tilakram Chaudhari v Kodumal Jethanand*, AIR 1925 Bom 175; *A. Milton & Co v Ojha Automobile Engg Co*, AIR 1931 Cal 279. See further cases cited at p. 418 of Ponnuswami and Puri, CASES AND MATERIALS ON CONTRACT. A contract providing for jurisdiction of Dhanbad courts only has been held to be binding. The excluded court cannot consider the balance of convenience. *Ganpatrai Agarwalla v Fertiliser Corp*n, AIR 1984 Cal 35. *Unique Pharmaceutical Laboratories v Stalco Freight International Co*, (2005) 6 Bom CR 829, goods booked from Bombay to a port in UAE contract provided for jurisdiction of UAE courts. Choice of the parties prevailed because the courts there had concurrent jurisdiction with Bombay courts Dallah.

343. (1971) 1 SCC 286: AIR 1971 SC 740: (1971) 3 SCR 313.

344. *Ibid.* A consignment note signed neither by the consignor nor consignee and containing a clause on the back excluding the jurisdiction of all the courts except one was held to be not binding. There was no proper notification. *Road Transport Corp*n v *Kirloskar Bros Ltd*, AIR 1981 Bom 299. A lottery ticket containing at the reverse in small print conditions about jurisdiction, held not binding as there was no proper notice. *Govt of Rajasthan v Venkataramana Seshiyer*, AIR 1984 AP 5. However, parties can opt for any available jurisdiction and exclude others. *Globe Transport Corp*n v *Triveni Engg Works*, (1983) 4 SCC 707; *All Bengal Transport Agency v Hare Krishna Banik*, AIR 1985 Gau 7, a contract of carriage allowing the sender only one jurisdiction out of several available under CPC, held valid. *Kumud Agarwalla v Fertilizer Corp*n of India Ltd, AIR 1985 Cal 89, contract provided for jurisdiction of Gorakhpur courts. Held, action could lie only at Gorakhpur. The court may however relieve a party from clauses where the court finds that jurisdiction permitted by the agreement is so inconvenient that it would be oppressive, inequitable and unfair for the party. *Pattnaik Industries (P) Ltd v Kalinga Iron Works*, AIR 1984 Ori 182. Parties’ choice of forum under an arbitration agreement does not violate S. 28. *Indian Rare Earths Ltd v Unique Builders Ltd*, AIR 1987 Ori 30 where a clause that the courts of Maharashtra only would have jurisdiction has been held to be valid and not vague or uncertain. See also *Biswanath Chowdhury v U.P. Forest Corp*n, AIR 1986 Cal 334, a clause that suits would be filed at Lucknow was held to be binding and an action allowed at Calcutta on balance of convenience was revoked. *Economic Transport Organisation v United India Insurance Co Ltd*, 1986 KLT 220: (1986) 2 TAC 25, mere delivery of a printed document does not constitute a contract so as to exclude jurisdiction. *Shriram City Union Finance Corp*n Ltd v *Rama Mishra*, (2002) 9 SCC 613: AIR 2002 SC 2402, it is open to parties to choose any one of the two competent courts to decide their dispute. It is not open to any of the parties to choose a different jurisdiction afterwards. *Hanil Era Textiles (P) Ltd v Puromatic Filters (P) Ltd*, (2004) 4 SCC 671: AIR 2004 SC 2432, a part of the cause of action arose at Bombay and a part at Delhi, clause in the agreement provided for proceedings to be taken at Bombay, held not opposed to public policy. Order was placed at Bombay and also accepted there and part payment also made there. Also to the same effect, *New Moga Transport Co v United India Insurance Co Ltd*, (2004) 4 SCC 677; *Kotak Mahindra Finance Ltd v T. Thomas Education Trust*, (2003) 5 Bom CR 579, no part of the cause of action had arisen at Bombay, a provision in the contract that it was subject to Bombay jurisdiction was held to be not valid, the fact that the plaintiff resided or carried on business there, did not have the effect of conferring jurisdiction on the Bombay courts. *Nailesh H. Doshi v O.P. Pharma*, (2003) 1 ICC 152 (AP), jurisdiction cannot be conferred on a court by agreement which does not otherwise have it. *Swastic Gases (P) Ltd v Indian Oil Corp*n Ltd, (2013) 9 SCC 32: (2013) 4 SCC Civ 157,

agreement to confer jurisdiction on a court, which it does not possess under the Civil Procedure Code.<sup>345</sup> But where two courts or more have under the Code of Civil Procedure jurisdiction to try a suit, an agreement between the parties that the dispute between them shall be tried in one of such courts is not contrary to public policy. Such an agreement does not contravene Section 28 of the Contract Act.”<sup>346</sup>

Generally, three jurisdictions are available: the place of the making of a contract, that of its performance and the defendant's place of business or residence. If, out of these three jurisdictions, at least one is left open, competent under the Civil Procedure Code it will not offend Section 28, provided that the jurisdiction which is left open is a convenient one, i.e. available at reasonable expense and not inaccessible.<sup>347</sup> A clause of an

various types of exclusion clauses and their consideration surveyed by the Supreme Court in the judgment in this case. *R.K. Maheshwari v. Nagarjun Construction Co Ltd*, AIR 2007 NOC 1119 (MP), suit for recovery of dues, work order was delivered at a place at which the payment was also settled to be made. The defendant was not able to prove that the contract was made at some other place. The court said that parties cannot confer jurisdiction by agreement on a court in which there is no jurisdiction. It was wrong for the trial judge to hold that the court at the place of delivery of order and payment had no jurisdiction.

345. Relied upon in *Patel Roadways Ltd v Prasad Trading Co*, (1991) 4 SCC 270; AIR 1992 SC 1514 so as to hold that if the carrier has a subordinate office at the place where the goods were delivered for transport and the cause of action also arose there because the goods were destroyed by fire at that place, an action would lie only there and not at the company's head office as provided in the contract because the courts there would have had no jurisdiction. *Ranjana Nagpal v Devi Ram*, AIR 2002 HP 166, the agreement cannot vest jurisdiction in a court which otherwise does not have it. The agreement related to immovable property. The suit could be filed before the court where the property was situate and nowhere else, whatever may be the agreement between the parties.
346. The principle enunciated in this case can also be seen at work in the following cases: *L.T. Societa v Lakshminarayanan*, AIR 1959 Cal 669, a bill of lading provided that all requests for compensation to be submitted at the place of discharge and indicated two other places for claims, held valid; *M.B.T. Co Madras v A.N. Rao*, (1968) 1 An WR 424, forwarding note providing for one jurisdiction; *Patel Bros v Vadilal Kashidas Ltd*, AIR 1959 Mad 227, the printed terms as to Bombay jurisdiction were held to be not binding because proper notice of the terms was not given to the other party; *C. Satyanarayana v Kanumarpudi Lakshmi Narsimham*, AIR 1968 AP 330, where also the printing did not become a part of the contract; *Kanpur Sugar Supply Co v Harsukh Lal*, AIR 1971 All 502, mere printing on bills of exchange and letters that the transactions would be “subject to Rajkot Courts only” did not have the effect of an agreement on the point; *Grandhi Pitchaiah Venkatraju & Co v Palukuri Jagannadham & Co*, AIR 1975 AP 32; *Surajmall Shiwbhagawan v Kalinga Iron Works*, AIR 1979 Ori 126, a statement on purchase order as to jurisdiction, not binding; *Jagannath v Nanakkal*, 1972 MP LJ 981, printed heading on sale of goods documents as to jurisdiction, no agreement; *Prakash Road Lines (P) Ltd v HMT Bearing Ltd*, AIR 1999 AP 106, contract of carriage, agreement providing for jurisdiction at a place where no jurisdiction otherwise existed, held not binding.
347. *E.I.D. Parry (India) Ltd v Savani Transport (P) Ltd*, AIR 1980 AP 30; *Globe Transport Corp v Triveni Engg Works*, (1983) 4 SCC 707; *A.B.C. Laminart (P) Ltd v A.P. Agencies*, (1989) 2 SCC 163; AIR 1989 SC 1239; *All Bengal Transport Agency v Hare Krishna Banik*, AIR 1985 Gau 7, action allowed at New Gong, the place of business, town Matta, which was highly inconvenient being very remote, was the only jurisdiction allowed by the contract; *Prakash Roadlines (P) Ltd v P. Mulhuswamy Gounder & Co*, AIR 1985 Mad 84, action allowed at Madras though the contract provided for Bangalore as exclusive jurisdiction. *Burn Standard Co Ltd v ONGC Ltd*, AIR 2000 Cal 283, a clause in a bank guarantee provided for exclusive jurisdiction of the courts at the place where the contract and the guarantee

agreement between the parties provided that the venue of arbitration was to be Hyderabad and courts there would have exclusive jurisdiction to adjudicate the dispute between the parties. The court said that parties cannot lawfully confer jurisdiction on a court which it does not possess under the Civil Procedure Code. The clause was void. No cause of action or even a part of the cause of action had arisen at Gujarat and therefore only the competent court there had jurisdiction.<sup>348</sup> A bilateral agreement under which an option is provided for choosing the jurisdiction of a particular country was held to be not opposed to public policy.<sup>349</sup>

It is necessary that serious terms of this nature must be specifically brought to the notice of the parties whose rights are sought to be curtailed.<sup>350</sup> Something more must be done than merely printing the terms on consignment documents.<sup>351</sup> The law requires that before making a person bound by any such term (a clause in a consignment note as to exclusive jurisdiction) it must be proved that the same was brought to the knowledge of the consignor in such a way that it should seem to be the result of a mutual assent.<sup>352</sup> Where a consignment way bill contained the words "subject to Calcutta jurisdiction", the court ignored it since it was not one to which the plaintiff assented.<sup>353</sup> Where the original contracting party, i.e. the consignor

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were executed. An application for stay of enforcement could not be filed at any other place. *Rajaram Maize Products v M.P. Electricity Board*, AIR 1999 MP 44, the contract provided for settlement of disputes only at place "J" which was one of the possible jurisdictions. A suit filed at another place was held to be not proper though the cause of action had arisen at that place. *A.V.M. Sales Corp v Anuradha Chemicals (P) Ltd*, (2012) 2 SCC 315: (2012) 1 SCC (Civ) 809, the agreement provided for jurisdiction at Calcutta Courts excluding Vijayawada Courts, but even so a Vijayawada Court entertained the suit, the Supreme Court directed it to be transferred to Calcutta Court.

348. *DIC-NCC (JV)—A Joint Venture of Daelim Industrial Co v M. Sahai & Associates (P) Ltd*, AIR 2010 NOC 843 (Guj).
349. *Nirmala Balagopal v Venkatesulu Balagopal*, AIR 2004 Mad 255.

350. *Road Transport Corp v Kirloskar Bros Ltd*, AIR 1981 Bom 299.
351. *Oriental Fire & General Insurance Co Ltd v New Suraj Transport Co (P) Ltd*, AIR 1985 All 136. Thus where the consignment note was not even signed by the booking party or his agent, the consignor was not bound by a printed term about the exclusive jurisdiction. *South Eastern Roadways v United India Insurance Co Ltd*, AIR 1991 Ker 41. Provisions relating to exclusion of the jurisdiction of courts are very strictly construed. The exclusion is not to be readily inferred and, therefore, must either be explicitly expressed or clearly implied. *Bismillah v Janeshwar Pandit*, (1990) 1 SCC 207, 210: AIR 1990 SC 540. In the matters of international trade and the choice of forum see *British India Steam Navigation Co Ltd v Shanmughavilas Cashew Industries*, (1990) 3 SCC 481. *Rhodia Ltd v Neon Laboratories Ltd*, AIR 2002 Bom 502 at p. 513, the parties agreed that their disputes would be resolved through English courts. They were bound by their agreement. The agreement was executed in a country to which the parties did not belong. Their choice of the law of a third country was held to be binding on them. The court considered its own earlier decision in *NTPC v Singer Co*, (1992) 3 SCC 551: AIR 1993 SC 998, the agreement provided that the English law was to apply to the interpretation of their agreement. *Hari Shanker Jain v Sonia Gandhi*, (2001) 8 SCC 233: AIR 2001 SC 3689, the foreign law would have to be pleaded and proved like any other fact.

352. *Road Transport Organisation of India v Barunai Powerloom Weavers' Coop Society Ltd*, (1994) 84 Cut LT 174.
353. *Grandhi Pitchaiah Venkatraju & Co v Palukuri Jagannadham & Co*, AIR 1975 AP 32. To

has been adequately informed, it will be a question of fact in each case whether the parties subsequently acquiring his rights will also be bound by the notified terms. The carrier would have no opportunity of knowing about him and much less of giving him any notice. A Bench of the Andhra Pradesh High Court, therefore, came to the conclusion that the consignee to whom the booking documents are indorsed to enable him to obtain delivery at the destination would also be bound by the terms.<sup>354</sup> If the original party is not bound by those terms, neither would be those who acquire their rights under the document.<sup>355</sup> Following these principles in another case, the Andhra Pradesh High Court came to the conclusion that a term as to the place of suit was not binding on the insurer who had paid out the consignee and who was then suing the carrier for the negligent loss of the goods unless it could be proved that the insurer too was made or was otherwise aware of the terms.<sup>356</sup>

An agreement made subject to the jurisdiction of a stated court would not have the effect of ousting the jurisdiction of other courts.<sup>357</sup> An ouster clause in a contract can oust the territorial jurisdiction only of a civil court but not that of a High Court.<sup>358</sup> The fact that the contract clause does not use the word "alone", "only" or "exclusively" does not *ipso facto* warrant that there was no intention to provide for exclusive jurisdiction of the court specified in the clause. The court must consider all the facts and circumstances while construing the clause.<sup>359</sup>

Where the terms and conditions attached to the quotation contained an arbitration clause provided that: "any order placed against this quotation shall be deemed to be a contract made in Calcutta and any dispute arising therefrom shall be settled by an arbitrator to be jointly appointed by us", it was held that it merely fixed the situs of the contract at Calcutta and it did not mean to confer an exclusive jurisdiction on the Court at Calcutta, and when a part of the cause of action had arisen at Salem, the Court there had also jurisdiction to entertain the suit under Section 20(c) of the Code of Civil Procedure.<sup>360</sup>

The Supreme Court in *Angile Insulations v Davy Ashmore India Ltd*,<sup>361</sup> held as under:

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the same effect is *Road Transport Corpn v Kirloskar Bros Ltd*, AIR 1981 Bom 299. The court said that it is for the carrier to plead and prove that the print on the receipt was brought to the notice of the consignor and that he had agreed to and accepted the same.

354. *V. Raja Rao v A.P.T. Co*, (1969) 2 APLJ 151.

355. *Govt of Rajasthan v Venkataramana Seshiyer*, AIR 1984 AP 5, a term as to jurisdiction in a lottery ticket, held not binding on a buyer of the ticket.

356. *East India Transport Agency v National Insurance Co Ltd*, AIR 1991 AP 53.

357. *Cheema Enterprises v Mayu Enterprises*, AIR 1998 Gau 86.

358. *P.R. Transport Agency v Union of India*, (2005) All LJ 3568: AIR 2006 All 23 (DB).

359. *Pacific Refractories Ltd v Stein Heurtey India Projects (P) Ltd*, (2006) 3 Mah LJ 438: (2006) 4 Bom CR 311.

360. *Salem Chemical Industries v Bird & Co (P) Ltd*, AIR 1979 Mad 16.

361. (1995) 4 SCC 153: AIR 1995 SC 1766; *Maharashtra State Road Development Corpn v Larsen & Toubro Ltd*, (2004) 5 Bom CR 186, jurisdiction otherwise available under the

“So, normally that Court also would have jurisdiction where the cause of action, wholly or in part, arises. But it will be subject to the terms of the contract between the parties. In this case, Clause (21) read thus:

‘This work order is issued subject to the jurisdiction of the High Court situated in Bangalore in the State of Karnataka. Any legal proceeding will, therefore, fall within the jurisdiction of the above Court only.’

A reading of this clause would clearly indicate that the work order issued by the Appellant will be subject to the jurisdiction of the High Court situated in Bangalore in the State of Karnataka. Any legal proceeding will, therefore, be instituted in a Court of competent jurisdiction within the jurisdiction of High Court of Bangalore only.”

An ouster clause becomes effective when a contract is formed. It remains ineffective when the contract formation process ends prematurely. The tender which was submitted by the contractor along with earnest deposit permitted jurisdiction of courts at two places and at no other place. But this particular tender was not accepted. No contract came into being. The contractor was free to file his case at all places available under the Civil Procedure Code.<sup>362</sup>

Where the contract provided for jurisdiction in respect of purchase orders at the court in Pune, and the plaintiff filed a case there which was of composite nature, because it included disputes not arising out of purchase orders, it was held that the Pune court acquired jurisdiction to try the whole case because of the joinder of causes of action.<sup>363</sup>

#### *Right to approach courts on matters of compensation*

A provision in a supply agreement was that the purchaser would have unilateral right to determine the amount of liquidated damages which would be recoverable and that such quantification would be final and not challengeable by the supplier. The court said that the provision was clearly in restraint of legal proceedings. It was an attempt to oust the jurisdiction of the courts and the right of the party to seek judicial adjudication.<sup>364</sup>

#### **Provision for foreign jurisdiction**

A contract stated to be an international commercial contract contained a clause which provided for dispute redressal mechanism through arbitration and that the contract to be construed and governed by English law. The court said that the effect of the provision was that only English courts would have exclusive jurisdiction. The Indian party was thus deprived of its rights

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Civil Procedure Code was allowed where the jurisdiction clause in the contract was found to be ambiguous.

362. *Orissa Agro Industries Corp v KCS (P) Ltd*, 2004 AIHC 1788 (Ori).

363. *Bajaj Auto Ltd v Sandeep Polymers (P) Ltd*, (2004) 4 Mah LJ 396.

364. *BSNL v Motorola India (P) Ltd*, (2009) 2 SCC 337: (2009) 1 SCC (Civ) 524: AIR 2009 SC 357.

to proceed before courts in India. The court could not permit it because it violated Section 28 of the Contract Act.<sup>365</sup> The court cited one of its own earlier decisions.<sup>366</sup> The provision in the contract was for reference to arbitration by the company before an arbitrator to be appointed by the company but the award was to be binding on both parties. The court said that the effect of the clause was that it was a unilateral agreement and consequently not enforceable through a court of law.

In the case of a contract, the available jurisdiction was either at Chennai or Hyderabad. The contract had nothing to do with Delhi and yet Delhi was the only permitted jurisdiction. A proceeding instituted in Lok Adalat at Hyderabad was held to be valid because Lok Adalat, being not a court, the restriction was not applicable to it.<sup>367</sup>

## Exceptions

### 1. Reference of future disputes to arbitration

The section does not render void a contract by which two or more persons agree that any dispute which may arise between them shall be referred to arbitration and that only the amount awarded in the arbitration shall be recoverable. An agreement between the parties to refer disputes to arbitration is perfectly valid.<sup>368</sup> Thus in *Koegler v Coringa Oil Co Ltd*:<sup>369</sup>

A clause in an agreement that all disputes would be referred to arbitration of two competent London brokers and their decision would be final, was held valid.

GARTH CJ said:<sup>370</sup> “If a contract were to contain a double stipulation that any dispute between the parties should be settled by arbitration, and that neither party should enforce his rights under it in a court of law, that would be a valid stipulation so far as regards its first branch, viz., that all disputes between the parties should be referred to arbitration, because that of itself would not have the effect of ousting the jurisdiction of the courts, but the latter branch of the stipulation would be void because by that the jurisdiction of the courts would be naturally excluded.”

The right to proceed against the arbitrator’s award, for example, to have it set aside, cannot be excluded by contract.

365. *Emmsons International Ltd v Metal Distributors (UK)*, 2005 AIHC 1190 (Del): (2005) 116 DLT 559.

366. *A.V.N. Tubes Ltd v Bhartia Cutler Hammer Ltd*, (1992) 46 DLT 453: (1992) 2 Arb LJ 8 (DB).

367. *Inter Globe Aviation Ltd v N. Satchidanand*, (2011) 7 SCC 463: (2011) 3 KLT 295: (2011) 3 CPJ 1 (SC).

368. *Gajindalal v Rameshwar Das*, 171 IC 584; *Gopinath Daulat Dalvi v State of Maharashtra*, (2005) 1 Mah LJ 438, a settlement of labour dispute contained an arbitration clause over any dispute or as to interpretation of the settlement, neither void nor contrary to S. 28.

369. ILR (1876) 1 Cal 466.

370. *Ibid*, pp. 466–68.

A provision in a contract that the decision of the conservator of forests shall be final<sup>371</sup> and a clause in a contract of insurance that arbitration would be a condition precedent for any action against the company, have been held to be valid.<sup>372</sup> An arbitration clause remains binding even where the contract has ended by breach or otherwise. It is, therefore, theoretically possible that a contract may come to an end, and that arbitration agreement may not. It is also possible that the arbitration clause may not be valid but the rest of the contract may be valid.<sup>373</sup> It has been held by the Supreme Court that expressions any dispute “arising out of” or “concerning” or “in connection with”, or “in consequence of” or “relating to” this contract, are sufficiently wide to compel parties to refer even this matter to arbitration whether the contract is itself valid.<sup>374</sup>

A clause providing for arbitration and declaring that the Arbitration Act would not apply was held to be void. The arbitration clause was held to be valid. The part which excluded the application of the Arbitration Act being severable from the rest of the agreement was alone struck down.<sup>375</sup> A contract clause provided that the right to claim arbitration would come to an end after the expiry of 90 days from the date of intimation of the final bill being ready for payment. The matter was raised within the designated time. The award did not contain a decision on merits. It was held that the right of the contractor to seek arbitration remained alive. The award was set aside. The arbitrator was asked to decide the claim of the petitioner on merits.<sup>376</sup>

Where the head office of the institution was situate at Delhi and the contract provided for resolution of disputes by arbitration, an interim relief obtained by filing a suit at Chennai was held to be an abuse of the judicial process and, therefore, against public policy. A suit could be instituted only at the place of the registered office.<sup>377</sup>

## *2. Reference of existing questions to arbitration*

This exception saves contracts to refer to arbitration questions that have already arisen.<sup>378</sup> Where the parties agreed to refer their disputes to

371. *Mukteshwar Singh v State of Bihar*, AIR 1979 Pat 40; *Satish Kumar v Surinder Kumar*, AIR 1970 SC 833: (1969) 2 SCR 244. *World Sport Group (Mauritius) Ltd v MSM Satelite (Singapore) Pte Ltd*, (2014) 11 SCC 639: AIR 2014 SC 968, an arbitration agreement restricting right of parties to approach court, not opposed to public policy, nor it is in restraint of legal proceedings.

372. *National Insurance Co Ltd v Calcutta Dock Labour Board*, AIR 1977 Cal 492.

373. *Jawahar Lal Barman v Union of India*, AIR 1962 SC 378: (1962) 3 SCR 769.

374. *Khardah Co Ltd v Raymon & Co (India) (P) Ltd*, AIR 1962 SC 1810: (1963) 3 SCR 183.

375. *Rajasthan Housing Board v Engineering Projects (India) Ltd*, AIR 2000 Raj 200; *Universal Petrochemicals Ltd v Rajasthan SEB*, AIR 2001 Cal 102, an agreement cannot override the application of statutory provisions.

376. *J.K. Anand v DDA*, (2001) 92 DLT 598.

377. *National Council of YMCAs of India v C. Raja Singh Warrior*, 1999 AIHC 885 (Mad).

378. See *Union of India v Kishorilal Gupta & Bros*, AIR 1959 SC 1362: (1960) 1 SCR 493, where a contract is valid, the arbitration clause is binding.

arbitration, they were held to be bound to do so. The fact that the arbitrators were situated in a foreign country could not by itself be enough to nullify the arbitration when the parties accepted the arrangement with their eyes wide open and willingly. More so when the parties appointed arbitrators and participated in proceedings.<sup>379</sup>

### Uncertain agreements [S. 29]

**S. 29. Agreements void for uncertainty.**—Agreements, the meaning of which is not certain, or capable of being made certain, are void.

#### *Illustrations*

- (a) A agrees to sell to B "a hundred tons of oil". There is nothing whatever to show what kind of oil was intended. The agreement is void for uncertainty.
- (b) A agrees to sell to B one hundred tons of oil of a specified description, known as an article of commerce. There is no uncertainty here to make the agreement void.
- (c) A, who is a dealer in coconut oil only, agrees to sell to B "one hundred tons of oil". The nature of A's trade affords an indication of the meaning of the words, and A has entered into a contract for the sale of one hundred tons of coconut oil.
- (d) A agrees to sell to B "all the grain in my granary at Ramnagar". There is no uncertainty here to make the agreement void.
- (e) A agrees to sell to B "one thousand maunds of rice at a price to be fixed by C". As the price is capable of being made certain, there is no uncertainty here to make the agreement void.
- (f) A agrees to sell to B "my white horse for rupees five hundred or rupees one thousand". There is nothing to show which of the two prices was to be given. The agreement is void.<sup>380</sup>

The reason why certainty is necessary appears from the following statement of the House of Lords:<sup>381</sup>

It is a necessary requirement that an agreement in order to be binding must be sufficiently definite to enable the court to give it a practical meaning. Its terms must be so definite, or capable of being made definite without further agreement of the parties, and that promises and performances to be rendered by each party are reasonably certain.

An interesting illustration is *Guthing v Lynn*.<sup>382</sup> A horse was bought for a certain price coupled with a promise to give £5 more if the horse proved lucky. The agreement was held to be void for uncertainty. The court has no machinery to determine what luck, bad or good, the horse had brought to the buyer. Such cases have generally arisen in connection with sale of goods, there being uncertainty as to the price. For example, where goods are sold,

379. *Atlas Export Industries v Kotak & Co*, (1999) 7 SCC 61.

380. See *Dhanrajmal Gobindram v Shamji Kalidas & Co*, AIR 1961 SC 1285: (1961) 3 SCR 1320, 1035. *Panchanan Dhara v Monmatha Nath Maity*, (2006) 5 SCC 340: AIR 2006 SC 2281, the defence of uncertainty not allowed to be raised for the first time before the Supreme Court. Even otherwise the court found no uncertainty on the facts of the case.

381. *Scammell v Ousto*, 1941 AC 251, 268–69 per Lord WRIGHT.

382. (1831) 2 B & Ad 232.

the price being payable subject to "hire purchase terms"<sup>383</sup> or clause"<sup>384</sup> or at such price as should be agreed upon between the parties,<sup>385</sup> the agreement in each case was held to be void for uncertainty as to price. Where the price is left to be fixed by a third party, there is no uncertainty and the agreement will be enforceable. Similarly, if the agreement is totally silent as to price, it will be valid, for, in that case, Section 9 of the Sale of Goods Act, 1930 will apply and reasonable price shall be payable.<sup>386</sup>

#### *Agreement to agree or negotiate*

An agreement to agree in the future is void, for there is no certainty whether the parties will be able to agree.<sup>387</sup> In the words of Anson:<sup>388</sup>

The law is generally anxious to uphold the contract wherever possible lest it should incur the reproach of being the destroyer of bargains,<sup>389</sup> but the court must be satisfied that the parties have in fact concluded a contract and not merely agreed to contract in the future.

The decision of the House of Lords in *May & Butcher Ltd v R*<sup>390</sup> laid down a guiding principle.

383. *Scammell v Ousto*, 1941 AC 251.

384. *Bishop & Baxter Ltd v Anglo-Eastern Trading & Industrial Co*, 1944 KB 728; *British Electrical & Associated Industries (Cardiff) Ltd v Patley Pressing Ltd*, (1953) 1 WLR 280.

385. *May & Butcher Ltd v R*, (1934) 2 KB 17n. See also *ITC Classic Finance Ltd v Grapco Mining & Co Ltd*, AIR 1997 Cal 397, an agreement for arbitration provided for appointment of arbitrator by an appointing authority but the identity of such authority was not indicated nor was it capable of being made out, agreement void.

386. *M.S. Madhusoodhanan v Kerala Kaumudi P Ltd*, (2004) 9 SCC 204: AIR 2004 SC 909, transfer of shares, consideration left to be determined at a later date, transfer held not void for uncertainty. S. 9 of the Sale of Goods Act, 1930 allows such transfers. *Jharna Majumdar v Suprobbhat Bhowmick*, (2002) 4 ICC 959 (Cal), uncertain tenancy terms, contract must be specific, the court cannot undertake to supply defects or remove ambiguities. *Claude-Lila Parulekar v Sakal Papers (P) Ltd*, (2005) 11 SCC 73: (2005) 124 Comp Cas 685, acceptance of proposal for sale of goods without payment or agreement as to price, which was to be determined by a third party valuer, valid agreement, the argument that the buyer could hold the seller to ransom was not tenable because not the buyer but a third party had to fix the price and quite naturally the price had to be reasonable and not exploitative.

387. *Punit Beriwala v Suva Sanyal*, AIR 1998 Cal 44, a sum of money paid in advance for purchasing property on terms to be finalised. No such finalisation having taken place for bringing about a registered sale-deed, the court ordered refund of the earnest money. *Leisure Complex v Malaysia Credit Finance Berhad*, (1994) 1 Current LJ 185 (Malaysia), a recommendation to the board of directors that an oral proposal should be accepted, did not amount to acceptance.

388. LAW OF CONTRACT (23rd Edn by Guest, 1972) 25. See, for example, *Union of India v Philips Construction*, (1980) 1 KLT 42 (Case No. 78), where the agreement was for the construction of a railway line and the contractor was not allowed to run away from it by saying that the land was yet to be acquired, particularly when the Government was prepared to give him the benefit of extended time.

389. Quoting Lord TOMLIN in *Hillas & Co Ltd v Arcos. Ltd*, (1932) 147 LT 503, 512 (HL). See R.A. Samek, *Requirement of Certainty of Terms in the Formation of Contract*, 48 Can BR 233.

390. (1934) 2 KB 17n.

There was an agreement for the sale of tentage with a stipulation that the price, dates of payment and manner of delivery "shall be agreed upon from time to time".

The agreement was held to be void for uncertainty. Lord BUCKMASTER remarked: "It has long been a well-recognised principle of contract law that an agreement between two parties to enter into an agreement in which some critical part of the contract matter is left undecided is no contract at all.... It is not open to them to agree that they will in the future agree upon a matter which is vital to the arrangement between them and has not yet been determined." The law requires for the making of a good contract a concluded bargain, "and a concluded contract is one which settles everything to be settled and leaves nothing to be settled by agreement between the parties".

Thus, if the execution of a further contract is a condition or term of the bargain, no contract arises because the law does not recognise a contract to enter into a contract.<sup>391</sup> This view finds further support in the decision of the Court of Appeal in *Courtney & Fairbairn Ltd v Tolaini Bros (Hotels) Ltd*.<sup>392</sup>

A property owner and a property developer-cum-building contractor sat together to arrange a collaboration between them. The contractor wrote a letter to the owner that he was willing to introduce persons who would finance the development of the site and that his own interest was only in the building work. The letter concluded that if a successful arrangement was made with the financiers introduced by him, the owner will enter into negotiations for a fair and reasonable building contract. The negotiations broke down because of a disagreement as to the price. The owner then entered into building contracts with others while still using those very sources of finance.

The contractor sued for the breach of the contract which had either been made or was contracted to be made. The Court of Appeal did not accept his case. Price is a very important term of every contract and the parties in this case neither could agree upon it nor did they lay down any means by which it could be ascertained. Lord DENNING emphasised that there could neither be a contract to enter into a contract nor a contract to negotiate.

P contracted to purchase supplies of propane from D and voluntarily offered to pay a higher price "on the understanding that they would be able to renegotiate a new contract for the following year based on economic value at that time". D did not reply to P's letter but did bill P at a higher price in accordance with P's offer. D refused to renew P's contract. P claimed for breach of contract and, in the alternative that D received

391. Lord PARKER in *Van Hatzfeldt Wildenburg v Alexander*, (1912) 1 Ch 284, 288–89.

392. (1975) 1 WLR 297 (CA). See also *Keshavilal Lallubhai Patel v Lalbhai Trikumal Mills*, AIR 1958 SC 512: 1959 SCR 213 where the contract provided for extension of time in such manner that the whole contract would become uncertain.

excess payment in trust to the use of *P*. It was held that no binding contract regarding the renegotiation of the original contract ever came into existence. A fundamental term was to fix the price in terms of “economic value” which had a different meaning to each party. Therefore, there was no acceptance by *D* of *P*’s offer. *P* was entitled to recover the amount of overpayment.<sup>393</sup>

Where at the time of the agreement for sale of property, a portion of the property was likely to be acquired for road widening and the agreement fixed the price per square yard for whatever area was left after the acquisition, it was held that the agreement suffered from no uncertainty and was, therefore, specifically enforceable.<sup>394</sup>

#### *Undefined property*

The land promised to be sold was to be out of the land still to be acquired or out of the existing property upto the value of one lakh rupees. The price was to be agreed upon at a later date. There was still no certainty upto the time of the suit for specific performance as to identification of the land and price fixation. The agreement was held to be void for uncertainty.<sup>395</sup> The court said in another case that for seeking specific performance, the contract in question must be correct and precise. The plaintiff had failed to identify the property by giving its *Khasra* number or boundary number. The agreement of sale being void for uncertainty, it could not be specifically enforced.<sup>396</sup>

393. *Hidrogas v Great Plains Devp Co of Canada*, (1972) 5 WWR 22 (All Sup Ct). See also *Radhakrishna Sivadutta Rai v Tayeballi Dawoodbhai*, AIR 1962 SC 538: 1962 Supp (1) SCR 81, bought and sold notes differed in contents. No contract resulted. *Nircon Developers (P) Ltd v Zohrabai Fakbruddin*, (1998) 1 Bom CR 153, agreement for sale of land without prior sanction of I.T. authorities, vital entries like names, amounts and places still in blank, held no agreement and no specific enforcement. *Old World Hospitality (P) Ltd v India Habitat Centre*, (1997) 73 DLT 374, a complete agreement in all respects, agreement over all the essential terms. *B.D.A. Ltd v State of U.P.*, AIR 1995 All 277, renewal of agreement for assignment of trade to be on terms agreed by mutual consent, did not create any obligation upon either party for renewal. *Army Welfare Housing Organisation v Sumangal Services (P) Ltd*, (2004) 9 SCC 619: AIR 2004 SC 1344, a promise that the builder would get the building plan approved by the authorities, void for uncertainty. An agreement to obtain a statutory order from a statutory Authority is not enforceable since the promisor cannot have any control upon Authorities.

394. *Sughra Bee v Kaneez Fatima Qureshi*, (2004) 3 ALD 821; *Shobatdei v Devipal*, (1972) 3 SCC 495: AIR 1971 SC 2192, price to be paid for the instruments of husbandry, it was provided that the buyer would pay the price fixed by the first defendant, held no uncertainty.

395. *P. Panneerselvan v A. Baylis*, (2005) 5 CTC 17; *Ganesh Industries v Bharat Rubber Co*, (2006) 2 CTC 182, property not identifiable, no time limit for performance, even price was not mentioned, no concluded contract. *N.K. Giriraja Shetty v N.K. Parthasarathy*, (2006) 3 AIR Kant 136 (DB): AIR 2006 Kant 180, agreement of sale nowhere mentioned the extent of respective shares of sellers and what consideration was to be paid to them respectively, the extent of property to be sold was also vague, the plaintiff was also not able to offer any explanation, no enforcement; *Umeshanker Sao v Sonsai Sahu*, AIR 2006 Chhat 102, sale of land, evidence of identity of land was placed on record, no infirmity, mentioning of *Khasra* number, etc was not necessary, agreement not vitiated.

396. *Surendra Kumar Gupta v Narayan Ram*, AIR 2011 Chh 138.

*Preliminary negotiations taking definite shape*

Where, on the other hand, the preliminary negotiations have crystallised into a definite shape, the parties can be compelled to contract on those terms. This is borne out by the following two decisions. One of them is that of the House of Lords in *Hillas & Co Ltd v Arcos Ltd.*<sup>397</sup>

The contract was to purchase for the year 1930 "22,000 standards of soft wood goods of fair specification", with an option to buy 1,00,000 for the year 1931. When the option for 1931 was sought to be exercised, the seller said that this part of the agreement was not enforceable because it did not specify any particulars.

The agreement was, however, allowed to be enforced. The dealing for the previous year indicated the intention to have a similar dealing and also made it unnecessary for the particulars to be repeated.

The other case is *Mallozzi v Carapelli.*<sup>398</sup>

The contract was for the sale of oats and maize to be shipped from Argentina to the West Coast of Italy. The port of discharge was to be agreed between the parties when the ship would cross the Straits of Gibraltar. The seller ordered, without consulting the buyer, the cargo to be discharged at Naples. The buyer suffered two-fold loss, viz., owing to congestion at that port and further transport. The seller contended that that term being left to future agreement the contract was void.

But the court saw no element of uncertainty. There was a definite agreement that the port of discharge would be settled by mutual agreement and it was this agreement which the seller had broken.

In a similar case before a Canadian court<sup>399</sup> a motor vehicle dealer was negotiating with his manufacturer for shifting his agency to larger premises. As a part of these negotiations the manufacturer undertook to absorb the dealer's losses till their new arrangement was concluded. How the losses would be absorbed was not stated. Even so the agreement was held to be binding. How the losses would be absorbed was the manufacturer's concern and not that of the dealer. The manufacturer had committed himself to a definite obligation.

With this should be contrasted the case<sup>400</sup> in which a sum of money was deposited with a car dealer for purchasing a used car which the depositor was ultimately unable to buy. The parties then agreed that the dealer should hold the amount till the depositor was able to buy a car at a stated price or more. The depositor then sought refund of his deposit and was allowed. The type of car, the time of purchase, the mode of finance were all uncertain and these uncertainties prevented the parties from being bound. A document for

397. (1932) 147 LT 503, 512 (HL).

398. (1976) 1 Lloyd's Rep 407 (CA).

399. *MacIver v American Motors*, (1976) 70 DLR (3d) 473.

400. *Dwinell v Custom Motors*, (1975) 12 NSR (2d) 524 (SC App Div).

sale of certain lands provided that the sale and purchase agreement was to be signed on or before the specified date and it was to incorporate all the terms of the sale and other usual terms and conditions and that if the agreement was not signed by the cut-off date, the amount of deposit was to be refunded. The court said that the document did not mature into a contract. No specific enforcement of the sale could be ordered.<sup>401</sup>

*Partial uncertainty: "Capable of being made certain"*

Where only a part or a clause of the contract is uncertain, but the rest is capable of bearing a reasonably certain meaning, the contract will be regarded as binding. In a contract to sell 3000 tons of steel reinforcing bars, the buyer accepted, but subject to "the usual conditions of acceptance only". There being no evidence of any such usual conditions, the buyer was held to be bound by the rest of the contract.<sup>402</sup>

In a contract for the purchase of land, the price was payable in three phases and the land was also to be released for further construction in three phases. The contract was held to be void by reason of uncertainty as to which part of the land was to be released in the successive phases. Should the power be vested in the purchaser, the vendor might be seriously prejudiced by the manner in which the power was exercised. In the absence of any express term as to how the land to be included in each phase was to be selected, the contract was void for uncertainty.<sup>403</sup> But in a contract for sale

401. *Kam Mah Theatre v Tan Lay Soon*, (1994) 1 Curr LJ 1 "The correspondence between the parties after the date of the document was relevant for finding out whether there was any contract at all, *Hussey v Horne-Payne*, (1879) LR 4 AC 311 at p. 316. The question whether the parties have entered into contractual relationship with each other essentially depends upon the proper understanding of the expressions they have employed in communicating with each other considered against the background of the circumstances in which they have been negotiating including in those circumstances the provisions of any applicable law. Where they have expressed themselves in writing, the proper construction of the writing against the background will answer the question." Cited by the court from the Privy Council decision in *Daiman Development v LCT Mathew*, (1981) 1 Malasiya LJ 56 at p. 58.

402. *Nicolene Ltd v Simmonds*, (1953) 1 QB 543; (1953) 2 WLR 717. *Mayban Finance v Aik Soon Auto*, (1994) 1 Curr LJ 273 (Malaysia), no discount rates were stated, received money on discount, the contract having been acted upon with knowledge that discount rates would have to be settled by agreement, contract binding, no uncertainty. *Kalyan Singh v Ranjot Singh*, AIR 2002 HP 180, the undertaking that the plaintiff would not enforce the payment of a cheque till goods were delivered was held to be void because there was no definite time fixed for performance, but it was valid to the extent to which the defendant admitted that he had actually received the goods. *Rajkishor Mohanty v Banabehari Patnaik*, AIR 1951 Ori 291.

*Damodhar Tukaram Mangalmurti v State of Bombay*, AIR 1959 SC 639, the court can construe the terms of an agreement in fair and equitable manner in case of uncertainty. *Khivraj Chordia v Esso Standard Eastern Inc*, AIR 1975 Mad 374, rent to be fixed with reference to rent prevailing in the locality. Such rent could be ascertained. *Veera Exports v T. Kalavathy*, (2002) 1 SCC 97: AIR 2002 SC 38 uncertainty in a cheque can be removed by parties.

403. *Bushwall Properties Ltd v Vortex Properties Ltd*, (1976) 1 WLR 591 (CA). *Dwinell v Custom Motors*, (1975) 12 NSR (2d) 524 (SC App Div). An agreement to pay when the party

of "one acre of front land", out of a tract of 5 acres, the contract was held to be not uncertain, it being possible to find out what was the meaning of the parties by the words "front land".<sup>404</sup> At the time when the agreement to sell a property was made, it was known that a portion of the property was likely to be acquired for road widening. The agreement, therefore, stipulated that whatever property was left behind after acquisition would be sold at agreed rate. The agreement was held to be capable of performance. The relief of specific performance was allowed.<sup>405</sup> A person wished to purchase corn feed pellets and his brokers carried out negotiations with a seller through intermediary brokers. There were various telex messages pursuant to which the seller contended that a binding contract had been concluded, but the buyer contended that many points had still to be settled. The court said that the parties were *ad idem* as to the main terms of the proposed contract and it was perfectly possible for parties to make an interim agreement for the sale of goods which required further negotiations to iron out the less important details of the transaction.<sup>406</sup> Where an agreement provided that a property in joint names should be sold at a price agreed between the owners, and if not sold within six months, should be placed at auction, it was necessary to imply a term that the agreed price should be a reasonable price. The contract was clear and workable in its existing form.<sup>407</sup> Where the vital terms of the contract like the price and the area of land and the time for completion of sale were all fixed, the Supreme Court held that the mere fact that the mode of payment of the price was not settled did not render the contract to be ineffective.<sup>408</sup> Where a contract for the sale of bearing springs over a course of time gave latitude to the seller as to quantity of delivery in each instalment, it did not make the agreement uncertain.<sup>409</sup> Sometimes the principle of business efficacy is used to lend support to the agreement to make it effective in consonance with the parties' intention. This can be done only when

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is in a position to pay has been held to be void for uncertainty. *Puspabala Ray v LIC*, AIR 1978 Cal 221.

404. *Kandamath Cine Enterprises (P) Ltd v John Philipose*, AIR 1990 Ker 188.

405. *Sughra Bee v Kaneez Fatima Qureshi*, (2004) 3 ALD 821.

406. *Pagnan Spa v Feed Products*, (1987) 2 Lloyd's Rep 601 (CA).

407. *Miller v Lakefield Estates*, The Daily Telegraph, May 8, 1988 (CA).

408. *Kollipara Sriramulu v T. Aswathanarayana*, AIR 1968 SC 1028: (1968) 3 SCR 387. Also see *Dhanrajmal Gobindram v Shamji Kalidas & Co*, AIR 1961 SC 1285: (1961) 3 SCR 1320 where it was held that a sale agreement subject to the usual *Force Majeure clause* was not void for vagueness.

See also *Uttam Singh Dugal and Co (P) Ltd v Hindustan Steel Ltd*, AIR 1982 MP 206, where the court held that deposit by a contractor of insurance bonds instead of Government securities which was put under consideration did not prevent the contract from arising; the fact that penalty for delayed completion could be on the basis of total cost or cost of the incomplete part as could be decided by the head office and difficulties of interpretation did not make the agreement uncertain.

409. *Jamma Auto Industries v Union of India*, AIR 1984 Del 235. *Remington Rand of India v Sohanlal Rajgharia*, AIR 1984 Cal 158, tenancy on the basis of market rent, which the court found to be ascertainable, held not uncertain.

the agreement or its terms are either ambiguous or not clear.<sup>410</sup> Contracts are not readily declared to be invalid for uncertainty or vagueness. The court found in the case before it a contract which was for sale of immovable property but the parcel of land was not identified, nor it was ascertainable. Hence there was no contract which could be enforced.<sup>411</sup> In a case before the Allahabad High Court, the facts and decision appear from the following passage:<sup>412</sup>

The terms of the agreement were that the tenant was to construct a sitting place and install a new gate and deduct the cost from rent which was enhanced from Rs 5 to Rs 11/8 per month. The cost of construction was not known to the parties at the time, but it is obvious that they agreed that the entire cost, whatever the amount, would be adjusted against rent. The agreement was, therefore, capable of being made certain and did in effect become certain when the constructions were completed and the amount spent was known. The purpose of Section 29 is to ensure that the parties should be aware of the precise nature and scope of their mutual rights and obligations.

#### *Agreement to increase wages*

An act of the State to increase wages of its employees is a welfare measure. When such increase takes place with retrospective effect, its validity can be upheld because it is for the benefit of its employees. Such a gesture could not be enforced against a licensee of the State. The licensee would have been bound if there was a specific term in the licence to that effect. Section 29 would not permit enforcement of the terms of a scheme which are so vague and indefinite that it may not be possible to ascertain with reasonable certainty the intention of the parties. The meaning of a contract must be clear on its face. Furthermore, whatever increase was agreed to be given in this case had already been granted. A new liability cannot be enforced under a contract which had already been worked out.<sup>413</sup>

#### *Agreement not capable of being enforced*

This happens when the agreement is in the state of a mess. The plaintiff in this case was the owner of two houses which were not constructed by him with his own funds and he permitted his brother (defendant) to occupy one of the houses. The defendant pleaded about an agreement which contained

410. *Satya Jain v Anis Ahmed Rushdie*, (2013) 8 SCC 131; (2013) 3 SCC (Civ) 738.

411. *Pawan Kumar Dutt v Shakuntala Devi*, (2010) 15 SCC 601; (2013) 2 SCC (Civ) 235.

412. *Chandra Sheikhar v Gopi Nath*, AIR 1963 All 248; *Kovuru Kalappa Devara v Kumar Krishna Mitter*, ILR 1945 Mad 521; AIR 1945 Mad 10, agreement to pay a certain sum after two years with interest and deductions to be agreed upon, void. *Samina Venkata Sureswara Sarma v Meesala Kota Muvullayya*, AIR 1996 AP 440, sale of premises within stipulated time, tenants to be evicted within that time, failure to do so but efforts being made, did not make the agreement uncertain and void.

413. *Govt of Maharashtra v Deokar's Distillery*, (2003) 5 SCC 669: AIR 2003 SC 1216.

a term that the construction was carried out with contributed funds and the plaintiff agreed to transfer one house to the defendant on a settlement of the account. An endorsement was made in the agreement that the plaintiff relinquished his share in the property in favour of his mother. The mother executed a will bequeathing the property in favour of two sons, plaintiff and defendant. Thus the agreement became inexecutable.<sup>414</sup>

### *Lock-out agreement*

A lock-out agreement by which one party for good consideration agrees for a specified period of time, not to negotiate with anyone (sale of business and premises in this case) except the other party for the sale of his property, can constitute an enforceable agreement. Such an agreement enables the would be buyer to purchase, for a price, an exclusive right of negotiations for finalising the deal. However, an agreement to negotiate in good faith for an unspecified period is not enforceable and nor can a term to that effect be implied in a lock-out agreement, since the vendor is not obliged under such an agreement to conclude a contract with the purchaser. He would not be able to know when he can withdraw from on-going negotiations. The court cannot also be expected to decide whether, subjectively, a proper reason existed for the termination of negotiations.<sup>415</sup>

### *Option for renewal of tenancy*

An option for renewal of a tenancy or lease is an enforceable option.<sup>416</sup> But an option clause which provides for renewal of a lease on such terms as may be agreed upon by the parties at the time of renewal would make it invalid and unenforceable for uncertainty.<sup>417</sup>

### *Contract linked with repeal of an Act*

Where the performance of an agreement could be demanded only on the repeal of an Act, which prevented fragmentation of holdings, the same was held to be void because repeal was an uncertain event and the object was in violation of an existing Act.<sup>418</sup>

## **Wagering agreements [S. 30]**

Section 30 deals with wagering agreements.

**S. 30. Agreements by way of wager, void.**—Agreements by way of wager are void; and no suit shall be brought for recovering anything alleged to be won on any wager, or entrusted to any person to abide by the result of any game or other uncertain event on which any wager is made.

414. *D. Narasimhamurthy v D. Krishnamurthy Rao*, (2005) 1 An LD 75: (2005) 1 CCC 566 (AP).

415. *Walford v Miles*, (1992) 2 AC 128: (1992) 2 WLR 174 (HL).

416. *Caltex (India) Ltd v Bhagwan Devi Marodia*, AIR 1969 SC 405: (1969) 2 SCR 238, option of renewal of lease.

417. *Aboobacker Keyi v Govindan Sons*, (1990) 2 KLT 551.

418. *Parvathamma v Uma*, AIR 2011 Kant 58.

**Exception in favour of certain prizes for horse racing.** — This section shall not be deemed to render unlawful a subscription or contribution, or agreement to subscribe or contribute, made or entered into for or towards any plate, prize or sum of money, of the value or amount of five hundred rupees or upwards, to be awarded to the winner or winners of any horse race.

**Section 294-A of the Indian Penal Code not affected.** — Nothing in this section shall be deemed to legalize any transaction connected with horse-racing, to which the provisions of Section 294-A of the Indian Penal Code (XLV of 1860) apply.

### Requirements of definition

Section 30 only says that “agreements by way of wager are void”. The section does not define “wager”. SUBBA RAO J (afterwards CJ) in *Gherulal Parakh v Mahadeodas*<sup>419</sup> said: “Sir William Anson’s definition of “wager” *As a promise to give money or money’s worth upon the determination or ascertainment of an uncertain event*, brings out the concept of wager declared void by Section 30 of the Contract Act.”

The most illustrative definition of “wager” is that given by HAWKINS J in *Carlill v Carbolic Smoke Ball Co.*<sup>420</sup>

A wagering contract is one by which two persons professing to hold opposite views touching the issue of a future uncertain event, mutually agree that, dependent on the determination of that event, one shall pay or hand over to him, a sum of money or other stake; neither of the contracting parties having any other interest in that contract than the sum or stake he will so win or lose, there being no other real consideration for the making of such contract by either of the parties. It is essential to a wagering contract that each party may under it either win or lose, whether he will win or lose being dependent on the issue of the event, and, therefore, remaining uncertain until that issue is known. If either of the parties may win but cannot lose, it is not a wagering contract.<sup>421</sup>

This statement has the merit of bringing out all the essential features that make a transaction a wager.

#### 1. *Uncertain event*

The first thing essential to wager is that the performance of the bargain must depend upon the determination of an uncertain event. A wager generally contemplates a future event; but it may even relate to an event which has already happened in the past, but the parties are not aware of its result or the time of its happening.<sup>422</sup>

419. AIR 1959 SC 781: (1959) 2 SCR 406.

420. (1893) 1 QB 256 (CA).

421. This statement has been cited with approval in a number of cases in India. See for example, *Jethmal Madanlal Jokotia v Nevatia & Co*, AIR 1962 AP 350, 352.

422. See Anson’s PRINCIPLES OF THE ENGLISH LAW OF CONTRACTS (22nd Edn by A.G. Guest, 1964) 301 where the learned writer says that the parties may bet upon the “result of an

## 2. Mutual chances of gain or loss

The second essential feature is that upon the determination of the contemplated event each party should stand to win or lose. If there are no such mutual chances of gain or loss, there is no wager. Thus, in *Babasaheb v Rajaram*:<sup>423</sup>

Two wrestlers agreed to play a wrestling match on condition that the party failing to appear on the day fixed was to forfeit Rs 500 to the opposite party, and the winner was to receive Rs 1125 out of the gate money. The defendant failed to appear in the ring and the plaintiff sued him for Rs 500.

It was held that the agreement could not be looked upon as one of wagering in law. "It is of the essence of wager that each side should stand to win or lose according to the result of the uncertain event."<sup>424</sup> In the present case neither side stood to lose according to the result of the wrestling match. "The stakes did not come out of the pockets of the parties, but had to be paid from the gate money provided by the public."<sup>425</sup> The prize would not have been recoverable if it was to be subscribed by the competitors themselves. Accordingly, where each of the parties deposited £200 with a stakeholder to abide the issue of a walking match and the loser was to forfeit his £200,<sup>426</sup> and where each party deposited £100 to abide the result of a billiard match,<sup>427</sup> the agreements were held to be of wagering nature. In contrast to it the transaction in *Carlill v Carbolic Smoke Ball Co* was held to be not a wager. The company had no chance of winning, neither Mrs Carlill any chance of losing.<sup>428</sup>

A chit fund does not come within the scope of "wager". It is no doubt true that some chance gain may come to some of the members, but none of them stands to lose his money, for his periodical deposits are refunded to him at the end of the scheme. This was so held by the Madras High Court in *Narayana Ayyangar v K. Vallachami Ambalam*.<sup>429</sup> RAMESAM J said: "It is true that in most chit fund transactions, no subscriber loses the money he has contributed; and so long as getting back the actual amount of subscription is assured, the interval of time, however long it may be, is immaterial."

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election which is over, if the parties do not know in whose favour it has gone". See also Cheshire and Fifoot, *LAW OF CONTRACT* (6th Edn 1964) 232, where it is said that "wager may relate to past, present or future events".

423. AIR 1931 Bom 264.

424. BARLEE J quoted this definition from *Sassoon v Tokersey*, ILR (1913) 28 Bom 616.

425. MADGAVKAR J quoted from *Shoobred v Roberts*, (1899) 2 QB 560.

426. *Diggle v Higgs*, (1877) LR 2 Ex D 422.

427. *Shoobred v Roberts*, (1899) 2 QB 560.

428. *Carlill v Carbolic Smoke Ball Co*, (1893) 1 QB 256 (CA). See also *Ellesmere v Wallace*, (1929) 2 Ch 1 (CA).

429. ILR (1927) 50 Mad 696.

The transaction being valid, a member was allowed to recover his subscriptions when the organisers refused to run the scheme up to the promised schedule.

### 3. *Neither party to have control over the event*

Thirdly, neither party should have control over the happening of the event one way or the other. "If one of the parties has the event in his own hands, the transaction lacks an essential ingredient of a wager."<sup>430</sup>

### 4. *No other interest in the event*

Lastly, neither party should have any interest in the happening of the event other than the sum or stake he will win or lose. This is what marks the difference between a wagering agreement and contract of insurance. Every contract of insurance requires for its validity the existence of insurable interest. An insurance effected without insurable interest is no more than a wagering agreement and, therefore, void.<sup>431</sup> "Insurable interest" means the risk of loss to which the assured is likely to be exposed by the happening of the event assured against. In a wager, on the other hand, neither party is running any risk of loss except that which is created by the agreement itself.<sup>432</sup>

Whether an agreement is of a wagering nature depends upon the substance and not the words of the agreement.<sup>433</sup> The real object of the parties must be discovered. "It makes no difference that there was real intention to part with the goods. If a horse of £ 100 is to be sold and the buyer and seller agree that upon one event the price shall be nothing and upon another £ 200, that is a wager, though there may be real intention of selling the horse."<sup>434</sup>

The facts of the case<sup>435</sup> in which the above passage occurs were that a seller and buyer disagreed respecting whether or not payment had been made for some goods in the past. They mutually agreed that one price would be payable if the buyer was correct and another price would be paid if the seller was correct. The seller's memory proved better, but he could not recover anything from the buyer as the court held the arrangement to be of wagering nature.

### *Right to seek performance*

Where the contract conferred the right to seek actual delivery of goods and, therefore, the plaintiff could compel actual performance, the court said

430. BIRDWOOD J in *Dayabhai Tribhovandas v Lakshmichand*, ILR (1885) 9 Bom 358, 363.

431. See *Alamiani v Positive Govt Security Life Assurance Co*, ILR (1898) 23 Bom 191.

432. See BLACKBURN J in *Wilson v Jones*, (1867) LR 2 Exch 139. See also *Manishankar v Allianz Und Stuttgarter Life Ass Bank Ltd*, 193 IC 155.

433. *Ismail Lebbe Marikar Ebrahim Lebbe v Bartlett & Co*, (1942) 55 LW 332: AIR 1942 PC 19: 199 IC 574 an appeal from Ceylon.

434. Lord CAMPBELL CJ in *Rourke v Short*, (1856) 5 El & Bl 904: 119 ER 717.

435. *Rourke v Short*, (1856) 5 El & Bl 904: 119 ER 717.

that the contract could not be termed as a wager. Common intention of the parties to enter into a wagering transaction is a *sine qua non* for a transaction to be dumped as wager.<sup>436</sup>

### *Speculative transactions*

An agreement to settle the difference between the contract price and market price of certain goods on a specified day has been repeatedly held to be a wager. But, as transactions of this kind are always expressed in the form of an agreement for the sale or purchase of goods, it often becomes difficult to ascertain the real object of the parties. Yet the intention of the parties is the only deciding factor, for the Privy Council ruled in 1901 in an appeal from Burma<sup>437</sup> under Section 30 of the Contract Act that “where the circumstances as to contracts for sale, purchase and delivery of goods are such as to warrant the legal inference that the parties never intended any actual transfer, but only to pay or receive differences, the contracts must be deemed to be by way of wager”.<sup>438</sup> “Thus, there must be from the outset a common intention of both the parties to make and accept no delivery and to deal only in differences. From the mere fact that the delivery of the goods was not taken, no inference can be drawn that the contract was a wagering contract.”<sup>439</sup> If it is intended and is possible that the goods contracted for can be delivered then, the mere fact that in certain circumstances either party would be liable to make good to the other the difference in price, cannot make it a wager.<sup>440</sup>

Wagering agreements are speculative in nature but every speculation need not necessarily be wager. Derivatives contracts satisfy first ingredient as there are two parties. Second ingredient that one may stand to lose may be absent as plaintiff in event of losing in the underlying contract on account of currency fluctuation may get compensated by hedging and vice versa. Third test of wager is absent as both parties definitely have actual interest in rate of exchange hitting high or low. Derivatives transaction resembles contract of insurance. In a wager there must be common intention to wager and such intention is absent in derivatives contracts. Derivatives transactions follow scientific pattern on basis of financial mathematics. Derivatives contracts are not wagering contracts.<sup>441</sup>

The intention of the parties is gathered from the circumstances surrounding their agreement. Thus, where a rice mill owner agreed to sell 1,99,000

436. *Rajshree Sugars and Chemicals Ltd v Axis Bank Ltd*, AIR 2011 Mad 144.

437. *Kong Yee Lone & Co v Lowjee Nanjee*, (1900–01) 28 IA 239: ILR (1902) 29 Cal 461.

438. MUKARJI J's summing upon the ratio of the Privy Council decision in *Badridas Kothari v Meghraj Kothari*, AIR 1967 Cal 25.

439. *Hagami Lal Ram Prasad v Bhuralal Ram Narain*, AIR 1961 Raj 52.

440. *Buddulal Goerlal Mahajan v Shrikisan Chandmal*, AIR 1961 MP 57. *Morgan Grenfell & Co Ltd v Welwyn Hatfield District Council*, (1995) 1 All ER 1, one of the interest rates in swap cases, where the court held that transactions entered into by way of business under the Financial Services Act, 1986 (English) are out of the scope of wagering transactions.

441. *Rajshree Sugars & Chemicals Ltd v Axis Bank Ltd*, (2009) 1 CTC 227 (Mad).

bags of rice, worth about a crore of rupees, when his actual capacity was much less, the Privy Council held the agreement to be a wager.<sup>442</sup> Their Lordships said: "Now the output of the firm itself would not be much over 60,000 bags during the currency of the contracts. The capital of the company was a trifle more than a lakh of rupees. The cost of goods would be that amount multiplied by five hundred fold. It is possible for traders to contemplate transactions so far beyond their basis of trade but it is very unlikely. In point of fact, they never completed nor were they called on to complete any one of the ostensible transactions. The rational inference is that neither party ever intended completion."

Similarly, where a contract was made for the sale of certain goods in a market where such goods never appeared, it was held that the common intention was to wager.<sup>443</sup>

In another Privy Council decision, delivery orders having been issued which could have been converted into actual delivery if a party so desired, it was held that the transaction could not be described as a wager.<sup>444</sup> Similarly, where out of a large number of transactions, the court found that on occasions delivery of goods was made and accepted, making it difficult to know beforehand which way a particular transaction was going to end, the intention to wager was held to be not established.<sup>445</sup> In an Andhra Pradesh case,<sup>446</sup> a *pucca addatia*, whom the court found to be an independent contractor and not an agent, received orders from his principal to purchase certain goods. He contracted to do so but subsequently settled the difference with the seller and claimed the loss and his commission from the principal. The court said: The circumstances do not warrant the inference that the plaintiff intended to deliver or the defendant intended to take delivery of the wagon of groundnut oil. In fact the defendant had no shop or godown at Adoni and is not even a resident of the place.

Accordingly, no action lay for the enforcement of the transaction.<sup>447</sup>

### Effects of wagering transactions

A wagering agreement being void cannot be enforced in any court of law. Section 30 expressly declares that "no suit shall be brought for recovering anything alleged to be won on any wager, or entrusted to any person to abide the result of any game or other uncertain event on which any wager is made". Thus the amount won on a wager cannot be recovered. In a case before the Calcutta High Court:<sup>448</sup>

442. *Kong Yee Lone & Co v Lowjee Nanjee*, (1900–01) 28 IA 239: ILR (1902) 29 Cal 461.

443. *Doshi Talacshi v Shah Ujarsi Velsi*, ILR (1899) 24 Bom 227.

444. *Sukdevdoss Ramprasad v Govindoss Chathurbujdoss & Co*, (1927–28) 55 IA 32: AIR 1928 PC 30; also see *Duni Chand Rataria v Bhuvalka Bros Ltd*, AIR 1955 SC 182: (1955) SCR 1071; *Bashir Ahmad v Govt of A.P.*, AIR 1970 SC 1089.

445. *Arjunsa Raghusa v Mohanlal Harakchand*, AIR 1937 Nag 345.

446. *T.G. Lakshmi Narayana Chetty v K.V. Nanjaiah Chetty*, AIR 1965 AP 136.

447. Compare with *Kishanlal v Bhanwar Lal*, AIR 1954 SC 500 (1955).

448. *Badridas Kothari v Meghraj Kothari*, AIR 1967 Cal 25.

Two persons entered into wagering transactions in shares and one became indebted to the other. A promissory note was executed for the payment of that debt.

The note was held to be not enforceable.<sup>449</sup> A subsequent substituted agreement of the same consideration, namely, the amount won on a wager, is also not enforceable.<sup>450</sup> In other words, a new promise to pay money won upon a wager is equally void. Similarly, money deposited with a person to enable him to pay to the party winning upon a wager cannot be recovered. The winner cannot recover the money, but before it is paid to him, the depositor may recover from the stakeholder.<sup>451</sup> But where the money has already been paid over, it cannot be recovered back.<sup>452</sup>

### *Collateral transactions*

It has been laid down by the Supreme Court, following previous authorities, in *Gherulal Parakh v Mahadeodas*<sup>453</sup> that “though a wager is void and unenforceable, it is not forbidden by law”. Hence a wagering agreement is not unlawful under Section 23 of the Contract Act,<sup>454</sup> and, therefore, the transactions collateral to the main transaction are enforceable. “Accordingly an agent who paid the losses on wagering transactions was allowed to recover the amount paid by him from his principal.”<sup>455</sup> Similarly, in another case, “the plaintiff who lent money to the defendant to enable him to pay off a gambling debt was given a decree to recover the same from the defendant”.<sup>456</sup> “Where two partners entered into a contract of wager with a party and one partner had satisfied his own and his co-partner’s liability under the contract, the Nagpur High Court<sup>457</sup> held that the partner who paid the amount could legally claim the other partner’s share of the loss.” Similarly, the Supreme Court held in *Gherulal Parekh v Mahadeo*<sup>458</sup> that for a partnership to enter into wagering transactions is not illegal under Section 23 of the Act and therefore a partner who has paid the losses on wagering transactions may recover proportionate indemnity from his co-partners.



CASE PILOT

### **Exceptions**

#### **1. Horse race [S. 30 (exception)]**

The section does not render void a subscription or contribution, or an agreement to subscribe or contribute, toward any plate, prize or sum of

449. MUKHERJI J reviews at p. 28 all the earlier authorities.

450. *Hill v William Hills (Park Lane) Ltd*, 1949 AC 530 (HL).

451. See *Ratnakalli Guranna v Vachalipu*, AIR 1923 Mad 434.

452. See BOWEN LJ in *Bridger v Savage*, (1885) LR 15 QB 363, 367.

453. AIR 1959 SC 781: (1959) 2 SCR 406.

454. This was so held as early as 1883 in *Pringle v Jafar Khan*, ILR (1883) 5 All 443.

455. *Shibbo Mal v Lachman Das*, ILR (1901) 23 All 165.

456. *Beni Madho Das v Kaunsal Kishore Dhusar*, ILR (1900) 22 All 452.

457. *Mohd Gulam Mustafa Khan v Padamsi*, AIR 1923 Nag 48.

458. *Gherulal Parakh v Mahadeodas*, AIR 1959 SC 781: (1959) 2 SCR 406.

money, of the value or amount of five hundred rupees or upwards to the winner or winners of any horse races.

## 2. Crossword competitions and lottery

“If skill plays a substantial part in the result and prizes are awarded according to the merits of the solution, the competition is not a lottery. Otherwise it is.”<sup>459</sup> Thus, literary competitions which involve the application of skill and in which an effort is made to select the best and most skilful competitor, are not wagers.<sup>460</sup> But where prizes depend upon a chance, that is a lottery.<sup>461</sup> The Madhya Pradesh High Court has characterised lotteries as wager. An agreement for payment of prize money on a lottery ticket came within the category of wagering agreement as contemplated by Section 30. The court further said that the provisions of neither a Central Act nor that of a State Act controlling the activities relating to lottery would change the basic nature of the transaction.<sup>462</sup> A suit for recovery of the prize money was not allowed. The lottery in question was organised by the Raffle Committee, Indore, for raising funds for a Table Tennis Trust with due permission from the State Government.

## ILLEGAL AND VOID AGREEMENTS

The Contract Act draws a distinction between an agreement which is only void and the one in which the consideration or object is also unlawful. “Section 23 points out in what cases the consideration of an agreement is unlawful, and in such cases the agreement is also void, that is, not enforceable at law.”<sup>463</sup> Sections 25 to 30 refer to cases in which the agreement is only void, though the consideration is not necessarily unlawful. An illegal agreement is one which is actually forbidden by the law; but a void agreement may not be forbidden, “the law may merely say that if it is made, the courts will not enforce it”.<sup>464</sup> Thus, every illegal contract is also void, but

459. Lord HEWARD CJ in *Coles v Odhams Press Ltd*, (1936) 1 KB 416 (DC).

460. *Moore v Elphick*, (1945) 2 All ER 155 (CA).

461. *Boucher v Rowsell*, (1947) 1 All ER 870 (DC).

462. *Subhash Kumar Manwani v State of M.P.*, AIR 2000 MP 109. The DB upheld the dismissal of a similar suit based on a lottery ticket by relying on the decision of the Bombay High Court in the case of *Sir Dorabji Jamsetji Tata Ltd v Edward P. Lance*, AIR 1917 Bom 138. In that case (*Shekhar Chand Jain*) it was a state lottery and a suit founded on a ticket sold in the lottery was dismissed holding that though the State lottery was not illegal, it was nonetheless in the nature of a wager. The court cited the decision of the Supreme Court in *B.R. Enterprises v State of U.P.*, (1999) 9 SCC 700: AIR 1999 SC 867, the Supreme Court refused to recognise lottery as a trade or profession. Even the State sponsored lotteries have the same element of chance as private lotteries, there being no application of skill in either case. The State sponsorship only creates public confidence by ruling out fraud, etc. Imposing a tax on lottery does not give it the status of a trade or profession.

463. See *Pringle v Jafar Khan*, ILR (1883) 5 All 443, 445.

464. Sir William Anson's PRINCIPLES OF THE ENGLISH LAW OF CONTRACT (20th Edn, 1952) 205, cited by SUBBA RAO J (as he then was) in *Gherulal Parakh v Mahadeodas*, supra at p. 341.

a void contract is not necessarily illegal. However, the distinction is not always clear.

### Main transaction void in either case

Another similarity between an illegal and a void agreement is that in either case, the main or the primary agreement is unenforceable. Nothing can be recovered under either kind of agreement and if something has been delivered or some payment made, it cannot be recovered back.

### No action under the main transaction

As laid down by the Supreme Court:

The principle of public policy is this: *ex dolo mala non oritur actio*. No court will lend its aid to a man who found his cause of action upon an immoral or an illegal act. If the cause of action appears to arise *ex turpe cause*, or the transgression of a positive law, there the court says that he has no right to be assisted.<sup>465</sup>

Thus, a guilty party has no right of action on an illegal contract. A person who contracted to hire a premises, unknown to the landlord, for holding a meeting for a blasphemous purpose, was not allowed to sue the landlord for breach of contract when the landlord, on learning the real purpose, refused to give the premises.<sup>466</sup> Money lent for an illegal purpose is irrecoverable.<sup>467</sup> A renewed promise to pay an illegal debt will be equally tainted by the illegality.<sup>468</sup> In such cases the law leaves the parties where it finds them. "The court will help neither party. 'Let the estate lie where it falls'."<sup>469</sup> Where a person paid a sum of money to a charitable organisation and promised to pay more if a knighthood was procured which never materialised, he could not recover back the money.<sup>470</sup> Where a sum of money was paid to secure a Government job through high-profile political leaders and there being no success, an attempt was made to take back the money. The recipient issued a cheque in refund. The payment of the cheque was not allowed to be enforced. No prosecution under Section 138 Negotiable Instruments Act was allowed because there was no legally enforceable debt or liability.<sup>471</sup> Where a contract is lawful at its inception, but is performed in an unlawful manner, no recovery may be allowed. Thus, in a contract of transport, the lorry was overloaded, which was an offence under the Road Traffic Act, 1988 and the goods having been damaged during the journey,

465. *Kedar Nath Matani v Prahlad Rai*, AIR 1960 SC 213, 217: (1960) 1 SCR 861; *Koteswar Vittal Kamath v K.R. Baliga & Co*, (1969) 1 SCC 255, 265: AIR 1969 SC 504.

466. *Cowan v Milbourn*, (1867) 36 LJ Ex 24.

467. *C.H.T. Ltd v Ward*, (1965) 2 QB 63: (1963) 3 WLR 1071 (CA), money lent for betting purposes.

468. *Hill v William Hills (Park Lane) Ltd*, 1949 AC 530 (HL).

469. *Surasibalini Debi v Phanindra Mohan Mazumdar*, AIR 1965 SC 1364.

470. *Parkinson v College of Ambulance Ltd*, (1925) 2 KB 1.

471. *Virender Singh v Laxmi Narain*, (2006) 135 DLT 273.

the consignor was not allowed to recover the loss. His manager had knowledge of the overloading.<sup>472</sup>

“When it is apparent on the face of a contract that it is unlawful, it is the duty of the judge himself to take an objection and that too, whether or not the parties take or waive the objection. It is, therefore, open to the court even without a pleading to consider the question whether the agreement relied on or proved in the case is immoral.”<sup>473</sup>

### Exceptions

#### 1. Where the contract is still executory

Where the contract is still executory, in the sense that no part of the illegal purpose has been carried into effect, the money paid or goods delivered under it may be recovered. “But if he waits till the illegal purpose is carried out, or if he seeks to enforce the illegal transaction, in neither case can he maintain an action.” In that case,<sup>474</sup> a debtor executed a transfer to deceive his creditors, but before any creditor could be deceived, he repented and sought to recover back the property, which he was allowed to do. It seems that the repentance of the debtor was due to the failure of his design. After executing the transfer he had summoned a meeting of his creditors to effect a compromise, but the creditors did not turn up. In subsequent cases the principle of *locus poenitentiae* has been confined to cases where the repentance is not due to the failure of the illegal object, but occurs much before any attempt is made to carry out the illegality.<sup>475</sup> This seems to emerge from *Bigos v Bowsted*<sup>476</sup> where the court did not allow certain share certificates to be recovered which were delivered as a security under an agreement to exchange privately the English currency with Italian, one party having backed out. PRITCHARED J stated the effect of the authorities in the following words: “The defendant and the plaintiff were *in pari delicto*, which means that they were equally guilty. The law is that the court will help a person who repents, provided his repentance comes before the illegal purpose has been substantially performed.”

The learned judge then pointed out that the present case showed frustration, not repentance.

Where money is paid to a person to induce him to commit a crime, can it be recovered before he does anything to commit the crime? In such cases, the answer will depend upon the degree of criminality. It is suggested in Anson:

472. *Ashmore, Benson, Pease & Co Ltd v A.V. Dawson Ltd*, (1973) 1 WLR 828; *Jagamath Tewari v Gopal Prasad*, (1983) 31 BLJR 17 (Pat), where rent paid over and above controlled rent with full knowledge could not be recovered back.

473. *Kotharaju Narayana Rao v Tekumalla Ramachandra Rao*, AIR 1959 AP 370.

474. MELLISH LJ in *Taylor v Bowers*, (1876) LR 1 QBD 291, 300. See also *Shanta Agarwal v Baldota Bros*, 1971 SCC OnLine Bom 134. Black money allowed to be recovered.

475. See *Kearley v Thomson*, (1890) LR 24 QBD 742 (CA).

476. (1951) 1 All ER 92. An illegality cannot be waived by private agreement, *Warman Srinivas Kim v Ratilal*, AIR 1959 SC 689: 1959 Supp (2) SCR 217.

"It seems highly unlikely that the court will allow any *locus poenitentiae* at all in the most serious cases of moral reprehensibility, as for example, where money is paid to another to commit murder."<sup>477</sup>

The parties' conduct and relative moral capability could be relevant in determining whether, as a matter of public policy, the court would take notice of the illegality. On the facts of the case the court disregarded the plaintiff's illegality because he had an unanswerable claim against the defendant for fraudulent misrepresentation and because the defendant's own moral culpability greatly outweighed that of the plaintiff's.<sup>478</sup>

Where a father transferred some of his shares to his son without receiving any price, for the purpose of defeating his creditors, and the son refused to return the shares to the father, the father was allowed recovery. The court said that one of the major exceptions to the *pari delicto* rule arises where the transferor repents before the transaction is carried into effect. In this case, the illegal purpose was to defraud the creditors but no creditor could be defrauded. Accordingly, it was not too late for the father to change his mind and recover the shares from his son.<sup>479</sup>

## 2. Parties not "in pari delicto"

It is settled law that where the parties are not *in pari delicto* the less guilty may be able to recover money paid, or property transferred, under the contract. This possibility may arise in three situations:

First, the contract may be of a kind made illegal by a statute in the interest of a particular class of persons of whom the plaintiff is one.

Secondly, the plaintiff must have been induced to enter into the contract by fraud or strong pressure.

Thirdly, there is some authority for the view that a person who is under a fiduciary duty to the plaintiff will not be allowed to retain property, or to refuse to account for money received, on the grounds of an illegal transaction.<sup>480</sup>

One illustration is the decision of the Privy Council in *Mistry Amar Singh v Kulubya*.<sup>481</sup> Certain land was given to a non-African under a lease in violation of a law for the protection of Africans in Uganda. The action was by the African party for recovery of rent and possession. The other party pleaded illegality. Allowing the action, their Lordships quoted the following passage from the judgment of Lord MANSFIELD in *Browning v Morris*:<sup>482</sup>

But where contracts or transactions are prohibited by positive statutes for the sake of protecting one set of men from another set of men, the one, from their situation and condition, being liable to be oppressed or

477. LAW OF CONTRACT (23rd Edn by Guest, 1972) 359.

478. *Saunders v Edwards*, (1987) 1 WLR 1116 (CA).

479. *Tribe v Tribe*, 1996 Ch 107 (CA).

480. See *Fakir Chand Seth v Dambarudhar Bania*, AIR 1987 Ori 50.

481. 1964 AC 142 (PC).

482. (1778) 2 Coup 790, 791.



imposed upon by the other; there, the parties are not *in pari delicto*; and in furtherance of those statutes, the person injured may bring his action and defeat the contract.

Where one of the parties was induced by a fraud to make payments under a contract, which, unknown to him was of champertous nature,<sup>483</sup> and where an agent of an insurance company fraudulently induced a woman to take out an illegal insurance,<sup>484</sup> in either case the payments were allowed to be recovered back. The result would have been otherwise if no fraud was involved.<sup>485</sup> Where payment was made in advance for purchasing a paddy crop not knowing that a control order was being violated, it was allowed to be recovered.<sup>486</sup> Where additional payment was made to a creditor to induce him to accept a scheme of compromise because his acceptance would have influenced the other creditors, the debtor was allowed to recover back the same. The court said:<sup>487</sup> "It is said that both parties are *in pari delicto*. It is true that both are *in delicto*, because the act is a fraud upon the other creditors, but is not *par delictum*, because, one has the power to dictate, the other no alternative, but to submit."

Payments obtained by a person in breach of his fiduciary duty can also be recovered back even if the transaction involved illegality. Thus, a lawyer would be bound to refund the money obtained by him from his client under a champertous agreement.<sup>488</sup> In an export transaction, the goods were falsely invoiced to enable the buyer to evade import tax. The consignment was stolen. The insurer's attempt to escape liability because of the illegality involved did not succeed. There was no deception towards the insurer, nor was the insurance claim based upon the illegal contract.<sup>489</sup>

The Supreme Court refused to interfere in a matter of rent fixation because it was found that whatever rent the parties were paying and accepting was the result of their voluntary understanding. "There is no element of compulsion or exploitation and both parties have by consensus contravened the provisions of law for their mutual advantage."<sup>490</sup>

#### *Cause of action under void contract*

A party to a void contract is entitled to file a suit for its enforcement and in the alternative to pray for refund of money paid under the contract. It cannot be said that the plaint under such a contract does not disclose a cause of action or that it should be rejected or not entertained. The court

483. *Reynell v Sprye*, (1852) 1 De G M&G 660: 42 ER 710.

484. *Hughes v Liverpool Victoria Legal Friendly Society*, (1916) 2 KB 482.

485. *Harse v Pearl Life Assurance Co*, (1904) 1 KB 558.

486. *Fakir Chand Seth v Dambarudhar Bania*, AIR 1987 Ori 50.

487. *Alkinson v Denby*, (1861) 6 H&N 778; affirmed *Atkinson v Denby*, (1862) 7 H&N 934: 158 ER 749.

488. *Helsby, re*, (1894) 1 QB 742.

489. *Euro-Diam Ltd v Bathurst*, (1988) 2 WLR 517 (CA).

490. *Budhwanti v Gulab Chand Prasad*, (1987) 2 SCC 153: AIR 1987 SC 1484, *per* NATRAJAN J.

has to decide to what extent and for what reason the contract is void. There can be decision on voidness or illegality only after taking the suit on record.<sup>491</sup>

### 3. Where recovery possible without relying on illegal contract

Transactions arising out of an agreement to do an illegal act, if they are such that when taken separately from the illegal act, they would be valid, they would remain valid and enforceable notwithstanding the illegality of the agreement.<sup>492</sup> In *Mistry Amar Singh v Kulubya*<sup>493</sup> where the action was to recover possession of property leased out in violation of a statute, their Lordships of the Privy Council observed: "He would have presented his claim without being under any necessity of setting up the unlawful agreements in his plaint. He required no aid from the illegal transaction in order to establish his case. It was sufficient for him to show that he was the registered proprietor of the plots of land and that the defendant was in occupation, without possessing the consent in writing of the Governor for such occupation, and, accordingly, the defendant had no right to occupy."

Similarly, machine tools delivered under an illegal sale were allowed to be recovered.<sup>494</sup> The Court of Appeal laid down that a man's right to his property will be enforced as against a person in possession even if he obtained possession under an unlawful agreement. The Supreme Court of India applied this principle in *Surasaibalini Debi v Phanindra Mohan Mazumdar*.<sup>495</sup> The court allowed a person to recover possession of his property and business, which he had made over to his brother-in-law for evasion of taxes. In a case before the Privy Council on appeal from Malaya:<sup>496</sup>

The plaintiff purchased a lorry from the defendant and operated it on his own account. But it had to be registered in the defendant's name because only he had a haulage licence in respect of it. The defendant snatched the lorry from the plaintiff without the latter's consent and the plaintiff sued him to recover back his possession.

The action was allowed. Lord DENNING said: "Although the transaction between the plaintiff and the defendant was illegal, nevertheless it was fully executed and carried out; and on that account it was effective to pass the

491. *Govind Goverdhanas Daga v Field Mining & Ispat Ltd*, (2009) 6 Mah LJ 398.

492. *BOI Finance Ltd v Custodian*, (1997) 10 SCC 488; AIR 1997 SC 1952.

493. 1964 AC 142 (PC).

494. *Bouwmakers Ltd v Barnet Instruments Ltd*, 1945 KB 65 (CA).

495. AIR 1965 SC 1364; (1965) 1 SCR 861. *Saudagar Chaudhary v Bipati*, AIR 1986 Pat 211, recovery allowed without bringing in the unlawful agreement. *Ghanshyambhai Dattaram v Babubhai Shankarlal*, 1984 GLH 247, allowed a landlord to sue for eviction of a tenant who entered premises by paying additional consideration in violation of an Act. *Tinsley v Milligan* (1994) 1 AC 340 (HL), held by a majority that where a property is transferred by one person to another in pursuance of an unlawful purpose, the transferor can recover back the property under the doctrine of resulting trust and without having to rely on the transaction which is illegal.

496. *Singh v Ali*, 1960 AC 167 (PC).

property in the lorry to the plaintiff. There are many cases which show that when two persons agree together in a conspiracy to effect a fraudulent or illegal purpose—and one of them transfers the property to the other in pursuance of the conspiracy—then, as soon as the contract is executed and the fraudulent or illegal purpose is achieved, the property which has been transferred by one to the other remains vested in the transferee, notwithstanding its illegal origin. The reason is that the transferor, having fully achieved his unworthy end, cannot be allowed to turn round and repudiate the means by which he did it—he cannot throw over the transfer. And the transferee, having obtained the property, can assert his title to it against all the world, not because he has any merit of his own, but because there is no one who can assert a better title to it. The court does not confiscate property because of illegality—it has no power to do so.”

When a contract is repudiated on account of its illegality, the innocent party may recover compensation “proportionate to the amount of work done”. In *Clay v Yates*,<sup>497</sup> a book having been printed, the printer refused to print the dedication because it was libellous, it was held that the painter could recover on *quantum meruit* basis for the work done by him.

#### 4. Collateral transactions

The only material difference between an illegal and void agreement relates to their effect upon the collateral transactions. A collateral transaction means a transaction subsidiary to the main transaction. For example, where money is given to a person to enable him to pay a wagering debt, the wager is the main transaction and the loan is subsidiary to it. If the main transaction is illegal, for example, smuggling, a collateral transaction like money given to enable a person to smuggle, will also be tainted with the same illegality and the money will be irrecoverable.<sup>498</sup> But if the main transaction is only void, its collateral transaction will remain enforceable. Thus, in *Gherulal Parakh v Mahadeodas*,<sup>499</sup> the Supreme Court allowed a partner to recover from his co-partner his proportionate indemnity for losses suffered by him in entering into wagering transactions on behalf of the firm, wagering being only void.

The Supreme Court has also emphasised that a landlord and his tenant cannot be regarded as on par in all respects and, therefore, where the tenant had to pay Rs 2000 to the landlord to secure possession, in contravention of the Rent Act, the landlord's assurance that the amount would be adjusted towards rent was binding on him.<sup>500</sup> The court, however, took care to point out that the doctrine of *in pari delicto* would not be attracted when

497. (1856) 1 H&N 73: 156 ER 1123.

498. See *C.H.T. Ltd v Ward*, (1965) 2 QB 63: (1963) 3 WLR 1071 (CA), money lent for betting was held to be irrecoverable, *Chandra Sreenivasa Rao v Korapatti Raja Rama Mohana Rao*, AIR 1952 Mad 579, money given for an illegal marriage, not recoverable.

499. AIR 1959 SC 781: (1959) 2 SCR 406.

500. *Mohd Salimuddin v Misri Lal*, (1986) 2 SCC 378: AIR 1986 SC 1019.

there is no element of compulsion or exploitation and both parties have by consensus contravened the provisions of law for their mutual advantage. Following this, the Supreme Court did not allow adjustment for an amount which the tenant had been paying in addition to the standard rent. There was no evidence of any compulsion.<sup>501</sup>

## 5. Severance

Where an agreement is only partly illegal, the court will enforce the part which is not illegal provided that it is severable from the rest of the agreement. Where a partnership was created in a truck alongwith a route permit which amounted to a part sale of both, the court held that the whole agreement was vitiated, although it was only the sale of permit which was illegal but that was not severable from the rest of the agreement.<sup>502</sup> A contract to provide money to a person to enable him to establish his share in an estate in return for a promise to pay back the money, and also a share in the amount that would be recovered from the estate, has been held by the Supreme Court to be a composite contract for one consideration making the two types of payment not severable.<sup>503</sup>

In many cases of contracts relating to trade or legal proceedings the courts knock out the objectionable clause of the agreement and allow the rest to be enforced. For example, Section 27 says that the agreement shall be void to that extent, *i.e.* to the extent of unreasonable restraint. In *Nordenfelt v Maxim Nordenfelt Guns & Ammunition Co*<sup>504</sup> that part of the contract was held to be not binding which imposed unreasonable restraint. Similarly, in two cases<sup>505</sup> relating to separation deeds between a husband and wife which imposed restraint upon legal proceedings, the Court of Appeal struck out the restraining part.

Applying these principles to the facts, the Court of Appeal held that the wife's covenant not to sue was the only consideration she gave for the husband's promise of annuity, the whole of the agreement became void.

Where the contract is severable, it would make no difference that the parties had knowledge of the fact that their contract contained an illegal element.

A house was leased out on rent subject to the condition that the lessee, in addition to paying the controlled rent, would also purchase certain chattels from the lessor for an agreed price. The price, being much more than the natural value of the goods, the transaction in essence amounted to paying a premium for the possession of the house. The lessee occupied the premises but offered to pay only the natural price of the goods.

501. *Budhwanti v Gulab Chand Prasad*, (1987) 2 SCC 153: AIR 1987 SC 1484.

502. *Ghulam Ahmed v Mohd Iqbal*, AIR 1970 J&K 165.

503. *Rattan Chand Hira Chand v Askar Nawaz Jung*, (1991) 3 SCC 67.

504. 1894 AC 535.

505. *Goodinson v Goodinson*, (1954) 2 QB 118 (CA).

The lessor sought eviction on the ground that the whole agreement was unlawful. The court did not agree with him. The arrangement had two aspects, namely, the agreement of lease and the promise to pay a premium. The latter part was unlawful and it being severable from the rest, the lease was valid.<sup>506</sup>

In another case,<sup>507</sup> a husband promised to his wife separate maintenance, she agreeing on her part not to sue him as long as he paid, nor to sue for divorce even if he lived in adultery. The husband defaulted with the payments and contended, as against the wife's action, that, owing to the exoneration for adultery, the whole agreement was unlawful. The court allowed the wife's action saying that only that clause of the agreement was unlawful by which the husband had bought his freedom from the consequences of adultery.<sup>508</sup>

To secure the performance of a contract for purchase of shares, a guarantee and mortgage were provided by way of additional security. They turned out to be illegal. Since they were collateral and, therefore, severable, the main transaction remained enforceable.<sup>509</sup>

506. *Ailion v Spickermann*, (1976) 2 WLR 556.

507. *Goodinson v Goodinson*, (1954) 2 QB 118 (CA).

508. See also *Bennet v Bennet*, (1952) 1 KB 249 (CA).

509. *Carney v Herbert*, 1985 AC 301: (1984) 3 WLR 1303 (PC). *BOI Finance Ltd v Custodian*, (1997) 10 SCC 488: AIR 1997 SC 1952, notified persons under the Special Court (Trial of Offences Relating to Transactions in Securities) Act, 1992, a transaction for transfer of shares, falling partly within the category of transfer by notified persons, rest of the transaction being severable was valid.

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The following cases from this chapter are available through EBC Explorer™:

- *BOI Finance Ltd v Custodian*, (1997) 10 SCC 488
- *Central Inland Water Transport Corpn v Brojo Nath Ganguly*, (1986) 3 SCC 156
- *DTC v Mazdoor Congress*, 1991 Supp (1) SCC 600
- *Fakir Chand Seth v Dambarudhar Bania*, AIR 1987 Ori 50
- *Gherulal Parakh v Mahadeodas*, AIR 1959 SC 781: (1959) 2 SCR 406
- *Niranjan Shankar Golikari v Century Spg & Mfg Co Ltd*, AIR 1967 SC 1098: (1967) 2 SCR 378



CASE PILOT

# Discharge of Contract

## Modes of discharge

After the formation of a contract, the next stage is reached, namely, the fulfilment of the object the parties had in mind. When the object is fulfilled, the liability of either party under the contract comes to an end. The contract is then said to be discharged. But “performance” is not the only way in which a contract is discharged. A contract may be discharged:

- (1) by Performance; [Ss. 31–67]
- (2) by Impossibility of Performance; [S. 56]
- (3) by Agreement; [Ss. 62–67] and
- (4) by Breach.<sup>1</sup>

## PERFORMANCE OF CONTINGENT CONTRACTS

### Definition

The expression “contingent contracts” is defined in Section 31 of the Contract Act:

**S. 31. “Contingent contract” defined.**—A “contingent contract” is a contract to do or not to do something, if some event, collateral to such contract, does or does not happen.

#### *Illustration*

A contracts to pay B Rs 10,000 if B's house is burnt. This is a contingent contract.

### Conditional contract

It is a sort of a conditional contract and the condition is of uncertain nature. A contract which is subject to a certain or an absolute type of condition cannot be regarded as a contingent contract. A contract, for example, to pay a sum of money on the expiry of a time or on the death of a person is not a contingent contract because these events are of a certain nature. The time or the person in question will definitely expire and the money will become

1. Ss. 39 and 73. Expiry of the period of limitation for enforcement of rights and obligations under a contract is not a mode of discharge recognised by the Contract Act. Lapse of time does not put an end to rights and obligations under the contract, *Mahadeo Nathaji Patil v Surjabai Khushalchand Lakkad*, (1994) Mah LJ 1145.

payable. When the condition is of uncertain nature, then only the contract can be regarded as truly contingent. For example, a contract to pay a sum of money on the destruction of a premises by fire, is a contingent contract, for that contingency may or may not happen. From this point of view, all contracts of insurance, are contingent contracts.<sup>2</sup> Ordinarily, therefore, a contingent contract will contemplate a future event. But a contract may also relate to an event which has already happened and the only thing uncertain being that the parties do not know which way it happened.

### Contingency to be collateral to contract

The section emphasises that the contingency contemplated by the contract must be collateral to the contract. It means that a contract has already arisen or a subsisting contract is there, but its performance cannot be demanded unless the contemplated event happens or does not happen. Such a contract has to be distinguished from a proposal which does not result in a contract unless the condition is first fulfilled. For example, an offer to pay a sum of money on the discovery of a missing dog is not a contract at all. It becomes a contract only when the dog is searched out and then it is no more contingent. On the other hand, a contract to pay a sum of money on the loss of a ship is a contingent contract. The contract is already there and is not to arise on loss, but the performance can be demanded only on the loss of the ship. A contract to pay a sum of money in return for some work or labour is also not contingent, no contract exists and no wages can be demanded without performing the work first. In an agreement for sale of land, the condition was that the sale deed would be executed after the seller obtained permission for use of the land as village land. It was held that the contract was not contingent. The agreement matured into a binding contract once permission was obtained. It was specifically enforceable. The suit filed within three years after obtaining permission was not time barred.<sup>3</sup>

A contract to buy land which is under dispute made with a party to the dispute and to become operative if he wins the case, is a contingent contract, its performance being wholly dependent upon the result of the litigation. A contingent contract failed because permission was required (environmental permission) from the authority concerned but was not granted. The necessity of such clearance was clearly anticipated in the contract as a prerequisite to its performance. The Supreme Court held that consequent restoration of the parties to the position in which they were before the contract was

2. *Chandulal Harjivandas v CIT*, AIR 1967 SC 816, 818: (1967) 1 SCR 921, 925. Commission payable on success of litigation, this part was held to be a contingent contract. *N. Peddanna Ogeti Balayya v Kotta V. Srinivasayya Setti Sons*, AIR 1954 SC 26. A contract of life insurance is also a contingent contract. See *Commr of Excess Profits Tax v Ruby General Insurance Co Ltd*, AIR 1957 SC 669. *Parvathamma v Uma*, AIR 2011 Kant 58, a contract for transfer of a fragmented piece of land to be implemented on the repeal of an Act which prevented fragmentation was held to be void because the contingency was of an uncertain nature.

3. *Rojasara Ramjibhai Dahyabhai v Jani Narottamdas Lallubhai*, (1986) 3 SCC 300: AIR 1986 SC 1912.

proper.<sup>4</sup> The court distinguished such failure from impossibility of performance. The failure of a contingent contract is due to non-happening of an anticipated event. Whereas impossibility is due to happening of an unanticipated event.<sup>5</sup> A contract for sale of property was subject to the condition that it would be approved by the seller's labour. No such approval became available. The contract failed. Earnest money directed to be refunded with 18 per cent interest.<sup>6</sup>

A, whose property was attached, contracted to sell the same to B and undertook to apply to the court for the approval of the sale. A did apply to the court in the performance of his undertaking, but the court rejected his application. Thereupon A sold the land to C. B sued him for the land. It was held that the contract of sale to B was a contingent contract, being subject to the approval of the court, and that approval having not been given, the contingency did not happen and hence its performance could not be demanded.<sup>7</sup> A contract to sell a piece of agricultural land which was the subject-matter of the ongoing consolidation proceedings was held to be of contingent nature because nobody could tell beforehand to whom the land might become allotted. It was not enforceable until and unless the consolidation would leave the land in the hands of the seller.<sup>8</sup>

### Contingency depending upon will of a person

A contract will be no less contingent where the happening or non-happening of the contingency depends upon the will of a party. A contract the performance of which depends upon the promisee's marriage is a contingent contract, though his marriage is a contingency exclusively within his control. A situation of this kind was before the Madras High Court in *Secy of State for India v A.J. Arathoon*.<sup>9</sup> The case involved supply of timber to a Government Department. The timber was to be approved by the superintendent of a factory. He did not approve the timber actually supplied. The supplier sued the Government for breach of contract contending that the timber corresponded with its description in the contract and, therefore, it should have been approved. There are two possible approaches to the solution of a problem of this kind. One is to regard the contract as absolute subject only

4. *SAIL v Tycoon Traders*, (2015) 5 SCC 767.

5. *Gian Chand v York Exports Ltd*, (2015) 5 SCC 609; (2015) 3 SCC (Civ) 189.

6. *Nandkishore Lalbhai Mehta v New Era Fabrics (P) Ltd*, (2015) 9 SCC 755; AIR 2015 SC 3796.

7. *Dalsukh M. Pancholi v Guarantee Life and Employment Insurance Co Ltd*, AIR 1947 PC 182.

8. *Tirthanand Singh v Sk Zer Mohammad*, (2001) 2 BLJR 1499 (Pat). *Millenia Realotes (P) Ltd v SJR Infrastructure (P) Ltd*, (2005) 6 Kant LJ 36, contract for sub-lease of allotted site after obtaining permission of the Board, not contingent, enforceable as it is lessor's responsibility to obtain permission or face consequences of breach.

9. ILR (1869-70) 5 Mad 173; *J.P. Builders v A Ramadas Rao*, (2011) 1 SCC 429, contingency depending upon the act of a party (endogenous contingency) or upon happenings independent of the parties (exogenous), contingency linked with a party's conduct cannot be available for invoking impossibility.

to approval, in which case the court should be able to see whether the goods answered their description in the contract and the rejection being arbitrary, it should be set aside. An argument in the support of this approach is that if goods can be rejected arbitrarily at one's own pleasure and sweet-will, then it can as well be said that there is no contract at all. The so-called contract would reduce itself to this that the Government would buy if the Superintendent so likes. This can hardly be described as a contract. Hence, to give some meaning to the contract, it would be necessary to hold that approval should not be arbitrarily refused.

The second possible approach is to regard the contract as contingent. The fact of approval being collateral to the performance of the contract, its performance could not be demanded till such approval. The trial court adopted the first approach. It felt that the Superintendent being himself a party to the contract, his decision could be biased and, therefore, his decision should not be final. But the Madras High Court rejected this approach and followed the other approach of regarding the contract as contingent. The contingency was not fulfilled and hence there was no question of any action for breach.

The position would be different where the goods have already been supplied and the only thing that the contract says is that buyer shall pay when he is in a position to pay. This is not a contingent contract. The liability to pay has already arisen. The making of payment at one's ease was only a personal concession and it would have been an abuse of this concession to prolong the payment for an unreasonable time. Hence, the money was payable within reasonable time.

A contract for sale of goods prescribing the condition that the goods would be inspected before despatch was held to be a firm contract. The import of materials pursuant to such a contract was valid.<sup>10</sup>

### Contingency to be condition precedent

Generally, the condition which is collateral to the performance of a contract is a condition precedent, that is, it has to be satisfied first and then performance can be demanded. It has to be distinguished from a condition subsequent, namely, a condition which has to be satisfied after the formation of the contract. Where, for example, a person applied for shares in a company subject to his being appointed as a cashier in the company, it was held that shares could not be allotted to him without first making him a cashier. On the other hand, where the application for shares was subject to the condition that the applicant would pay nothing until the company paid dividends, the contract was held to be not a contingent contract. A valid contract had arisen already; only the payment under it was deferred to the fulfilment of a condition. Where a person agreed to transfer his vehicle and permit, it was held to be a valid contract and not contingent or incomplete

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10. *Collector of Customs v Rakesh Press*, (1997) 10 SCC 457.

only because permission under the Motor Vehicles Act was necessary. He becomes bound to sign papers for applying for transfer.<sup>11</sup>

Similarly, where a valid contract has arisen but is liable to be defeated on the happening of some subsequent condition, it will not be a contingent contract. Where, for example, certain land is sold subject to a condition of repurchase on the happening of some event, it is not a contingent contract. The Supreme Court has laid down that a contract, stipulating that on the day of the redemption of the mortgaged house by the plaintiff, the defendant would execute a sale deed of the house in favour of the plaintiff, is a typical illustration of a contingent contract within the meaning of Section 31.<sup>12</sup>

A contract for the sale of an unspecified share in property; the sale deed to be executed on actual partition of the property has been held to be not a contingent contract and is, therefore, capable of specific enforcement.<sup>13</sup> In an auction of mining leave, the statutory provision was that bidders should first get approval of the competent authority. A bid was accepted subject to the condition of approval. It was held that the non-approval of the bidder prevented a contract from arising making it not enforceable.<sup>14</sup>

### Where enforcement depends upon happening of an event [S. 32]

**S. 32. Enforcement of contracts contingent on an event happening.**—Contingent contracts to do or not to do anything if an uncertain future event happens, cannot be enforced by law unless and until that event has happened.

If the event becomes impossible, such contracts become void.

#### *Illustrations*

- (a) A makes a contract with B to buy B's horse if A survives C. This contract cannot be enforced by law unless and until C dies in A's lifetime.
- (b) A makes a contract with B to sell a horse to B at a specified price, if C, to whom the horse has been offered, refuses to buy him. The contract cannot be enforced by law unless and until C refuses to buy the horse.
- (c) A contracts to pay B a sum of money when B marries C. C dies without being married to B. The contract becomes void.

The section lays down two basic principles. First, a contract to do an act on the happening of a future uncertain condition cannot be enforced unless and until that event happens.<sup>15</sup> Second, if the happening of that event has become impossible, the contract becomes void. The illustrations appended to the section clarify both the principles. An option to buy shares of a bank if and when the bank is converted into a financial corporation is a contingent

11. *Khawaza Bux v Mirza Mohammad Ismail*, AIR 1984 All 83.

12. *Ramzan v Hussaini*, (1990) 1 SCC 104: AIR 1990 SC 529.

13. *Harbaksh Singh Gill v Ram Rattan*, AIR 1988 P&H 60.

14. *Abhilash Singh v State of U.P.*, 2004 All LJ 557: 2004 AIHC 1456.

15. On the happening of the requisite contingency, specific performance of the contract can be demanded. *Rojasara Ramjibhai Dahyabhai v Jani Narottamdas Lallubhai*, (1986) 3 SCC 300: AIR 1986 SC 1912.

contract of this kind, namely, which is to be performed on the happening of a future uncertain event.<sup>16</sup> A contract for the sale of land with a factory was to be performed only if the labour unions agreed to the sale and further if the change of land use was approved by the appropriate authority. None of these contingencies could be fulfilled because neither there was approval by the labour unions nor by the relevant authority. The contract was accordingly not allowed to be enforced against the seller.<sup>17</sup>

The contract would also not be enforceable where the event does not happen in the way contemplated by the contract. Where a car was insured against loss in transit, the car was damaged without being put in the course of transit, the insurer was held to be not liable.<sup>18</sup> Once the event has happened, the contingent contract ripens into an absolute one.<sup>19</sup>

### When performance depends upon non-happening of an event [S. 33]

**S. 33. Enforcement of contracts contingent on an event not happening.**—Contingent contracts to do or not to do anything if an uncertain future event does not happen, can be enforced when the happening of that event becomes impossible, and not before.

#### *Illustration*

A agrees to pay B a sum of money if a certain ship does not return. The ship is sunk. The contract can be enforced when the ship sinks.

Where the performance of a contract depends upon the non-happening of an event, naturally the parties have to wait till the happening of that event becomes impossible. When such circumstances come to pass that show that the event can no more happen, then only the performance of the contract can be demanded. The illustration appended to that section makes the sense of the section clear. An agreement to sell land provided that the earnest money would be returned in case the land is notified for acquisition. Unknown to the parties, the land was already under notification. The contract became impossible of performance and, therefore, void on declaration under Section 6 of the Land Acquisition Act.<sup>20</sup>

### Events linked with human conduct [S. 34]

**S. 34. When event on which contract is contingent to be deemed impossible, if it is the future conduct of a living person.**—If the future event on which a contract is contingent is the way in which a person will act at an unspecified time, the event shall be considered to become impossible when

16. *Jethalal C. Thakkar v R.N. Kapoor*, AIR 1956 Bom 74.

17. *Nandkishore Lalbhai Mehta v New Era Fabrics (P) Ltd*, (2015) 9 SCC 755: AIR 2015 SC 3796.

18. *V.P. Desa v Union of India*, AIR 1958 MP 297.

19. *N. Peddanna Ogeti Balayya v Kotta V. Srinivasayya Setti Sons*, AIR 1954 SC 26; *Bashir Ahmad v Govt of A.P.*, AIR 1970 SC 1089. Where the contingency was neither pleaded nor put in argument at the trial stage, the same was not allowed to be raised in appeal.

20. *Gian Chand v Gopala*, (1995) 2 SCC 528.

such person does anything which renders it impossible that he should so act within any definite time, or otherwise than under further contingencies.

*Illustration*

A agrees to pay B a sum of money if B marries C. C marries D. The marriage of B to C must now be considered impossible, although it is possible that D may die, and that C may afterwards marry B.

When the event for which the parties are waiting is linked with the future conduct of a person, that is to say, where the contract is enforceable if a certain person is to act in a certain way, the event shall be considered to have become impossible if that person does something which makes it impossible that he should act in that way in any definite time or without further contingencies being fulfilled. For example, in *Frost v Knight*,<sup>21</sup> the defendant promised to marry the plaintiff on the death of his father. While the father was still alive, he married another woman. It was held that it had become impossible that he should marry the plaintiff and she was entitled to sue him for the breach of the contract. Similarly, where a person promised to sell certain land to the plaintiff within a certain time, but sold to another within that time, it was held that the performance had become impossible or was possible only upon the further contingency of the defendant buying back the land in order to perform his contract with the plaintiff.

Where there was a written agreement to buy the benefits of plaintiff's invention if it was approved by the engineer, it was held that there was no concluded contract because the invention was not approved by the engineer.<sup>22</sup>

**S. 35. When contracts become void, which are contingent on happening of specified event within fixed time.**—Contingent contracts to do or not to do anything if a specified uncertain event happens within a fixed time, become void if, at the expiration of the time fixed, such event has not happened, or if, before the time fixed, such event becomes impossible.

**When contracts may be enforced, which are contingent on specified event not happening within fixed time.**—Contingent contracts to do or not to do anything, if a specified uncertain event does not happen within a fixed time, may be enforced by law when the time fixed has expired and such event has not happened, or, before the time fixed has expired, if it becomes certain that such event will not happen.

*Illustrations*

- (a) A promises to pay B a sum of money if a certain ship returns within a year. The contract may be enforced if the ship returns within the year, and becomes void if the ship is burnt within the year.
- (b) A promises to pay B a sum of money if a certain ship does not return within a year. The contract may be enforced if the ship does not return within the year, or is burnt within the year.

21. (1872) LR 7 Exch 111.

22. *Pym v Campbell*, (1856) 6 El&Bl 370: 119 ER 903.

**S. 36. Agreements contingent on impossible events, void.**—Contingent agreements to do or not to do anything, if an impossible event happens, are void, whether the impossibility of the event is known or not to the parties to the agreement at the time when it is made.

*Illustrations*

- (a) A agrees to pay B 1000 rupees if two straight lines should enclose a space. The agreement is void.
- (b) A agrees to pay B 1000 rupees if B will marry A's daughter C. C was dead at the time of the agreement. The agreement is void.

These provisions are self explanatory.

## PERFORMANCE OF CONTRACTS

Section 37 says that “the parties to a contract must either perform or offer to perform, their respective promises....” Thus, each party is bound to perform his obligation under the contract, unless the performance is dispensed with or excused under the provisions of the Contract Act, or of any other law.<sup>23</sup> Section 37 which lays down the obligation to perform proceeds as follows:

**S. 37. Obligation of parties to contracts.**—The parties to a contract must either perform, or offer to perform their respective promises, unless such performance is dispensed with or excused under the provisions of this Act, or of any other law.

Promises bind the representative of the promisors in case of the death of such promisors before performance, unless a contrary intention appears from the contract.

*Illustrations*

- (a) A promises to deliver goods to B on a certain day on payment of Rs 1000. A died before that day. A's representatives are bound to deliver the goods to B, and B is bound to pay Rs 1000 to A's representatives.
- (b) A promises to paint a picture for B by a certain day, at a certain price. A dies before the day. The contract cannot be enforced either by A's representatives or by B.

### *Obligation of parties to perform*

The buyer of property retained some money so as to compel the seller to perform certain obligations, like evicting tenants and handing over vacant possession. The relevant document revealed the transaction to be a sale with *consensus ad idem*. The court said that non-payment of a part of the sale consideration could not give a cut at the very root of the contract, since it

23. S. 37. Performance may be dispensed with, for example, by agreement [S. 62] or it may be excused under S. 56 by supervening impossibility of performance. *Syndicate Bank v. R. Veeranna*, (2003) 2 SCC 15; (2003) 5 Kant LJ 1, the bank had the right under the agreement to vary interest upwards up to a certain percentage. The exercise of this power did not require that the borrower should have been put on notice.

was a concluded contract.<sup>24</sup> An agreement was signed by the parties and fully acted upon without the need for executing any further documents. The agreement was described at its foot as a preliminary and tentative draft for discussion purposes only. It was held to be a complete agreement entitling the claimant to relief.<sup>25</sup>

### *Submission of tender is proposal*

When a tender is submitted in response to an invitation it is a proposal and not a contract. It requires to be accepted. The validity period of the tender as specified in the tender itself was four months. Naturally no acceptance could be made after expiry of such period. The forfeiture of the security deposit amount by accepting the tender after validity period and failure of performance by tenderer was not proper.<sup>26</sup>

### **Promises bind representatives**

The proviso to the section says that a promise binds the representatives of the promisors in case of his death, unless a contrary intention appears from the contract. The Cuttack High Court came to the conclusion that this principle would apply even if the promisor has left behind no legal heir. The court said: "If the contract is legal, and enforceable, then even if one of the parties to the contract dies leaving no heir, the persons, who acquired interest over the subject-matter of the contract through that deceased party would be bound by the contract and specific performance can be enforced against such persons." However, this legal proposition in no way helped the appellant as she had failed to establish existence of the alleged agreement.<sup>27</sup>

### **Clause for renewal**

A contract contained a clause for renewal. The party having the right to do so under the contract, invoked the renewal clause. The other party

24. *M. Kamalakannan v M. Manikanndan*, (2011) 4 CTC 139, the court ordered specific performance.

25. *Geo-Group Communications Inc v IOL Broadband Ltd*, (2010) 1 SCC 562; *Govind Prasad Dalmia v W.B. SEB*, 2014 SCC OnLine Cal 22090: AIR 2015 NOC 1084 (Cal), supplies on agreed rates, no evidence to show that the other party accepted supplies at escalated rates. Supplier delayed deliveries because of expectation that escalated prices would be paid. Agreed penalty amount charged and not damages for breach, deduction from bills held to be proper. *SBI v Lalsangbera*, AIR 2015 Gau 67, the bank had the right under the loan agreement to publish the names of defaulting buyers. The court said that this did not include the right to publish photograph of the defaulter also. Photograph was capable of doing greater damage.

26. *Great Eastern Energy Corp Ltd v Jain Irrigation Systems Ltd*, (2010) 4 Mah LJ 759.

27. *Basanti Bai v Prafulla Kumar Routrai*, (2006) 101 Cut LT 686 (Ori); *United India Insurance Co Ltd v Kiran Combers & Spinners*, (2007) 1 SCC 368: AIR 2007 SC 393, the insurer having certified that the insured building was a first class construction, it was held that it could not be given the benefit of any structural defect not noticed by it. *Kunwar Singh Rawat v State of Uttarakhand*, AIR 2007 NOC 1789 (Utt). Government contract for construction of class rooms, construction completed, before the balance amount could be paid, the school building became damaged Inquiry report revealed that the damage was due to rains and landslide and not due to poor construction, the contractor was allowed to recover the balance amount.

refused to accept renewal. The Supreme Court said that the best course for the party was to get the right of renewal declared and enforced by a court of law or to get a declaration that the agreement stood renewed as contemplated by the renewal clause.<sup>28</sup>

### Offer of performance [S. 38]

The promisor, must offer to perform his obligation under the contract to the promisee. This offer is called “tender of performance”.<sup>29</sup> It is then for the promisee to accept the performance. If he does not accept, “the promisor is not responsible for non-performance, nor does he thereby lose his rights under the contract”. In other words, the tender of performance, if rejected by the other party, excuses the promisor from further performance and entitles him to sue the promisee for breach of the contract. Thus, a tender of performance is equivalent to performance. This is the effect of Section 38.

**S. 38. Effect of refusal to accept offer of performance.**—Where a promisor has made an offer of performance to the promisee, and the offer has not been accepted, the promisor is not responsible for non-performance, nor does he thereby lose his rights under the contract.

Every such offer must fulfil the following conditions—

- (1) it must be unconditional;
- (2) it must be made at a proper time and place, and under such circumstances that the person to whom it is made may have a reasonable opportunity of ascertaining that the person by whom it is made is able and willing there and then to do the whole of what he is bound by his promise to do;
- (3) if the offer is an offer to deliver anything to the promisee, the promisee must have a reasonable opportunity of seeing that the thing offered is the thing which the promisor is bound by his promise to deliver.

An offer to one of several joint promisees has the same legal consequences as an offer to all of them.

28. *Hardesh Ores (P) Ltd v Hede & Co*, (2007) 5 SCC 614.

29. A party who promised to sell property on obtaining permission from Income Tax Authorities was not excused from offering performance by saying that he could not manage the clearance certificate. The contract remained alive and enforceable. The buyer had been put in possession of a part of the premises. The seller could not be allowed to take advantage of his own wrong. *Raghunath Rai v Jogeshwar Prashad Sharma*, AIR 1999 Del 383. *Travancore Rubber & Tea Co Ltd v CIT*, (2000) 3 SCC 715: AIR 2000 SC 1980, the obligation of the parties to perform continues till the contract is determined according to its terms; *Jai Durga Finvest (P) Ltd v State of Haryana*, (2004) 3 SCC 381: AIR 2004 SC 1484, the contract under the mining lease could not be performed because of certain acts and omissions on the part of the Government; forfeiture of security money not allowed. *Food Corporation of India v Surana Commercial Co*, (2003) 8 SCC 636, where the obligation of the contracting party was for conversion of *arhar*, whole pulse into *dal* and the work was completed and accepted by the other party, the obligation of the contractor came to an end. *United India Insurance Co Ltd v Pushpalaya Printers*, (2004) 3 SCC 694: AIR 2004 SC 1700, insurance cover against damage to building by “impact” among other things, damage caused by a close-by passing bulldozer without actually touching the building, held, it was damage by impact.

*Illustration*

*A* contracts to deliver to *B* at his warehouse, on the 1st March, 1873, 100 bales of cotton of a particular quality. In order to make an offer of performance with the effect stated in this section, *A* must bring the cotton to *B*'s warehouse, on the appointed day, under such circumstances that *B* may have a reasonable opportunity of satisfying himself that the thing offered is cotton of the quality contracted for, and that there are 100 bales.

The tender of performance, in order to have its effect, must fulfil the following conditions:

*1. Tender of performance must be unconditional [S. 38(1)]*

The tender of performance must be unconditional. A tender becomes conditional when it is not in accordance with the terms of the contract. For example, a tender of an amount less than what is due under the contract is not an effective tender.<sup>30</sup>

*2. The tender of performance must be made at proper time and place, and under such circumstances that the person to whom it is made may have a reasonable opportunity of ascertaining that the person by whom it is made is able and willing there and then to do the whole of what he is bound by his promise to do*

Often the time and place of performance are fixed by the parties in their contract. The tender of performance must be made within the time and at the place so fixed. If it is so made, the promisor is under no further responsibility,<sup>31</sup> if the tender is not accepted. This was established as early as 1843 in *Startup v Macdonald*.<sup>32</sup>

The defendant bought of the plaintiff ten tons of linseed oil to be delivered within the last 14 days of the month of March. The plaintiff tendered on the last of the fourteen days at 9 o'clock at night. The defendant refused to accept owing to the lateness of the hour.

He was held liable for the breach as the jury found that, though the hour was unreasonable, yet there was time for the defendant to have taken in and weighed the goods before midnight. He should, therefore, have accepted the tender and "then no doubt, the contract would have been literally performed".

Where in an international trade contract, the agreement was that payment should reach on the 14th of the month, the court held that before

30. *Haji Abdul Rahman v Haji Noor Mahomed*, ILR (1892) 16 Bom 141; where the highest figure ascertained through tenders was found to be low and, therefore, a meeting of all the tenderers was called so as to give them an opportunity of revising their figures, the acceptance of the best figure thus obtained was held to be not arbitrary. *Food Corporation of India v Kamdhenu Cattle Feed Industries*, (1993) 1 SCC 71: AIR 1993 SC 1601.

31. See *P.L.S.A.R.S. Arunchelam Chetty v Krishna Iyer*, AIR 1925 Mad 1168: 90 IC 481.

32. (1843) 64 RR 810: 12 L.J. Ex 477: (1843) 6 Man & G 693.

repudiating the contract the defendant should have waited up to midnight of the 14th.<sup>33</sup>

Further, the tender must be made under such circumstances that the other party gets a reasonable opportunity of ascertaining whether the person making the tender is able and willing to fulfil the whole of his obligation under the contract. If the tenderer has to deliver something to the promisee, the latter must have a reasonable opportunity of seeing that the thing offered is the thing which the promisor is bound by his promise to deliver. In other words, the goods tendered must be of the contract description, otherwise the tender is not valid.<sup>34</sup> If there are several joint promisees, it is not necessary for the promisor to offer performance to every one of them. A tender made to any one of them has the same legal consequences as a tender to all of them.<sup>35</sup>

In the case of an obligation to pay a debt, the mere fact that the payment was tendered and refused does not discharge the debtor from his liability to pay the debt.<sup>36</sup> This principle of old standing has been indorsed by the Supreme Court in a case<sup>37</sup> where the debtor had the right on paying back his loan to recover vacant possession of his premises, and his tender having been refused, the court held that he was not discharged from his obligation to pay before he could recover his possession.

#### *Obligation to return security documents on payment*

A loan transaction was brought to an end by repayment. It then becomes the duty of the lender to return the security documents. He was not allowed to retain them on the ground that some litigation was pending between the parties.<sup>38</sup>

#### *Obligation to return security money on rejection of bid*

Where a bid was rejected after an unreasonable period of two years and only then the security deposit was refunded, the court directed payment of interest at 12 per cent p.a.<sup>39</sup>

#### By whom contracts must be performed [S. 40]

**S. 40. Person by whom promise is to be performed.**—If it appears from the nature of the case that it was the intention of the parties to any contract that any promise contained in it should be performed by the promisor himself, such

33. *Afovos Shipping Co v R. Pagnan*, (1982) 1 WLR 842; (1982) 1 Lloyd's Rep 562 (CA).

34. See *Carlos Federspil & Co v Charles*, 1957 Lloyd's Rep 230; *ONGC Ltd v Assn of Natural Gas Consuming Industries*, (2004) 5 SCC 253: AIR 2004 SC 2327, ONGC increased its supply price, GAIL had to demand more from consumers, held justified. On accumulated arrears simple interest was allowed.

35. S. 38, last para. See *Alcon Constructions v Board of Trustees*, AIR 1982 Goa 9.

36. *Dixon v Clark*, 136 ER 919: (1847) 16 LJ CP 237.

37. *Vidya Vati v Devi Das*, (1977) 1 SCC 293: AIR 1977 SC 397.

38. *Eco Ceramics v Karnataka State Financial Corpn*, AIR 2001 Kant 167: (2001) 4 Kant LJ 463.

39. *Shanker Lal v State of Rajasthan*, AIHC 2548 (Raj).

promise must be performed by the promisor. In other cases, the promisor or his representative may employ a competent person to perform it.

*Illustrations*

- (a) A promises to pay B a sum of money. A may perform this promise, either by personally paying the money to B, or by causing it to be paid to B by another; and if A dies before the time appointed for payment, his representatives must perform the promise, or employ some proper person to do so.
- (b) A promises to paint a picture for B. A must perform this promise personally.

**S. 41. Effect of accepting performance from third person.**—When a promisee accepts performance of the promise from a third person, he cannot afterwards enforce it against the promisor.

If there is something in the contract to show that personal performance was intended, then the contract will have to be performed by the promisor himself. Sometimes the nature of the promise is an indication by itself that the promisor must perform personally. This usually happens in cases where the use of the personal skill of the promisor is involved, for instance, a contract to paint, sing or marry and contracts of technical nature. In such cases the death of the promisor puts an end to the contract. The promise cannot be enforced against his legal representatives, neither can they enforce the promise.

Ordinarily, however, the rule as laid down in Section 37 is that “promises bind the representatives of the promisors in case of the death of such promisors before performance”. Thus, unless a contrary intention appears from the contract, a promise can be enforced against and also by the legal representatives of the seller or the buyer. There is nothing personal in the sale of goods or payment of price.<sup>40</sup>

“There is some English authority to the effect that discharge of a contract by a third person is effectual only if authorised or ratified by the debtor. In India, however, the words of Section 41 of the Contract Act leave no room for doubt that when the appellants have accepted performance of the promise from a third person, they cannot afterwards enforce it against the promisor.”<sup>41</sup>

## PERFORMANCE OF JOINT PROMISES

According to English law, if one of the several joint promisors dies, the rights and liabilities under the contract devolve upon the surviving joint promisors. The representatives of the deceased promisor neither obtain any rights nor assume any liability, unless they are the representatives of the last surviving promisor. This rule may sometimes cause injustice, inasmuch as

40. *Vaman Trimba Joshi v Changi Damodar Shimpi*, ILR (1925) 49 Bom 862. *CITI Bank N.A. v Standard Chartered Bank*, (2004) 1 SCC 12: AIR 2003 SC 4630: (2003) 117 Comp Cas 554, the performance must be of the original contract unless there is proof of its substitution.

41. *Kapurchand Godha v Mir Nawab Himayatalikhan Azamjeh*, AIR 1963 SC 250, 254: (1963) 2 SCR 168.

the creditor loses the security of the solvency of a promisor. Section 42 of the Contract Act, therefore, lays down a different rule:

### Devolvement of liabilities

**S. 42. Devolvement of joint liabilities.**—When two or more persons have made a joint promise, then, unless a contrary intention appears by the contract, all such persons, during their joint lives, and, after the death of any of them, his representatives jointly with the survivor or survivors, and, after the death of the last survivor, the representatives of all jointly, must fulfil the promise.

According to this section joint promisors must, during their joint lives, fulfil the promise. And if any of them dies, his representatives must, jointly with the surviving promisors, fulfil the promise and so on. On the death of the last survivor, the representatives of all of them must fulfil the promise. But this is subject to any private arrangement between the parties. They may expressly or impliedly prescribe a different rule.<sup>42</sup>

Another important aspect of joint promises is codified in Section 43.

### Joint and several

**S. 43. Any one of joint promisors may be compelled to perform.**— When two or more persons make a joint promise, the promisee may, in the absence of express agreement to the contrary, compel any (one or more) of such joint promisors to perform the whole of the promise.

**Each promisor may compel contribution.**—Each of two or more joint promisors may compel every other joint promisor to contribute equally with himself to the performance of the promise, unless a contrary intention appears from the contract.

**Sharing of loss by default in contribution.**—If any one of two or more joint promisors makes default in such contribution, the remaining joint promisors must bear the loss arising from such default in equal shares.

*Explanation.*—Nothing in this section shall prevent a surety from recovering, from his principal, payments made by the surety on behalf of the principal, or entitle the principal to recover anything from the surety on account of payments made by the principal.

### Illustrations

- (a) A, B and C jointly promise to pay D 3000 rupees. D may compel either A or B or C to pay him 3000 rupees.
- (b) A, B and C jointly promise to pay D the sum of 3000 rupees. C is compelled to pay the whole. A is insolvent, but his assets are sufficient to pay one-half of his debts. C is entitled to receive 500 rupees from A's estate, and 1250 rupees from B.

42. *Gannmani Anasuya v Parvatini Amarchand Chowdhary*, (2007) 10 SCC 296; AIR 2007 SC 2380, joint venture, the question of determination of shares, the terms and conditions were not reduced to writing, the conduct of parties, how they dealt with the affairs of business were held to be relevant.

- (c) A, B and C are under a joint promise to pay D 3000 rupees. C is unable to pay anything and A is compelled to pay the whole. A is entitled to receive 1500 rupees from B.
- (d) A, B and C are under a joint promise to pay D 3000 rupees. A and B being only sureties for C. C fails to pay. A and B are compelled to pay the whole sum. They are entitled to recover it from C.

This section lays down three rules:

#### *Any one compellable to perform*

Firstly, when a joint promise is made, and there is no express agreement to the contrary, the promisee may compel any one or more of the joint promisors to perform the whole of the promise.<sup>43</sup> “A, B and C jointly promise to pay D, 3000 rupees. D may compel either A or B or C to pay him 3000 rupees”.<sup>44</sup>

#### *Right of contribution [S. 43 (Para 2)]*

Secondly, a joint promisor who has been compelled to perform the whole of the promise, may require the other joint promisors to make an equal contribution to the performance of the promise, unless a different intention appears from the agreement. A, B and C are under a joint promise to pay D, 3000 rupees. D recovers the whole amount from A. A may require B and C to make equal contributions.

#### *Sharing of deficiency [S. 43 (Para 3)]*

Thirdly, if any one of the promisors makes a default in such contribution, the remaining joint promisors must bear the deficiency in equal shares. A, B and C are under a joint promise to pay D, 3000 rupees. C is unable to pay anything. The deficiency must be shared by A and B equally. If C's estate is able to pay one-half of his share, the balance must be made up by A and B in equal proportions.<sup>45</sup>

The first rule is at variance with the English Common Law. Referring to the English rule as laid down in *R. v Hoare*<sup>46</sup> and *Kendall v Hamilton*<sup>47</sup> STRACHEY CJ of the Allahabad High Court said, as explained in those judgments the doctrine that there is, in the case of a joint contract, a single cause

43. Para 1, S. 43. *Rama Shankar Singh v Shyamla Devi*, AIR 1970 SC 716: (1969) 2 SCR 360; *Mukund Das Raja Bhagwan Das v State Bank of Hyderabad*, (1970) 2 SCC 766: AIR 1971 SC 449.

44. Illustration (a) to S. 43. See *Rama Shankar Singh v Shyamla Devi*, AIR 1970 SC 716: (1969) 2 SCR 360, contribution between lessees. The court cannot say that its judgment should be enforced against one joint promisor in the first instance and against other thereafter. *Mukund Das Raja Bhagwan Das v State Bank of Hyderabad*, (1970) 2 SCC 766: AIR 1971 SC 449. *Hemmo Pharma v Dawood Shoes (P) Ltd*, (2003) 3 Bom CR 781, if one of several persons liable makes payment, it does not give a fresh period of limitation against other persons who were jointly and severally liable with him.

45. See illustration (b) and (c). These provisions as to contribution do not apply to contributions between mortgagors. *Kedar Lal Seal v Hari Lal Seal*, AIR 1952 SC 47: 1952 SCR 179.

46. (1844) 13 M & W 494: 67 RR 664.

47. (1879) LR 4 AC 504 (HL).

of action which can only be once sued on, is essentially based on the right of joint debtors in England to have all their co-contractors joined as defendants in any suit to enforce a joint obligation.”

But Section 43 allows an action to be brought against any one of the joint promisors without impleading the others as defendants. Suppose now that the creditor sues only one joint promisor, can he subsequently sue the others? According to English Law he cannot. What is the position in India? According to STRACHEY CJ there is no such bar in the words of Section 43 and, therefore, a subsequent suit against other promisors should be allowed to proceed.<sup>48</sup> Pollock and Mulla observe: “the reasoning of STRACHEY CJ seems to us conclusive.”<sup>49</sup> But some other High Courts have disallowed such actions.<sup>50</sup>

#### *Release of one joint promisor*

The creditor is also given the right to release anyone of the joint promisors from his liability and this does not discharge the others from their liability. Section 44 is as follows:

**S. 44. Effect of release of one joint promisor.**—Where two or more persons have made a joint promise, a release of one of such joint promisors by the promisee does not discharge the other joint promisor or joint promisors; neither does it free the joint promisor so released from responsibility to the other joint promisor or joint promisors.

This also marks a departure from the English Common Law, according to which a discharge of one joint promisor amounts to a discharge of all, unless the creditor expressly preserves his rights against them.

#### **Joint promisees [S. 45]**

Devolution of joint rights is governed by almost the same kind of principles as the devolution of joint liabilities. When a promise is made to more than one person jointly, the right to claim performance rests with all of them jointly. If anyone of them dies, it rests with his legal representatives jointly, with the survivors and after the death of the last survivor, with the representatives of all jointly. Section 45 is as follows:

**S. 45. Devolution of joint rights.**—When a person has made a promise to two or more persons jointly, then, unless a contrary intention appears from the contract, the right to claim performance rests, as between him and them, with them during their joint lives, and, after the death of any of them, with the

48. *Mohd Askari v Radhe Ram Singh*, ILR (1900) 22 All 307, 311–12.

49. The Indian Contract Act, (1957), p. 311.

50. See, for instance, Calcutta High Court’s decision in *Hemendro Coomar Mullick v Rajendrolall Moonshee*, ILR (1878) 3 Cal 353. See also *Lucknidas Khimji v Purshotam Haridas*, ILR (1882) 6 Bom 700; *Neelratan Mukhopadhyay v Cooch-Behar Loan Officer Ltd*, ILR (1941) 1 Cal 171, where different views have been explained.

representative of such deceased person jointly with the survivor or survivors, and after the death of the last survivor, with the representatives of all jointly.

*Illustration*

A, in consideration of 5000 rupees, lent to him and B and C, promises B and C jointly to repay them that sum with interest on a day specified. B dies. The right to claim performance rests with B's representative jointly with C during C's life, and, after the death of C, with the representatives of B and C jointly.

The Supreme Court has held that where a joint promisee refuses to join as a co-plaintiff, he should be taken on record as pro-forma defendant. The court cannot compel any person to be a plaintiff if he does not want to be so.<sup>51</sup>

The joint promisee and not the legatee under a will was held entitled to the amount payable under a joint term deposit.<sup>52</sup>

*Either or survivor saving account*

The saving account was originally opened by the husband and wife on either or survivor basis. Subsequently this mandate of either or survivor was withdrawn because of strained relations. The husband died. The bank did not allow the wife to operate the account without succession certificate. The court said that there was no illegality in it. If the legal heirs consented on an affidavit to permit their mother to withdraw the amount, the bank should allow it. Banks are supposed to have a human face and also adopt a consumer friendly approach.<sup>53</sup>

Time and place for performance [Ss. 46–50]

**S. 46. Time for performance of promise, where no application is to be made and no time is specified.**—Where, by the contract, a promisor is to perform his promise without application by the promisee, and no time for performance is specified, the engagement must be performed within a reasonable time.

*Explanation.*—The question “what is a reasonable time” is, in each particular case, a question of fact.

**S. 47. Time and place for performance of promise, where time is specified and no application to be made.**—When a promise is to be performed on a certain day, and the promisor has undertaken to perform it without application by the promisee, the promisor may perform it at any time during the usual hours of business on such day and at the place at which the promise ought to be performed.

51. *Jahar Roy v Premji Bhimji Mansata*, (1977) 4 SCC 562; AIR 1977 SC 2439. *Jose v Joseph*, (1993) 2 KLJ 712, devolution on legal representatives of the right to sue.

52. *Abhra Sinha v India Explosives Ltd*, (2003) 2 ICC 157 (Cal).

53. *Shanti Devi v Bhojpur Rohtas Gramin Bank*, AIR 2007 DOC 102 (NCC).

*Illustration*

A promises to deliver goods at B's warehouse on the 1st January. On that day A brings the goods to B's warehouse, but after the usual hour for closing it, and they are not received. A has not performed his promise.

When a promise has to be performed within a certain time, it must be performed on any day before the lapse of that time.<sup>54</sup> Where no time was specified for performance of the promise, the court said that in such cases performance must be offered within reasonable time. The period of three years as prescribed in Article 54 of the Limitation Act, 1963, can be taken as reasonable time.<sup>55</sup>

**S. 48. Application for performance on certain day to be at proper time and place.**—When a promise is to be performed on a certain day, and the promisor has not undertaken to perform it without application by the promisee, it is the duty of the promisee to apply for performance at a proper place and within the usual hours of business.

*Explanation.*—The question “what is a proper time and place” is, in each particular case, a question of fact.

**S. 49. Place for performance of promise, where no application to be made and no place fixed for performance.**—When a promise is to be performed without application by the promisee, and no place is fixed for the performance of it, it is the duty of the promisor to apply to the promisee to appoint a reasonable place for the performance of the promise, and to perform it at such place.

*Illustration*

A undertakes to deliver a thousand maunds of jute to B on a fixed day. A must apply to B to appoint a reasonable place for the purpose of receiving it, and must deliver it to him at such place.

**Debtor to seek his creditor**

The common law rule is that a debtor should seek his creditor and pay him. In keeping with this rule the section imposes a duty on a promiser to apply to his promisee for fixing a reasonable place for performance. Under the Negotiable Instruments Act, 1881, it is the duty of the payee (promisee) to present the instrument for payment.<sup>56</sup>

**S. 50. Performance in manner or at time prescribed or sanctioned by promisee.**—The performance of any promise may be made in any manner, or at any time which the promisee prescribes or sanctions.

*Illustrations*

- (a) B owes A 2000 rupees. A desires B to pay the amount to A's account with C, a banker. B, who also banks with C, orders the amount to be transferred from his account to A's

54. *Saraswat Trading Agency v Union of India*, AIR 2002 Cal 51: (2002) 1 ICC 1038.

55. *Nakubai Valu Dhokane v Bhagwan Singh Prakash Chandra*, (2008) 6 AIR Bom 392: AIR 2009 NOC 385 (Bom).

56. *Jose Paul v Jose*, (2002) 2 KLT 540.

credit, and this is done by C. Afterwards, and before A knows of the transfer, C fails. There has been a good payment by B.

- (b) A and B are mutually indebted. A and B settle an account by setting off one item against another, and B pays A the balance found to be due from him upon such settlement. This amounts to a payment by A and B, respectively, of the sums which they owed to each other.
- (c) A owes B 2000 rupees. B accepts some of A's goods in reduction of the debt. The delivery of the goods operates as a part payment.
- (d) A desires B, who owes him Rs 100, to send him a note for Rs 100 by post. The debt is discharged as soon as B puts into the post a letter containing the note duly addressed to A.

#### *Where no time specified and performance is to be without application*

The first principle as laid down in Section 46 is that where the promisor is to perform without any application by the promisee, and no time for performance is specified, the engagement must be performed within a reasonable time. The explanation to the section says that "what is a reasonable time" is, in each particular case, a question of fact.<sup>57</sup>

Unreasonably long delay cannot be regarded as reasonable. Thus, where a person undertook to discharge the debt of another but no time for payment was fixed, it was held that the offer of payment after three years was too late. That amounted to breach. A contract to keep a ship insured was held to have been broken although there was only a delay of three days. In the case of a ship much can happen in three days. But in a contract of sale of shares two months' time was held to be reasonable for completing it.

#### *Usual business hours*

The second general principle is stated in Section 47. Where the promisor has undertaken to perform without any application from the promisee, but the day of performance is fixed, the promisor may perform the promise during the usual business hours of the day and at the place where such promise ought to be performed. Since only the day of performance is stated but not the place, the promise should be performed at the place where its nature demands, that is, where it ought to be performed. In a promise, for example, to deliver goods at the buyer's warehouse, the tender of performance must be made at that place. The promisor should bring the goods at that place during the usual business hours. If he brings the goods after the business hours and they are not received, it cannot be said that the promise has been performed. When the day on which a promissory note or bill of exchange is at maturity is a public holiday, the instrument shall be deemed to be due on the next preceding business day.<sup>58</sup> But in other cases much depends on the usages of the particular trade. If such usage allows performance on the next succeeding day, it will be quite reasonable to offer performance on that day.

57. The passing of a decree does not wipe out the responsibility of the promisor to offer performance within reasonable time. *Hungersford Investment Trust Ltd v Haridas Mundhra*, (1972) 3 SCC 684: AIR 1972 SC 1826.

58. S. 25 of the Negotiable Instruments Act, 1881.

*Application for performance to be at proper place and time*

The third general principle is to be found in Section 48. Where the day of performance is fixed, but the promisor has not to perform without application from the promisee, it is the duty of the promisee to apply for performance at a proper place and within the usual business hours. The explanation to the section says that “what is a proper time and place” is a question of fact in each case.

*Application for reasonable place of performance*

The fourth general principle is in Section 49. When a promise is to be performed without any application by the promisee, and no place is fixed for performance, it is the duty of the promisor to apply to the promisee to appoint a reasonable place for the performance of the promise, and to perform it at such place. The illustration appended to the section supposes a case in which there is a contract to supply a quantity of jute on a fixed day. The seller must apply to the buyer to appoint a reasonable place for the performance of the promise and then to perform the promise at such a place. A promissory note executed at Bangalore stated that it would be payable at Bangalore or at any place in India. The payee settled in New Delhi and demanded payment at New Delhi. It was held that under Section 49 it was the duty of the debtor to seek his creditor and to pay him there.<sup>59</sup>

*Time and manner of performance, promisee's choice*

The next general principle is stated in Section 50. The section leaves the whole question as to the time and manner of performance upon the choice of the promisee. It says that the performance of any promise may be made in any manner, or at any time which the promisee prescribes or sanctions. The illustrations appended to the section deserve to be noted. If a person owes another a sum of money and the creditor tells him to pay the amount into his account in a bank, which is done; and afterwards, before the creditor comes to know of the fact of payment, the bank fails, so that the creditor does not get the benefit of the payment; even so the debtor is discharged from his liability. Where two persons are mutually indebted and they agree to set off their debts against each other, the balance being paid off by one to the other. Both stand discharged from their respective liability. Where the creditor accepts goods from the debtor in payment, the debtor stands discharged to the extent of the value of the goods. Where the creditor desires the debtor to send the money by post, the debtor will be discharged as soon as he posts a properly addressed and stamped letter containing the money.<sup>60</sup>

59. *L.N. Gupta v Tara Mani*, AIR 1984 Del 49.

60. See *CIT v Ogale Glass Works Ltd*, AIR 1954 SC 429: (1955) 1 SCR 185, a cheque posted as desired by the promisor. See also *Union of India v Radha Kisan Agarwala*, (1969) 1 SCC 225: (1969) 2 SCR 28: AIR 1969 SC 762. The responsibility of posting a dividend warrant is satisfied when the warrant is posted. *H.P. Gupta v Hiralal*, (1970) 1 SCC 437: 1970 SCC (Cri) 190: AIR 1971 SC 206: 1970 SCR 788. Payment may be made by entries in books of account.

## Performance of reciprocal promises [Ss. 51–54]

When a contract consists of an exchange of promises, they are called reciprocal promises. Section 2(f) say that “promises which form the consideration or part of the consideration for each other, are called reciprocal promises.<sup>61</sup> When such promises have to be simultaneously performed, the promisor is not bound to perform unless the promisee is ready and willing to perform his promise. This principle is laid down in Section 51.

**S. 51. Promisor not bound to perform, unless reciprocal promisee ready and willing to perform.**—When a contract consists of reciprocal promises to be simultaneously performed, no promisor need perform his promise unless the promisee is ready and willing to perform his reciprocal promise.

### Illustrations

- (a) A and B contract that A shall deliver goods to B to be paid for by B on delivery.  
A need not deliver the goods, unless B is ready and willing to pay for the goods on delivery.  
B need not pay for the goods, unless A is ready and willing to deliver them on payment.
- (b) A and B contract that A shall deliver goods to B at a price to be paid by instalments, the first instalment to be paid on delivery.  
A need not deliver, unless B is ready and willing to pay the first instalment on delivery.  
B need not pay the first instalment, unless A is ready and willing to deliver the goods on payment of the first instalment.

In a contract, for example, for the sale of goods on payment of price, the seller need not deliver the goods unless the buyer is ready and willing to pay for the goods on delivery. Similarly, the buyer need not pay unless the seller is ready and willing to deliver the goods on payment. If the price is to be paid in instalments and the first instalment is payable on delivery, the seller need not deliver unless the buyer is ready and willing to pay the first instalment and the buyer need not pay the instalment unless the seller is ready and willing to deliver the goods. Certain material was supplied. The terms and conditions of the supply order stated that 90 per cent of the cost of the material was to be paid on delivery and the remaining 10 per cent after a favourable test report about the material was received from the Indian Institute of Packaging. A negative report was received, in the form of a copy as the original was not available. The copy of the report showed tampering. Evidence also showed that testing rules of the Institute were not followed.

*Narayandas Shreeram Somani v Sangli Bank Ltd*, AIR 1966 SC 170: (1965) 3 SCR 777: (1965) 35 Comp Cas 596. *Canara Bank v Vijay Kumar Arora*, AIR 2004 Del 304, encashment of draft by discounting it, discounting bank became owner, loss of the draft in transit could not be loss of original owner. *Panchanan Dhara v Monmatha Nath Maity*, (2006) 5 SCC 340: AIR 2006 SC 2281, the time for performance became extended by conduct of parties. Breach of contract occurred when after such extension of time, the party came to know that the other has refused to perform. The period of limitation started from this event.

61. See *Radhakrishna Sivadutta Rai v Tayeballi Dawoodbhai*, AIR 1962 SC 538: 1962 Supp (1) SCR 81, 96; *Jiwan Lal v Brij Mohan Mehra*, (1972) 2 SCC 757: AIR 1973 SC 559. No separate consideration has to be shown in such cases because such promises constitute the consideration for each other, *Varghese Paul v Narayanan Nair*, (1999) 2 KLT 571.

Hence, it could not be said that the report was negative. The defendant was bound to pay the balance of the price.<sup>62</sup>

There was an agreement for reconstruction of the tenanted premises with the additional feature of providing a toilet. The tenant agreed to pay higher rent on reconstruction. Reconstruction was over but toilet facility was not provided. The Supreme Court held that the tenant was not obliged to pay higher rent though he was put in possession of the reconstructed premises.<sup>63</sup>

### *Order of performance*

The order in which reciprocal promises must be performed may be fixed by the contract and the order so fixed must be followed. But where the order is not expressly fixed, they will have to be performed in the order which the nature of the transaction admits. The relevant provision is Section 52.

**S. 52. Order of performance of reciprocal promises.**—Where the order in which reciprocal promises are to be performed is expressly fixed by the contract, they shall be performed in that order; and where the order is not expressly fixed by the contract, they shall be performed in that order which the nature of the transaction requires.

#### *Illustrations*

- (a) A and B contract that A shall build a house for B at a fixed price. A's promise to build the house must be performed before B's promise to pay for it.
- (b) A and B contract that A shall make over his stock-in-trade to B at a fixed price, and B promises to give security for the payment of the money. A's promise need not be performed until the security is given, for the nature of the transaction requires that A should have security before he delivers up his stock.

In a case before the Allahabad High Court:<sup>64</sup>

The defendant took a lease of land from the Municipality of a town on condition that he pays Rs 630 for levelling charges and possession was to be delivered after levelling. The question arose whether the sum was to be paid before or after the levelling. The agreement was silent on the point.

The court held that “in the ordinary course of business work is not usually paid for before it is done. It is the custom in some cases for payment to be made in instalments as the work progresses but the person for whom work is done is not expected to pay the entire cost in advance without an express agreement to that effect”.

62. *Ajeet International v HP Horticulture Produce Mktg & Processing Corp Ltd*, AIR 2002 HP 159.

63. *Mohammed v Pushpalatha*, (2008) 8 SCC 335.

64. *Hashman v Lucknow Improvement Trust*, (1927) 101 IC 847. See also *K. Abdulkhader v State*, (1993) 2 KLJ 977, failure on the part of the Government to pay for a part of the completed works in accordance with the agreement, delay on the part of the contractor was held to be attributable to that default. *Amarjeet S. Vidhyarthi v Sushiladevi K. Pillani*, (2002) 2 Bom CR 694, agreed payment to be made before claiming to be put in possession.

Section 53 lays down the principle that where one of the parties to reciprocal promises prevents the other from performing his promise, the contract becomes voidable at the option of the party so prevented; and he is entitled to compensation from the other party for any loss which he may sustain in consequence of the non-performance of the contract.

**S. 53. Liability of party preventing event on which contract is to take effect.**—When a contract contains reciprocal promises, and one party to the contract prevents the other from performing his promise, the contract becomes voidable at the option of the party so prevented; and he is entitled to compensation from the other party for any loss which he may sustain in consequence of the non-performance of the contract.

*Illustration*

A and B contract that B shall execute certain work for A for a 1000 rupees, B is ready and willing to execute the work accordingly, but A prevents him from doing so. The contract is voidable at the option of B; and, if he elects to rescind it, he is entitled to recover from A compensation for any loss which he has incurred by its non-performance.

*Liability of party preventing performance*

The same result would follow where the obstruction to performance is caused by the inadequacy of the machinery or material supplied by one of the parties. For example, in a case before the Privy Council,<sup>65</sup> where in order to get his mine cleared of a rock, the defendant had to supply a crusher. The crusher supplied was too inadequate for the job. This was held to be such an obstruction to performance as enabled the contractor to recover his expenses and loss of profits. Similarly, in a case before the Supreme Court,<sup>66</sup> a bidder to whom a coal mine was knocked down was allowed to have refund of his deposit when the coal commissioner refused to permit him to take the coal to U.P., any such restriction being not present in the terms of the auction.

Where the contract was for making a canal and the promisee department had to supply cement, etc., and while the contractor had started digging, the material was not supplied nor he was permitted to purchase in the open market, the working stopped. The department considered this as a breach. The security deposit and earnest money was forfeited. The payment for work already done was withheld. All this was held to be wrong. The amount forfeited and withheld payment were ordered to be released with interest at 9 per cent.<sup>67</sup>

65. *Kleinert v Abosso Gold Mining Co*, (1913) 59 Sol Jo 45, on appeal from the Supreme Court of Gold Coast.

66. *Har Prasad Choubey v Union of India*, (1973) 2 SCC 746: AIR 1973 SC 2380. *Uberoi Mohinder Singh v State of Haryana*, (1991) 2 SCC 362, in a contract for Yamuna quarrying, the contractor was prevented from performing his part because of the failure of the Flood Control Deptt. to give no objection and, therefore, it was held that the contractor was entitled to refund of his deposit money.

67. *Ramachandra Narayan Nayak v Karnataka Nerravari Nigam Ltd*, (2013) 15 SCC 140: (2014) 5 SCC (Civ) 159.

Where the nature of the reciprocal promises is such that one cannot be performed, or its performance cannot be claimed unless the other party performs his promise in the first place, then if the latter fails to perform, he cannot claim performance from the other, but must make compensation to him for his loss. Section 54 incorporates this principle.

**S. 54. Effect of default as to that promise which should be first performed in contract consisting of reciprocal promises.**—When a contract consists of reciprocal promises, such that one of them cannot be performed, or that its performance cannot be claimed till the other has been performed, and the promisor of the promise last mentioned fails to perform it, such promisor cannot claim the performance of the reciprocal promise, and must make compensation to the other party to the contract for any loss which such other party may sustain by the non-performance of the contract.

*Illustrations*

- (a) A hires B's ship to take in and convey, from Calcutta to the Mauritius, a cargo to be provided by A, B receiving a certain freight for its conveyance. A does not provide any cargo for the ship. A cannot claim the performance of B's promise, and must make compensation to B for the loss which B sustains by the non-performance of the contract.
- (b) A contracts with B to execute certain builders' work for a fixed price, B supplying the scaffolding and timber necessary for the work. B refuses to furnish any scaffolding or timber, and the work cannot be executed. A need not execute the work, and B is bound to make compensation to A for any loss caused to him by the non-performance of the contract.
- (c) A contracts with B to deliver to him, at a specified price, certain merchandise on board a ship which cannot arrive for a month, and B engages to pay for the merchandise within a week from the date of the contract. B does not pay within the week. A's promise to deliver need not be performed, and B must make compensation.
- (d) A promises B to sell him one hundred bales of merchandise, to be delivered next day, and B promises A to pay for them within a month. A does not deliver according to his promise. B's promise to pay need not be performed, and A must make compensation.

*Effect of one party's default*

Another illustration is the Supreme Court decision in *Nathulal v Phoolchand*:<sup>68</sup>

The plaintiff was the owner of a ginning factory constructed on agricultural land and nominally held in the name of his brother. He sold the factory to the defendant who paid half the price at once and was put in possession, the balance being payable on a fixed date. The buyer defaulted in paying up on that date and the seller rescinded the contract and brought an action for possession.

68. (1969) 3 SCC 120: AIR 1970 SC 546: (1970) 2 SCR 854. *Vegi Venkateswara Rao v Vegi Venkatarama Rao*, AIR 1998 AP 6, in a suit for specific performance of a reciprocal promise, the party seeking relief has to show that he was ready and willing to do his part of the contract. Following, *Vairavan Chettiar v Kannappa Mudaliar*, AIR 1925 Mad PC 91; *Tan Ab Boon v State of Johore*, AIR 1936 PC 236; *Abdullah Bey Chedid v Tenenbaum*, AIR 1934 PC 91.

SHAH J speaking for himself and HEGDE J held that the nature of the contract required the seller to have had his own name recorded as the owner and have obtained permission from the State Government for transfer of the agricultural land, before he could claim the final payment. If, therefore, under the terms of the contract the obligations of the parties have to be performed in a certain sequence, one of the parties to the contract cannot require compliance with the obligation by the other party without in the first instance performing his own part of the contract which in the sequence of obligations is to be performed by him earlier. So long as Nathulal (seller) did not carry out his part of the contract, Phoolchand could not be called upon to pay the balance of the price.<sup>69</sup>

The offer to perform a reciprocal promise in different terms than contemplated by the contract, for example, an offer of payment before the time fixed, is not valid performance so as to demand performance from the opposite side.<sup>70</sup>

Under a contractual arrangement the plaintiff-respondent was to supply to the other defendant-appellant TV signals and the appellant was to supply them to cable operators after decoding. The appellant informed the supplier that it was discontinuing the service to cable operators because of non-payment by them and that it would also not be able to pay to the supplier. Because of this the supplier stopped sending the signals. The supplier subsequently brought an action for damages for the unexpired period of the agreement which was not used by the appellant. The court said that Section 54 would not help the supplier. He acquiesced in the act of the appellant and stopped sending signals. He had the full right to rescind the contract and bring an action for breach, but he did not adopt this course.<sup>71</sup>

Where the contractor had to submit a bank performance guarantee within a certain time, and only then the other party could be called upon to perform his part of the contract, but he failed to do so and the letter of credit submitted by him was also conditional, it was held that since the other party had not ended the contract, it remained alive for the benefit of both parties. There was no breach and no dispute. This aspect was not referable to arbitration.<sup>72</sup>

Where a cheque issued by the owner of a motor vehicle for payment of premium for its insurance came back dishonoured and the insurer neither

69. *Nathulal v Phoolchand*, (1969) 3 SCC 120: AIR 1970 SC 546: (1970) 2 SCR 854. Followed in *Chandnee Widya Vati Madden v C.L. Katial*, AIR 1964 SC 978: (1964) 2 SCR 495, where also the condition for sale of plots was that the vendor should obtain planning permission from the Government within two months. *Bishambhar Nath Agarwal v Kishan Chand*, AIR 1998 All 195, the seller of land subject to ceiling permission must obtain such permission first before asking for payment.

70. *Vidya Vati v Devi Das*, (1977) 1 SCC 293: AIR 1977 SC 397.

71. *Jabalpur Cable Network (P) Ltd v ESPN Software India (P) Ltd*, AIR 1999 MP 271.

72. *State Trade Corpn of India Ltd v Marpro Ltd, U.K.*, (2000) 86 DLT 361. *Saraswat Trading Agency v Union of India*, AIR 2002 Cal 51: (2002) 1 ICC 1038, the Union of India did not keep its promise of paying an agreed amount within the stipulated time, it could not object to the award being made a rule of the court because the promise involved a reciprocal duty.

cancelled the policy nor sent any information to the owner about the dishonour of his cheque, it was held that the insurer could not deny liability to indemnify the insured for loss caused to the vehicle. The insurer had given no opportunity to the owner to make payment after dishonour of his cheque.<sup>73</sup>

*Promises comprising of legal and illegal parts*

**S. 57. Reciprocal promise to do things legal and also other things illegal.**—Where persons reciprocally promise, firstly to do certain things which are legal, and, secondly, under specified circumstances to do certain other things which are illegal, the first set of promises is a contract, but the second is a void agreement.

*Illustration*

A and B agree that A shall sell B a house for 10,000 rupees, but that, if B uses it as a gambling house, he shall pay 1,50,000 rupees for it.

The first set for reciprocal promises, namely, to sell the house and to pay 10,000 rupees for it, is a contract.

The second set is for an unlawful object, namely, that B may use the house as a gambling house, and is a void agreement.

Section 57 applies to cases where two sets of promises are distinct. When the void part of an agreement can be properly separated from the rest, the latter does not become invalid. The ready-forward transaction consists of two parts. In the ready leg there is a purchase or sale of securities at a stated price which is executed on payment of consideration for spot delivery of the security certificates together with transfer forms. The full and absolute ownership of the title in securities vests in the purchaser, the entire property in the security passing immediately upon such delivery and payment. The seller is divested of all the rights, title and interests in the securities. The forward leg is to be performed at a later date on the stated price being paid. The securities are to be delivered back when the title in interest therein would pass to the original seller.<sup>74</sup>

**S. 58. Alternative promise, one branch being illegal.**—In the case of an alternative promise, one branch of which is legal and the other illegal, the legal branch alone can be enforced.

*Illustration*

A and B agree that A shall pay B 1000 rupees, for which B shall afterwards deliver to A either rice or smuggled opium.

This is a valid contract to deliver rice, and a void agreement as to the opium.<sup>75</sup>

73. *United India Insurance Co Ltd v Abbisetti Venkataraao*, AIR 2008 AP 8. The court distinguished the case from the decision of the Supreme Court in *National Insurance Co Ltd v Seema Malhotra*, (2001) 3 SCC 151: AIR 2001 SC 1197, because here the insurer had informed the owner of the vehicles about the dishonour of his cheque and consequent cancellation of the policy.

74. *BOI Finance Ltd v Custodian*, (1997) 10 SCC 488: AIR 1997 SC 1952.

75. See *BOI Finance Ltd v Custodian*, (1997) 10 SCC 488: AIR 1997 SC 1952, when the void part can be separated from the valid, the latter does not become void.

### TIME FOR PERFORMANCE [S. 55]

Sometimes the parties to a contract specify the time for its performance. Ordinarily it is expected that either party will perform his obligation at the stipulated time. But if one of them fails to do so, the question arises what is the effect upon the contract. Section 55 contains the answer.

**S. 55. Effect of failure to perform at fixed time, in contract in which time is essential.**—When a party to a contract promises to do a certain thing at or before a specified time, or certain things at or before specified times, and fails to do any such thing at or before the specified time, the contract, or so much of it as has not been performed, becomes voidable at the option of the promisee, if the intention of the parties was that time should be of the essence of the contract.

**Effect of such failure when time is not essential.**—If it was not the intention of the parties that time should be of the essence of the contract, the contract does not become voidable by the failure to do such thing at or before the specified time; but the promisee is entitled to compensation from the promisor for any loss occasioned to him by such failure.

**Effect of acceptance of performance at time other than that agreed upon.**—If, in case of a contract voidable on account of the promisor's failure to perform his promise at the time agreed, the promisee accepts performance of such promise at any time other than that agreed, the promisee cannot claim compensation for any loss occasioned by the non-performance of the promise at the time agreed, unless, at the time of such acceptance, he gives notice to the promisor of his intention to do so.

#### Factors which make time of essence

According to this section, if the intention of the parties was that time should be the essence of the contract, then a failure to perform at the agreed time renders the contract voidable at the option of the opposite party. "Time is generally considered to be of the essence of the contract in the following three cases:

- (1) Where the parties have expressly agreed to treat it as of the essence of the contract;
- (2) Where delay operates as an injury;
- (3) Where the nature and necessity of the contract requires it to be so construed, for example, where a party asks for extension of time for performance."<sup>76</sup>

76. See R.K. PRASAD J, *Orissa Textile Mills Ltd v Ganesh Das*, AIR 1961 Pat 107. Unless the contract prescribes a time for performance, there is no question of any particular moment of time being regarded as of the essence of the contract, *D.S. Thimmappa v Siddaramakka*, (1996) 8 SCC 365: AIR 1996 SC 1960. The mere fact of time being mentioned with a statement that delay would have to be compensated does not of itself make time of the essence,

The well known authority is *Bhudra Chand v Betts*.<sup>77</sup>

The plaintiff stipulated with the defendant to engage his elephant for the purpose of *Kheda* operations (to capture wild elephants). The contract provided that the elephant would be delivered on the 1st October, 1910; but the defendant obtained an extension of time till the 6th October and yet did not deliver the elephant till the 11th. The plaintiff refused to accept the elephant and sued for damages for the breach.

He was held entitled to recover as the parties intended that time should be of the essence of the contract. "This conclusion is confirmed by the circumstance that the defendant obtained an extension of the time; if the time were not of the essence of the contract, he need not have asked for extension of time."<sup>78</sup>

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non-performance on the stipulated date did not give the party the right to treat the contract as ended and forfeit earnest money. *Thakorlal V. Patel v Lt. Col. Syed Badruddin*, (1993) 1 Guj LR 28. The court said (at p. 35): "The language of the agreement must show in most unmistakable terms that the intention of the parties was to make their rights to depend upon the observation of the time-limit. Intention may also be inferred from the nature of the property to be sold and the conduct of the parties and the surrounding circumstances at or before the contract and not what takes place after the contract has been entered into. Even where the parties have expressly provided that time is of the essence of the contract, other provisions may exclude the inference that the completion of the work by a particular date was intended to be fundamental, for example, if the contract were to include clauses providing for extension of time in certain contingencies or for payment of fine for every day or week the work remains unfinished, such clauses would be construed as rendering ineffective the express provision relating to the time being of the essence of the contract." The court picked up these observations from the decision of the Supreme Court in *Gomathinayagam Pillai v Palaniswami Nadar*, AIR 1967 SC 868: (1967) 1 SCR 227. *Vairavan v K.S. Vidyanandam*, AIR 1996 Mad 353, sale of immovable property with no stipulation that time was of the essence, there was stipulation for completion within six months failing which the advance paid was not to be returned. The court said that this would not make time of the essence. Recovery of property allowed by order of specific performance. *Badru Nisha v Yogendra Prasad Sinha*, AIR 2006 Pat 71: (2006) 1 BLJR 637 (Pat), in a contract for sale of immovable property, the date of performance was fixed with a provision for penalty if there was failure to keep the time, time was held to be the essence. Next day after the expiry of the date, purchaser sent a notice to the seller. Thus the conduct of the parties also showed that they attached importance to time. *Haryana Telecom Ltd v Union of India*, AIR 2006 Del 339, supply of cables, failure, the department claimed damages for non-supply, procured from other sources at cheaper rates, award of damages was set aside. Time was of the essence because there was a clause that every delay would be liquidated damages clause. *Coromandel Indag Products (P) Ltd v Garuda Chit & Trading Co (P) Ltd*, (2011) 8 SCC 601, the seller of property was in need of money, only short term extension was allowed, this showed that the short term period allowed for paying the price constituted time as of the essence.

77. (1915) 22 Cal LJ 566: 33 IC 347.

78. MOOKERJEE J at p. 567. Followed in *Colles Cranes of India Ltd v Speedeo Spares Corp*, AIR 1970 Cal 321. A contract containing provisions for extension of time in certain circumstances often has the effect of reducing the value of time of performance. *Abdulkhader v Plantation Corp of Kerala Ltd*, 1982 KLT 928. Where delay is due to the conduct of the party who has to supply material, penalty for delay cannot be imposed. *ONGC v S.S. Agarwalla & Co*, AIR 1984 Gau 11.

In business matters time generally of essence

*Businessmen attach importance to time*

The matter depends upon the intention of the parties. Even where “a specific date is mentioned for the completion of the contract,”<sup>79</sup> one has not to look at the letter but at the substance of the agreement in order to ascertain the real intention of the parties”.<sup>80</sup> “In commercial contracts time is ordinarily of the essence of the contract.”<sup>81</sup> This is so because the business world requires certainty<sup>82</sup> and also because “merchants are not in the habit of placing upon their contracts stipulations to which they do not attach some value and importance”.<sup>83</sup> Thus, in a contract to supply imported goods in October or November,<sup>84</sup> in a contract for the purchase of chassis for a diesel truck to be supplied within two months<sup>85</sup> and in an auction purchase, where the price was to be paid within 15 days,<sup>86</sup> time was held to be of the essence of the contract. Similarly, in a contract for the sale or purchase of goods the prices of which fluctuate rapidly in the market, the time of delivery and of payment are considered to be of the essence. In *Mahabir Prasad Rungta v Durga Datt*<sup>87</sup> the Supreme Court held on the facts of the case that time of payment was of the essence of the contract. The facts of the case were that a transporter contracted with Rungta, a colliery owner, to transport coal from a colliery to the railway station. The colliery-owner had to keep the road in repair and to arrange for petrol. He had also to pay for the transportation on the 10th of the next month. It was alleged that these things were not done in time and, therefore, the transporter could not go on with his work. The transporter rescinded the contract and brought an action for damages. It was held that in commercial transactions time is ordinarily of the essence of the contract. In this contract the time of payment and of arranging other things was, particularly, such an important condition of the contract that

79. Hence it becomes a mixed question of law and fact. *MCD v Jagan Nath Ashok Kumar*, (1987) 4 SCC 497: AIR 1987 SC 2316.

80. See *Sachidananda Patnik v G.P. & Co*, AIR 1964 Ori 269. *State of Karnataka v Coimbatore Premier Constructions*, (1988) 1 Kant LJ 249, where though time was described as of the essence, additional work allotted to the contractor was more extensive than the main work, the stipulated time lost its character of being essential. *U.K. Ramakrishnan v R. Raveendran*, (2004) 1 KLT (SN 7) 6 (Ker), where time, though specified, is not of the essence, performance must be offered within reasonable time. *Lakshmi Amma v Ayyappan*, (2003) 3 KLT 577, stipulation was that the plaintiff could file a suit within one week of the date of expiry of the agreement. The court said that this could not deprive the plaintiff of the right to file a suit within the period of limitation. S. 55 takes note of the effect of time as to performance and not as to filing of suits.

81. *China Cotton Exporters v Beharilal Ramcharan Cotton Mills Ltd*, AIR 1961 SC 1295. Followed in *Peeco Hydraulic (P) Ltd v East Anglia Plastics (India) Ltd*, (1987) 1 Cal LT 551, sale of machinery, commercial deal, time of essence.

82. *Hitkari Motors v Attar Singh*, AIR 1962 J&K 10.

83. *Bowes v Shand*, (1877) LR 2 AC 455, 463.

84. *China Cotton Exporters v Beharilal Ramcharan Cotton Mills Ltd*, AIR 1961 SC 1295.

85. *Hitkari Motors v Attar Singh*, AIR 1962 J&K 10.

86. *P.S. Duraikanoo v M. Saravana Chettiar*, AIR 1963 Mad 468.

87. AIR 1961 SC 990: (1961) 3 SCR 639; 645.

Section 55 could be invoked by the aggrieved party and the transporter was entitled to rescind the contract.

### *Construction contracts*

Time schedule in a construction contract is likely to be of the essence because construction is a commercial service. Where 24 months' time was given to the builder with a stipulation that if he failed to deliver within the stated time, he would pay 10 per cent per annum of the purchase price measured by the period of delay, time was held to be of the essence entitling recovery of the stipulated amount.<sup>88</sup> Similarly, where a builder's commitment with a bank was that he would make their building ready within six months, but could not do so, the bank was allowed to terminate the contract. The fact that the bank exercised this right after about two months after the expiry of the stipulated time did not amount to an extension of time.<sup>89</sup>

The termination of a contract was held to be proper where the contractor was not able to do anything to carry out the repair of a flood-protection dam inspite of the extension of time. The matter of time was a very important factor in the contract.<sup>90</sup> The Supreme Court observed that in construction contracts, the time of completion would be of the essence when special features exist.<sup>91</sup>

In a joint venture agreement, one of the clauses was that the defendants were to perform certain formalities within five years, and that, on failure to do so, the agreement was to become null and void. Neither any approval was obtained within that time, nor sanction of the building plan. The defendants could not start the construction within time. The court said that the provision in the contract for penalty and extension of time was of no use. The contract had ended by the efflux of time.<sup>92</sup> Where the construction of a warehouse could not be completed within the stipulated time and extensions were granted several times and even so the work could not be completed, it was held that the party could put an end to the contract at the end of the last extension if the work was still not completed.<sup>93</sup>

88. *Chye Fook v Teh Teng Seng Realty*, (1989) 1 Mal LJ 308 (Ipoh HC).

89. *United Commercial Bank v Jawaharlal Mill*, (1989) 2 Cal LJ 246.

90. *Nevilal Rohita Construction (P) Ltd v State of Bihar*, AIR 2005 Pat 190.

91. *McDermott International Inc v Burn Standard Co Ltd*, (2006) 11 SCC 181.

92. *R.K. Apartments (P) Ltd v Aruna Bahree*, (1999) 77 DLT 193.

93. *Food Corporation of India v Anupama Warehousing Establishment*, AIR 2004 Ker 137. *Municipal Corpn v Baluram*, (2006) 4 CLT 178 (P&CH), time was found to be of essence subject to availability of cement, cement was not available, the plaintiff arranged cement after expiry of time for completion, thereafter the work was completed promptly, performance good. *Indian Oil Corp v Lloyds Steel Industries Ltd*, AIR 2008 NOC 866 (Del), contract for designing, erection of Petroleum Products Terminal Depots, 16 months' period was granted for the Terminal at Jodhpur, delay could result in postponing of the project, time was, therefore, specified to be of essence, finding of the arbitrator was that in view of extensions, the condition that time was of essence lost its validity, court refused to interfere in the finding. *Venkatesh Construction Co v Karnataka Vidyuth Karkhanne Ltd*, (2016) 4 SCC 119: AIR

### *Sale transactions*

The courts would have to see on the facts of each case involving a sale transaction whether time factor was essential to performance or not. In a contract of sale of goods, the time of shipment is of the essence. There is a considerable authority in support of this rule and it has been recognised and accepted in *Bowes v Shand*.<sup>94</sup> Here in a contract of sale of rice to be shipped at Madras during March or April, 1874, by a ship of the name of Rajah of Cochin, the stipulation in regard to shipment was held to be a condition of the contract and the contract was held to be not satisfied by shipment a month earlier, that is, in February. A contract for sale of goods required fifteen days' loading notice. The court regarded it as a condition of the contract. The courts require precise compliance with stipulations as to time whenever the circumstances of the case indicate that that would fulfil the intention of the parties and that, in general, time is of the essence in mercantile contracts.<sup>95</sup>

A leading Supreme Court authority is *China Cotton Exporters v Beharilal Ramcharan Cotton Mills Ltd.*<sup>96</sup> The appellants who carried on an import business at Bombay contracted to supply to the respondent mill a quantity of Italian staple fibre cotton. The shipment was to take place in October or November. The contract concluded by the remark: "This contract is subject to import licence and therefore the shipment date is not guaranteed". A part of the goods were supplied and accepted, but the rest were not supplied in the time mentioned. The buyer wanted to avoid the contract on this ground. It was held that in spite of the remark that shipment date was not guaranteed, time was of the essence and the buyer was entitled to avoid the contract. DAS GUPTA J said: Remembering, as we must, that in commercial contracts time is ordinarily of the essence of the contract and giving the word "therefore" its natural grammatical meaning, we must hold that what the parties intended was that to the extent that delay in obtaining licence stands in the way of keeping to the shipment date, October/November, 1950, this shipment date was not guaranteed, but with this exception, October-November, 1950, was guaranteed. The sellers contended that the parties were mentioning only one of the many reasons which might cause delay in shipment and the conjunction "therefore" was used only to show the connection between one of the many reasons—by way of illustration and a general agreement that the shipment date was not guaranteed. We do not consider this explanation of the use of the word "therefore" acceptable. If the parties intended that quite apart from delay in obtaining import licence, shipment date was

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2016 SC 553, in a contract with fixed time frame, there was change in the nature of work and also involvement of additional work admitted by the parties. It was held that the parties could not be expected to go into a fresh round of negotiations and reframe terms of the contract. The suit was pending for over two decades.

94. (1877) LR 2 AC 455 (HL).

95. *Bunge Corp v Tradax Export S.A.*, (1981) 1 WLR 711 (HL).

96. AIR 1961 SC 1295.

not guaranteed, the natural way to expressing such intention would be to say: "The contract is subject to import licence and the shipment date was not guaranteed." The ordinary rules of grammar would not use the word "therefore" in such a context except to mean that only to the extent that delay was due to delay in obtaining import licence, shipment time was not guaranteed.

The delay in this case was due to the failure of the seller's own supplier to supply in time. This cannot be a defence unless it was a condition of the contract that the goods would be supplied only when received from the sources of supply. In a similar case before the Gujarat High Court:<sup>97</sup>

The undertaking was to ship by a particular ship in August, 1954. The plaintiff failed to ship in August and on their request the defendants extended the time to September 10. The plaintiffs failed to make good their default even within the extended time and, therefore, the defendants finally repudiated the contract. The plaintiff sued them for breach.

BHAGWATI J, following *China Cotton Exporters*, above, held that the time of shipment was of the essence and it was the plaintiff and not the defendants who were guilty of breach.

An application for extension of time does not take effect unless accepted and the fact that an extension for a week was offered would not amount to a waiver within the meaning of Section 63 of the right to insist upon the stipulated time.

There was a contract for the sale of red oxide of quality and quantity stipulated within 45 days, the time was described to be as of the essence. There were provisions for repudiation on default and also for liquidated damages and penalty. Considering these terms as also the commercial nature of the contract, the time was held to be as of the essence.<sup>98</sup> The contract was with a public sector undertaking for supply of iron ores. The petitioner was intimated to pay the consideration within seven days of the letter of intent. He could not do so. In the meantime iron ore prices increased considerably. Thus time was held to be of the essence. The action of the respondent to release supplies at increased rates could not be questioned in a writ petition.<sup>99</sup>

#### *Land and property dealings*

In a contract for the sale of land or immovable property, the Supreme Court has laid down that "it would normally be presumed that time was not of the essence of the contract. Mere incorporation in the written agreement of a clause imposing penalty in case of default does not by itself evidence an

97. *Wasoo Enterpriser v J.J. Oil Mills*, AIR 1968 Guj 57.

98. *Venkateswara Minerals v Jugalkishore Chiranjitlal*, AIR 1986 Kant 14. See further *Devender Singh v State of U.P.*, AIR 1987 All 306, where an application for extension of time was rejected after a long gap, the contractor was not allowed compensation for the waiting period. In hire-purchase transactions time of payment of hire instalments is of the essence.

99. *Manjunatha Overseas Granite Ltd v Mysore Minerals Ltd*, AIR 2010 NOC 69 (Kant).

intention to make time of the essence".<sup>100</sup> In such cases, therefore, the time factor would not be of essence for obtaining the relief of specific performance.<sup>101</sup> Intention of the parties can be ascertained from factors like nature of the property agreed to be sold, the possibility of price fluctuation, the need for entering into the contract, conduct of the parties before, at the time of and subsequent to the contract and other surrounding circumstances. A declaration that the stipulated time shall be of the essence would have to be taken in the light of other provisions and such other factors may either exclude or strengthen the inference that time was to be of the essence.<sup>102</sup> Where the agreement in clear terms provided that it was to be performed within six months else the earnest money would stand forfeited. The time was held to be of the essence.<sup>103</sup> In a contract for sale of land there was an express stipulation that time was of the essence. The consequences of non-performance within time were also stipulated. There was some surplus

100. *Gomathinayagam Pillai v Palaniswami Nadar*, AIR 1967 SC 868, 871: (1967) 1 SCR 227, 231-32; *Govind Prasad Chaturvedi v Hari Dutt Shastri*, (1977) 2 SCC 539: AIR 1977 SC 1005; *Ram Kishan Dass v Bhavi Chand Sharma*, AIR 1988 Del 20. In a contract for the sale of plots of land, 30 months' time was reserved by the seller for obtaining planning permissions, that was considered to be a sufficiently long period to disentitle the vendor from seeking any further time. *Mohd Nazran v Al-Ekhwan Construction*, (1991) 3 Current LJ 2324, High Court, Singapore. *E.S. Rajan v R. Mohan*, 1995 AIHC 3218 (Kant), the mere fact that time for performance is specified does not make it of the essence of the contract. Certain acts may be of such a nature that they may or may not be completed within the specified time. *Tatavarthi Jagannadham v Akkineni Radhakrishna*, (1997) 6 ALD 261 (DB). *Jayalakshmi v Anilkumar*, 1996 AIHC 4353 (Ker), in a sale of immovable property, the performance of the contract was dependent upon the fulfilment of certain requirements, and, therefore, it was held that the time reserved for completion of the transaction could not be of the essence of the bargain. *Ranganatha Gounder v Sahadeva Gounder*, AIR 2004 Mad 520, the time limit specified in the agreement cannot be regarded as irrelevant and can be ignored with impunity. But even so time cannot be regarded as of the essence in toto because the discretion vested in the court under Ss. 10 and 20 of the Specific Relief Act would be nullified. *Amteshwar Anand v Virender Mohan Singh*, (2006) 1 SCC 148: AIR 2006 SC 151, parties never treated time to be an important factor. Payments under the agreement were asked for much after the dates had expired. Time was held to be not of the essence. *Yogesh Mehta v Custodian*, (2007) 2 SCC 624, balance amount of consideration under terms of the contract was 60 days from grant of sanction of the offer by the Special Court, but confirmation of the sale was to be given by the Supreme Court. Hence 60 days were to run from the date of confirmation. Time not of the essence.

101. *Panchanan Dhara v Monmatha Nath Maity*, (2006) 5 SCC 340: AIR 2006 SC 2281.

102. *Kochappu v Somasundaram Chettiar*, (1991) 1 KLJ 525. In an agreement to sell immovable property, a part payment was to be made within a specified time and this the purchaser was not willing to make except upon further conditions, time was held to be of the essence. Specific enforcement was not allowed. *Chand Rani v Kamal Rani*, (1993) 1 SCC 519: AIR 1993 SC 1742. *Citadel Fine Pharmaceuticals v Ramaniyam Real Estates (P) Ltd*, (2011) 9 SCC 147: AIR 2011 SC 3351, commercial contract for sale of immovable property to builder, such purchaser could not keep time, he was not allowed to seek specific performance.

103. *Ceean International (P) Ltd v Ashok Surana*, AIR 2003 Cal 263. *M.K. Watts v Usha Sharma*, AIR 2004 P&H 295, in a transaction for sale of immovable property, the earnest money was not paid on the specified date. The payment was essential to the vendor for paying out his outstanding liabilities, express clause in the agreement described time to be of the essence held, time to be essence. *Syed Quadri v Syed Mujeebuddin*, AIR 2010 NOC 67 (AP), time prescribed for payment, otherwise consequences prescribed such as forfeiture, time regarded as of the essence.

land which required permission. The purchaser was put under the obligation to get permission. He could not do so. The court said that time being of the essence, the purchaser was not entitled to get the decree of specific performance.<sup>104</sup>

In an agreement to sell land there was a stipulation that the sale deed would be executed within one month of the date of securing permission from the Land Ceiling Authorities, but there was no stipulation as to the effect of failure of keeping the date. It was held that the vendor was entitled to specific performance. The stipulated time was not of the essence.<sup>105</sup> In another case the agreement which specified a date for performance was substituted by a new agreement which did not mention any date for execution of the sale deed. The agreement was made to depend upon the result of a case which was filed against the vendor by his brother and sister. No time was fixed for execution of the sale deed after decision in the suit. The court naturally said that time was not of the essence of the contract. The vendee served notice. The vendor refused. Suit filed within three years after such refusal was held to be within time.<sup>106</sup> The contract provided that the vendors would get the leasehold property converted into freehold prior to execution of sale deed. But they failed to fulfil this obligation. The court said that time of getting the property converted into freehold was not of the essence. The buyers could not be called upon to pay the balance price till them.<sup>107</sup>

Where in an agreement for sale of immovable property, there was no mention originally of the time of performance being of the essence and the buyer was ready and willing and had already paid two instalments, it was held that a unilateral attempt on the part of the vendor to make time as of the essence was improper.<sup>108</sup> As against this, a contract provided that the balance amount has to be paid and sale deed registered within a particular time and in no case the time would be extended. But the vendee failed to pay. The vendor gave him notice giving ten days further time for payment of the balance amount failing which the agreement would stand cancelled. Even so, the vendee failed to keep the date of payment. The vendee served on him the final notice of cancellation. The court said that the time of payment was of the essence. The defaulting vendee was not entitled to ask for specific performance.<sup>109</sup>

104. *Citadel Fine Pharmaceuticals v Ramaniyam Real Estates (P) Ltd*, (2011) 9 SCC 147: AIR 2011 SC 3351; *A.K. Lakshmi Pathy v Rai Saheb Pannalal H. Laboti Charitable Trust*, (2010) 1 SCC 287: AIR 2010 SC 577, clear condition in contract that the purchasers would have to definitely deposit the balance amount by the date stipulated in the contract for sale. Held, time of the essence.

105. *Rakha Singh v Babu Singh*, AIR 2002 P&H 270.

106. *Dalip Singh v Ram Nath*, AIR 2002 HP 106, the contract was specifically enforceable.

107. *Kuldip Gandotha v Shailendra Nath Endlay*, AIR 2007 Del 1.

108. *Swarnam Ramachandran v Aravacode Chakungal Jayapalan*, AIR 2000 Bom 410, the vendee had paid the instalments and was ready to pay the balance money without seeking indefinite extension of time.

109. *Vatsavayi Venkata Suryanarayana Raju v Metta Veerabhadra Rao*, (1999) 1 ALD 308. *Badru Nisha v Yogendra Prasad Sinha*, AIR 2006 Pat 71: (2006) 1 BLJR 637 (Pat), there

The Supreme Court has taken note of changed circumstances and observed that the age-old principle that in a contract relating to immovable property, time is not of essence requires to be revisited in view of the changed circumstances created by inflation and steep increase in the price structure of such properties (obiter). The contract contained a schedule specifying the periods for payment of consideration. The clause also provided that payment would be made on the next date if the date specified turned out to be a holiday. The execution of sale deed was delinked from the time schedule for payment. The court said that parties intention must have been to treat time of payment as of the essence.<sup>110</sup>

Where a decision was taken to sell a house immediately to raise urgently needed funds and six months' time was specified for payment, it was held that time of payment was of essence. The vendee's failure to make payment in time disentitled him from claiming specific performance.<sup>111</sup>

Under the agreement, the purchaser had to pay the balance amount of consideration at any time after the agreement within the outer limit of one year. Thereafter his right under the agreement to pay within one year was to cease and he was to lose all rights under the agreement. The court said that the agreement showed that the parties intended that time was of essence. Suit filing after seven years from the date of the agreement was held to be time barred.<sup>112</sup>

The vendors pleaded that they were in dire need of money and that is why they were selling, but they failed to adduce any evidence about the pressing need which goaded them to enter into the contract. Their conduct showed that they were not attaching any importance to time. The vendee showed sufficient balance in account to pay the balance money. Specific performance was not refused.<sup>113</sup>

The conduct of the parties plays an important role in determining importance of time of performance. Where both the parties seemed to have ignored the failures on the part of each other in the matter of implementation of their agreement, the court was of the view that it could not be said about such parties that they considered time to be of the essence.<sup>114</sup>

### *Allotment of plots*

A Development Authority allotted plots through auction sale. The auction-purchaser was granted time to make a late payment with interest. Even then he could not make it. The payment made by him after the expiry of

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was a clear stipulation that the sale should be completed within the specified time limit, no evidence to show that the plaintiff was ready and willing to complete her part, no specific performance.

110. *Sardamani Kandappan v S. Rajalakshmi*, AIR 2011 SC 3234.

111. *Nanjachary v P. Chennaveerachari*, AIR 2015 Mad 73.

112. *Narayan Sharma v Devender Kumar Sharma*, AIR 2014 NOC 219 (All).

113. *Mohd Abdul Azeem v South India Prime Tannery (P) Ltd*, AIR 2016 Hyd 170.

114. *Vishalkumar Nemichand Kakad v Shankar Mahadeo Kubde*, AIR 2009 NOC 258 (Bom).

time with interest was accepted by the Authority. The court said that there was a deemed extension of time. The cancellation of the whole thing was not proper.<sup>115</sup>

#### *Right of renewal and other personal privileges*

But the renewal of a lease is something different from sale of immovable property. This was pointed out by the Supreme Court in *Caltex (India) Ltd v Bhagwan Devi Marodia*:<sup>116</sup>

In this case, the lessee of a petrol pump had to apply for the renewal of the lease within a time fixed by the contract. He was late by ten days in his application for renewal. The landlord refused to renew.

The court held that the time so fixed was of the essence of the bargain. Equity would not relieve him of the consequences of his own neglect:

“An option for the renewal of a lease, or for the purchase or repurchase of a property, must in all cases be exercised strictly within the time limited for the purpose, otherwise it will lapse. The reason is that the renewal is a privilege and if the tenant wishes to claim the privilege he must do so strictly within the time-limit for the purpose. In such cases relief is not given in equity save upon the ground of unavoidable accident, fraud, surprise, ignorance (not wilful) or inequitable conduct on the part of the lessor precluding him from refusing to give the renewal.”<sup>117</sup>

#### *Agreement of reconveyance*

Similarly, a stipulation in a contract of sale of property that the buyer would reconvey the property to the seller if the latter refunded the consideration within a stipulated time, would constitute the time schedule to be of the essence and the right of reconveyance would be lost if the time is missed.<sup>118</sup>

115. *R.K. Saxena v DDA*, (2001) 4 SCC 137: AIR 2002 SC 2340.

116. AIR 1969 SC 405: (1969) 2 SCR 238. In *Govind Prasad Chaturvedi v Hari Dutt Shastri*, (1977) 2 SCC 539: AIR 1977 SC 1005, reserving two months' time on payment of earnest money if the property was not purchased within that time, the time was held to be of essence.

117. A property was transferred with a condition of reconveyance and that if reconveyance was not done within a certain time, the clause would become nullified, held, that some delay in repayment taking place was not to deprive the plaintiff of his right of reconveyance.

118. *Bibi Anwarunisa v Daulat Rai*, AIR 1988 Pat 229. *Bismillah Begum v Rahmatullah Khan*, (1998) 2 SCC 226: AIR 1998 SC 970, where also the right to seek reconveyance was lost because of the expiry of time. The court cited with approval the Federal Court decision in *Shanbhusham Pillai v Annalakshmi Ammal*, AIR 1950 FC 38: 1949 FCR 441 where it was held that in contracts relating to reconveyance of property, time factor has always been held to be of the essence of the contract. Citing HALSBURY'S LAWS OF ENGLAND, Art. 281 (Vol 3, 3rd Edn) 165, to the effect: “An option for renewal of lease, or for purchase or repurchase of property, must in all cases be exercised strictly within the time limited for the purpose, otherwise it will lapse.” Quoted with approval in *Hare v Nicoll*, (1966) 2 QB 130, 145: (1966) 2 WLR 441 (CA). A similar statement of law is to be found in FOA'S GENERAL LAW OF LANDLORD AND TENANT, Art. 453 (8th Edn) 310; also in HILL AND REDMAN'S LAW OF

### *Carriage by air*

A complainant under the Consumer Protection Act alleged that his cargo was not airlifted by the carrier within the time-limit. The National Commission agreed with the airliner that weighty cargo blocks could not be carried in time because the safety of the aircraft was an important factor at all times. The complainant had failed to establish that time was of the essence of the contract.<sup>119</sup>

### *Completion of term*

A licence was granted to run a telephone booth in a central bus terminus. The grant was for a limited period. At the time of the limited period allotment, the allottee made no grievance. On the expiry of the term the Corporation invited fresh bids. The existing licensee's challenge to this procedure was held to be not tenable.<sup>120</sup>

### *Sale of shares*

A transaction for sale of shares is of commercial nature. The time of completion of the transaction is likely to be an important factor. Where the agreement was for the sale of shares of unquoted private companies trading in a volatile sector, it was held that if a completion date had been named in the agreement, that would have been of the essence. Therefore, as soon as the scheme was prepared and completion could take place, it was open to the party to give notice to the other to complete the transaction specifying a reasonable time for completion. Thus, where time would have been of the essence if specified, there one party can make time of the essence by serving a reasonable notice upon the other to complete.<sup>121</sup>

### *Time of reporting*

A singer agreed to perform at a theatre for a certain season and to be present at least six days before the commencement of the engagement. But he reported only two days before. The theatre owner sought to put an end to the contract. But he was not allowed to do so. It was only a breach of a warranty and not of a term or condition which touched the substance of the contract. Hence, the plaintiff could only recover compensation for loss, if any, suffered by him.<sup>122</sup>

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LANDLORD AND TENANT (14th Edn) 54. *Raj Kishore v Prem Singh*, AIR 2011 SC 382, in a contract of reconveyance, time of essence.

119. *S.L. Exports v Singapore Airlines*, 2004 All LJ 202 (NC) Consumer Protection Act, 1986 [S. 2(1)(g)].

120. *G. Gurunadha Reddy v A.P. RTC*, AIR 1999 AP 179.

121. *British and Commonwealth Holdings plc v Quadrex Holdings*, 1989 QB 842: (1989) 3 WLR 723 (CA). See further *Claude-Lila Parulekar v Sakal Papers (P) Ltd*, (2005) 11 SCC 73: (2005) 124 Comp Cas 685, though the party can give notice to the other to perform within reasonable time but cannot unilaterally prescribe time for performance where the original agreement is silent about it.

122. *Bettini v Gye*, (1876) LR 1 QBD 183.

### *Non-commercial matters*

“In cases other than commercial contracts the ordinary presumption is that time is not of the essence of the contract.”<sup>123</sup> Accordingly, “in a contract for the sale of immovable property, time would not be regarded as of the essence unless it is shown that the parties intended so.”<sup>124</sup>

### *Extension of time*

The Supreme Court held in a case before it that the time of performance was extended by the parties and therefore it was not to be considered as of the essence of the contract.<sup>125</sup>

The contract was to provide a rig for a certain period which was to be extended in case of any breakdown in working. The rig broke down for some time and, without taking this into account, the owner of the rig wanted to withdraw it on the expiry of the period. The court said that though there cannot be unilateral extension of time, in this case, there was the agreement that the period would be extended so as to cover the breakdown period. The owner of the rig could not say that he should be permitted to withdraw the rig subject to his liability for damages. The machinery in question was rare and not easily available. Compensation would have served no purpose.<sup>126</sup>

Where a road building contract could not be completed in time due to security reasons and abnormally bad weather, among others, and the Authority refused to extend time despite the fact that the contractor was ready to give the undertaking that he would complete the project within one month of extension of time, the court said that extension should be granted because the only other alternative was cancelling the contract and retendering, which was likely to take five months. The contractor's work was found to be satisfactory.<sup>127</sup>

123. *Lucknow Automobiles v Replacement Parts Co*, AIR 1940 Oudh 443.

124. *Mulla Badruddin v Tufail Ahmed*, AIR 1963 MP 31. See also *Hindustan Construction Co Ltd v State of Bihar*, (1999) 8 SCC 436; AIR 1999 SC 3710 on appeal, *Hindustan Construction Co Ltd v State of Bihar*, (1999) 8 SCC 436; AIR 1999 SC 3710, affirmed by the Supreme Court in *Gomathinayagam Pillai v Palaniswami Nadar*, AIR 1967 SC 868: (1967) 1 SCR 227. In construction contracts also time is generally of the essence. Since construction involves several factors, one of which may operate to cause delay, the contract often contains fenced-round provisions for extension. This does not diminish the importance of the time of completion. It remains of the essence unless extended. See *N.N. Chowdhary v Hindustan Steel Works*, AIR 1934 AP 110. The mere fact, however, that the contract provides a penalty for delay is not sufficient in itself to show an intention to make time as of the essence. *Gomathinayagam Pillai v Palaniswami Nadar*, AIR 1967 SC 868: (1967) 1 SCR 227.

125. *Man Kaur v Harrtar Singh Sangha*, (2010) 10 SCC 512.

126. *Saipem SPA v Jindal Drilling & Industries Ltd*, (2003) 6 Bom CR 347. U.P. State Bridge Construction Corp Ltd v Bangalore Development Authority, AIR 2005 NOC 421 (Kant): (2005) 5 Kant LJ 112, penalty for delay, extension of time because of obstructions, held, time not of essence. *New India Assurance Co Ltd v Kusumanchi Kameshwara Rao*, (1997) 9 SCC 179, surety bond by an insurance company to pay the seller for his supplies.

127. *Ramakant Singh v Union of India*, (2004) 1 BLJR 173 (Pat). *S. Brahmanand v K.R. Muthugopal*, (2005) 12 SCC 764, original agreement fixed date for performance, request for postponing without specifying period, no action in response, that amounted to postponement of performance. Time became extended.

### Consequences of failure

Section 55 further declares that “if it was not the intention of the parties that time should be of the essence of the contract, the contract does not become voidable by the failure to do such things at or before the specified time”. It means that the innocent party will have to accept performance even if it is delayed. He does not have the right to reject. But he may sue the other party for any loss caused by the delay. In an Andhra Pradesh case,<sup>128</sup> there was some delay on the part of a contractor to supply to the State Electricity Board certain goods by the prescribed date and the court, finding no evidence whatsoever of the parties’ intention to regard time as of essence, held that the Board was bound to accept delayed deliveries. The right to recover compensation for the delay would be there. The Supreme Court has held that no notice would be necessary for exercising the right to seek compensation.<sup>129</sup>

Where, on the other hand, the time of performance is of the essence of the contract, any delay will render the contract voidable at the option of the other party. He may reject the performance and immediately sue for the breach. But he may at his option accept the delayed performance. If he does so he cannot afterwards recover compensation for the delay, “unless, at the time of such acceptance, he gives notice to the promisor of his intention to do so”.<sup>130</sup> Delay by itself does not put an end to the contract.<sup>131</sup> In a case before the Supreme Court,<sup>132</sup> in a building contract time was described to be

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128. *A.P. SEB v Patel and Patel*, AIR 1977 AP 172. *K.C. Skaria v Govt of State of Kerala*, (2006) 2 SCC 285, completion time 18 months, Govt delayed supply of cement and steel by 15 to 26 months, contractor justified in not being able to complete work within time, Government not entitled to recover from the contractor extra costs for getting the work done through other contractors.
129. *McDermott International Inc v Burn Standard Co Ltd*, (2006) 11 SCC 181; *Mecon Ltd v Pioneer Fabricators (P) Ltd*, AIR 2008 NOC 870 (Del), contractor’s claim for extra payment for expenditure because of delay, delay was attributable to both parties, the contractor was allowed only half the amount, he could not be allowed to take advantage of his own default.
130. *State of A.P. v Associated Engg Enterprises*, AIR 1990 AP 294, accepted site for construction out of time without giving notice of intention to sue for consequences of delay, no compensation was recoverable. *Bazpur Coop Sugar Factory Ltd v Surendra Mohan Agarwal*, AIR 1984 All 174, buyer insisting upon supplies even after the expiry of the period, he cannot say that time was of the essence. *Sind Biscuits Mfg Co v Delight Engg Works*, 1984 All LJ 964, where delayed supply of machinery was accepted without protest and, therefore, no claim for damages was entertained afterwards. *Superintending Engineer v K. Bapiraju*, (1997) 4 ALD 701: (1997) 5 An LT 146 (AP), Government delayed in handing over site but even so the contractor went on working without protest. This amounted to waiver of his right. His claim for compensation for delay and the arbitrator’s award for it were held to be unjustified and without jurisdiction.
131. *Jain Mills and Electrical Stores v State of Orissa*, AIR 1991 Ori 117.
132. *Hind Construction Contractors v State of Maharashtra*, (1979) 2 SCC 70: AIR 1979 SC 720; *K. Kallaiah v Ninegegowda*, AIR 1982 Kant 93; *Arosan Enterprises Ltd v Union of India*, (1999) 9 SCC 449, a contract described time to be of the essence but also provided for extension of time. The seller sought extension. The effect of silence on the part of the buyer was that the application for extension was not accepted. Without evidence of any renewed date, the court could not determine what was the future date of performance. There cannot be any presumption about extension. It has to be fixed or refixed in categorical terms. In this

of the essence of the contract. The contractor was given the facility to seek extension of time in advance on reasonable grounds, failing which a penalty was payable for each day of default. These stipulations were construed by the court as not making time to be of the essence. The contractor's application for extension was rejected and, on his failure to complete the works within the specified time, the Department rescinded the contract. The rescission was not approved by the Supreme Court. Some further period should have been allowed to the contractor telling him that the extended time would be of the essence and that it would neither be extended, nor excusable on payment of fine. Then only it would have been possible to rescind the contract.

In a contract for sale of land the vendor wanted payment to be made within a week, but on the insistence of the vendee, 10 days' period was agreed upon. The vendee offered money after ten days. The vendor refused. The court allowed no remedy to the vendee.<sup>133</sup>

### IMPOSSIBILITY OF PERFORMANCE AND FRUSTRATION

#### Initial impossibility [S. 56]

Section 56 first lays down the simple principle that "an agreement to do an act impossible in itself is void". For example, an agreement to discover a treasure by magic, being impossible of performance, is void.

#### Subsequent impossibility [S. 56]

The second paragraph of Section 56 lays down the effect of subsequent impossibility of performance. Sometimes the performance of a contract is quite possible when it is made by the parties. But some event subsequently happens which renders its performance impossible or unlawful. In either case the contract becomes void. Where, for example, after making a contract of marriage, one of the parties goes mad, or where a contract is made for the import of goods and the import is thereafter forbidden by a Government Order, or where a singer contracts to sing and becomes too ill to do so, the contract in each case becomes void.<sup>134</sup>

**S. 56. Agreement to do impossible act.**—An agreement to do an act impossible in itself is void.

**Contract to do act afterwards becoming impossible or unlawful.**—A contract to do an act which, after the contract is made, becomes impossible,

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case the contract was for supply of imported sugar. The buyer gave no response to the seller's request for extension, nor rescinded the contract. The effect was that the buyer lost the right to insist upon time to be of the essence.

133. *Kamal Rani v Chand Ram*, AIR 1980 Del 188.

134. Illustration (b), (d) and (e) to S. 56. *Chaman Lal Jain v Arun Kumar Jain*, AIR 1996 Del 108, a compromise for dissolving partnership converted into decree, not allowed to be challenged on the ground that the partnership had already frustrated. *Raj Kumar Gupta v Des Raj*, AIR 1995 HP 107, sale of agricultural land, sanction from Government, not possible because of subsequent change of law, frustration.

or, by reason of some event which the promisor could not prevent, unlawful, becomes void when the act becomes impossible or unlawful.

**Compensation for loss through non-performance of act known to be impossible or unlawful.**—Where one person has promised to do something which he knew, or, with reasonable diligence, might have known, and which the promisee did not know, to be impossible or unlawful, such promisor must make compensation to such promisee for any loss which such promisee sustains through the non-performance of the promise.

#### *Illustrations*

- (a) A agrees with B to discover treasure by magic. The agreement is void.
- (b) A and B contract to marry each other. Before the time fixed for the marriage, A goes mad. The contract becomes void.
- (c) A contracts to marry B, being already married to C, and being forbidden by the law to which he is subject to practise polygamy. A must make compensation to B for the loss caused to her by the non-performance of his promise.
- (d) A contracts to take in cargo for B at a foreign port. A's Government afterwards declares war against the country in which the port is situated. The contract becomes void when war is declared.
- (e) A contracts to act at a theatre for six months in consideration of a sum paid in advance by B. On several occasions A is too ill to act. The contract to act on those occasions becomes void.

#### **General principle of judicial non-interference**

In the first-known English case of *Paradine v Jane*<sup>135</sup> it was pointed out that subsequent happenings should not affect a contract already made:

There the defendant had taken an estate on lease from the plaintiffs. The defendant was dispossessed of it by alien enemies for some time and, therefore, refused to pay the rent for the period of dispossession.

It was held that “when the party by his own contract creates a duty, he is bound to make it good, if he may, notwithstanding any accident by inevitable necessity, because he might have provided against it by his contract; though the land be surrounded or gained by the seas, or made barren by wildfire, yet the lessor will have his whole rent”.

In the subsequent case to *Taylor v Caldwell*<sup>136</sup> BLACKBURN J laid down that the above “rule is only applicable when the contract is positive and absolute, and not subject to any condition either express or implied”.

In this case, the defendants had agreed to let the plaintiffs the use of their music hall between certain dates for the purpose of holding a concert there. But before that first day on which a concert was to be given, the hall was destroyed by fire without the fault of either party.

The plaintiffs sued the defendants for their loss. It was held that the contract was not absolute, as its performance depended upon the continued

135. *King's Bench*, (1647) Aleyn 26: 82 ER 897.

136. (1863) 3 B&S 826: 122 ER 309.

existence of the hall. It was, therefore, “subject to an implied condition that the parties shall be excused in case, before breach, performance becomes impossible from the perishing of thing without default of the contractor”.

With this decision began the struggle between the two principles, namely, the principle of sanctity of contract which supports the principle of absolute liability and the principle that a contract be discharged when the shared contractual assumption has been destroyed by change of circumstances.<sup>137</sup>

### Frustration

In the above case<sup>138</sup> the performance of the contract had become physically impossible because of the disappearance of the subject-matter. But the principle is not confined to physical impossibilities. It extends also to cases where the performance of the contract is physically possible, but the object the parties had in mind has failed to materialise. The well-known coronation cases of which *Krell v Henry*<sup>139</sup> is one, illustrates this:

The defendant agreed to hire from the plaintiff a flat for June 26 and 27, on which days it had been announced that the coronation procession would pass along that place. A part of the rent was paid in advance. But the procession having been cancelled owing to the King's illness, the defendant refused to pay the balance.

It was held that the real object of the contract, as recognised by both contracting parties, was to have a view of the coronation procession. The taking place of the procession was, therefore, the foundation of the contract. The object of the contract was frustrated by non-happening of the coronation and the plaintiff was not entitled to recover the balance of the rent.<sup>140</sup>

Thus, the doctrine of frustration comes into play in two types of situation, first, where the performance is physically cut off, and, second, where the object has failed. The Supreme Court of India has held that Section 56 will apply to both kinds of frustration. Referring to the section, B.K. MUKHERJEA J of the Supreme Court observed in *Satyabrata Ghose v Mugneeram Bangur & Co*<sup>141</sup> as follows: “This much is clear that the word ‘impossible’ has not been used here in the sense of physical or literal impossibility. The performance of an act may not be literally impossible but it may be impracticable and useless from the point of view of the object and purpose which the parties had in view; and if an untoward event or change of circumstances totally upsets the very foundation upon which the parties

137. See S.H. Goo, (1996) JBL 223 reviewing Professor Treitel's book, FRUSTRATION AND FORCE MAJEURE (1994 Edn). *Govindbhai Gordhanbhai Patel v Gulam Abbas Mulla Allibhai*, (1977) 3 SCC 179: AIR 1977 SC 1019, a contract becomes void by frustration only if something supervenes after its execution.

138. *Taylor v Caldwell*, (1863) 3 B&S 826: 122 ER 309.

139. (1903) 2 KB 740 (CA).

140. See McElory and Williams, *The Coronation Cases*, 4 Mod LR 241.

141. AIR 1954 SC 44: 1954 SCR 310.

rested their bargain, it can very well be said that the promisor finds it impossible to do the act which he promised to do.”<sup>142</sup>

Explaining the concept “frustration of the contract” in *Cricklewood Property & Investment Trust Ltd v Leighton's Investment Trust Ltd*<sup>143</sup> Viscount SIMON LC said that it means “occurrence of an intervening event or change of circumstances so fundamental as to be regarded by the law both as striking at the root of the agreement, and as entirely beyond what was contemplated by the parties when they entered into the contract”. To the same effect is the following statement of Lord WRIGHT:<sup>144</sup> “The word frustration is here used in a technical legal sense. It is a sort of shorthand: it means that a contract has ceased to bind the parties because the common basis on which by mutual understanding it was based has failed. It would be more accurate to say, not that the contract has been frustrated, but that there has been a failure of what in the contemplation of both parties would be the essential condition or purpose of the performance.”

This principle was applied by TEJA SINGH J of the Punjab High Court in *Parshotam Das v Municipal Committee, Batala*.<sup>145</sup>

A Municipal Committee leased out certain tonga stands to the plaintiff for Rs 5000. But no tonga driver came forward to use the stand throughout the year and the plaintiff could not realize anything. He sued for the refund of his money.

It was held that “the plaintiff obtained the lease and the committee granted the same to him on the assumption that the tonga stands would be used by drivers and the plaintiff would recover fees from them, but for reasons which both sides could not help the drivers did not use the stands, the doctrine of frustration applied with full force”.

A contract for sale of land for non-agricultural use was held to have frustrated when the application for such use was rejected by the authorities.<sup>146</sup>

142. These principles have been *affirmed* by the Supreme Court in *Dhruv Dev Chand v Harmohinder Singh*, AIR 1968 SC 1024, where SHAH J (afterwards CJ) held that the doctrine does not apply to completed transfers. *Indian Rare Earth Ltd v Southern Electric Supply Co of Orissa*, AIR 2010 Ori 115, no supply to factory because of uprooting of towers by super cyclone, no liability.

143. 1945 AC 221 (HL).

144. In *Twentsche Overseas Trading Co Ltd v Uganda Sugar Factory Ltd*, (1945) 58 LW 315: AIR 1945 PC 144.

145. AIR 1949 East Punjab 301, 304.

146. *Naimudin I. Bharmal v Charotar Gramoddhar Sahakari Mandli Ltd*, (1997) 1 Guj LR 547. *Central Bank of India Staff Coop Building Society Ltd v Dulipalla Ramachandra Kotesewara Rao*, AIR 2004 AP 18: (2003) 5 ALD 116 (DB), sale of vacant land for which permission was necessary, but not taken, law changed, alienation prohibited, the buyer remaining silent for 19 years, not enforceable, frustration with efflux of time. *N. Satyanarayana v Vedprakash Dusaj*, (2003) 3 ALD 884, transfer of land subject to permission of Cantonment Board, permission not granted, contract impossible of performance, hence no specific relief. *A. Mohd Basheer v State of Kerala*, (2003) 6 SCC 159, auction of forest, before confirmation of bid, partly destroyed by fire, reauction, fetching less, shortfall could not be recovered from first bidder.

### Commercial hardship

The alteration of circumstances must be “such as to upset altogether the purpose of the contract. Some delay or some change is very common in all human affairs, and it cannot be supposed that any bargain has been made on the tacit condition that such a thing will not happen in any degree”.<sup>147</sup> This makes the court rather cautious in discharging parties from their contract. An illustration in line is the decision of the Calcutta High Court in *Sachindra Nath v Gopal Chandra*.<sup>148</sup>

The plaintiff let certain premises to the defendant for a restaurant at somewhat higher rent. The defendant agreed to pay high rent because the British troops were stationed in the town and a clause in the agreement specially provided that “this agreement will remain in force so long as British troops will remain in this town”. After some months, the locality was declared out of bounds to the British troops.

The question was whether this frustrated the contract. HENDERSON J relied upon the above cited passage of Lord LOREBURN and held that though it was possible that the defendant would not have paid such a high rent apart from the expectation of deriving high profits from the British troops, that was not sufficient to make out a case of frustration.

A situation like this has been described as one of commercial hardship, which may make the performance unprofitable or more expensive or dilatory, but is not sufficient to excuse performance, for it does “not bring about a fundamentally different situation such as to frustrate the venture”.<sup>149</sup> The doctrine of frustration or impossibility does not apply to a situation so as to excuse performance “where performance is not practically cut off, but only rendered more difficult or costly”.<sup>150</sup> Such cases may not fall within the purview of Section 56 and this is amply shown by the Privy Council decision in *Hurnandrai Fulchand v Pragdas Budhsen*.<sup>151</sup>

By a contract in writing the plaintiff bought of the defendants a number of *dhotis* to be manufactured by specified mills and to be delivered as and when the same may be received from the mills. The sellers delivered only part of the goods owing to the mills failing to perform their

147. Per Lord LOREBURN in *F.A. Tamplin Steamship Co Ltd v Anglo-Mexican Petroleum Products Co Ltd*, (1916) 2 AC 397.

148. AIR 1949 Cal 240.

149. See Anson's *LAW OF CONTRACT* (22nd Edn by Guest, 1964) 459. *Travancore Devaswom Board v Thanath International*, (2004) 13 SCC 44: (2004) 1 KLT 56, it is not a ground for non-performance that performance had become onerous or for claiming enhancement of consideration. *Premier Explosives Ltd v Singareni' Collieries Co Ltd*, AIR 2010 AP 107, prospects of dwindling profit from contract due to inflation of procurement price of raw material, onerous performance, held to be not a factor falling within purview of S. 56.

150. Per THOMAS J in *Megan v Updike Grain Corpn*, 94 F 2d 551 (1938), collected from Shepherd and Wellington, *CONTRACT AND CONTRACT REMEDIES, CASES AND MATERIALS* (4th Edn, 1957) 718, 721.

151. (1922–23) 50 IA 9, on appeal from the Bombay High Court: *Hurnandrai Fulchand v Pragdas Budhsen*, (1922–23) 50 IA 9: AIR 1923 PC 54 (2).

contract with the defendants as they were engaged in fulfilling certain Government contracts. The defendants pleaded frustration.

The Privy Council held that the adventure was not frustrated, as the stipulation as to delivery did not make delivery by the mills a condition precedent. It was a simple case of breach. "The closing or even the destruction of the mills would not affect a contract between third parties, which is in terms absolute."

"It was suggested that the words 'as and when the same may be received from the mills', should be construed as if they were 'if and when the same may be received from the mills'. This is to convert words, which fix the quantities and times for deliveries by instalments into a condition precedent to the obligation to deliver at all, and virtually make a new contract. The words certainly regulate the manner of performance, but they do not limit the sale to such goods as the mills might deliver."

The principle of this case was followed by the Supreme Court in *Ganga Saran v Firm Ram Charan Ram Gopal*.<sup>152</sup>

A contract was made for supplying certain bales of cloth manufactured by the New Victoria Mills, Kanpur. The contract added: "We shall go on supplying goods to you of the Victoria Mills as soon as they are supplied to us by the said mills." The mill failed to supply the goods to the sellers and, therefore, the sellers pleaded frustration.

But they were held liable: "The agreement does not seem to us to convey the meaning that the delivery of the goods was made contingent on their being supplied to the respondents by the Victoria Mills. We find it difficult to hold that the parties ever contemplated the possibility of the goods not being supplied at all. The words 'prepared by the Mills' are only a description of the goods to be supplied, and the expression 'as soon as they are prepared' and 'as soon as they are supplied to us by the said Mills', simply indicate the process of delivery."

It was accordingly held that the contract was neither contingent under Section 32, nor did it fall within the second paragraph of Section 56.<sup>153</sup>

To the same effect is the decision of the Madras High Court in *Samuel Fitz & Co v Standard Cotton and Silk Wvg Co*.<sup>154</sup>

The defendants placed an order with the plaintiffs for the supply of tapestries of certain kind, making it clear that they intended to sell them in Australia. But the Australian Government prohibited the import of such goods. The defendants lost their market and, therefore, cancelled their order.

152. AIR 1952 SC 9; 1952 SCR 36 at p. 11.

153. A person who contracts to supply has to assure his stock. His inability to replenish his stock is his problem and not that of other party. *Standard Chemicals Co (P) Ltd v Palakol Cooperative Sugars Co Ltd*, (1988) 25 Rep 60.

154. AIR 1945 Mad 291 at p. 293.

In an action for breach of contract, HORWILL J held that the courts should not read into a contract an implied term that the enforceability of the contract was dependent upon the ability of the purchaser to find customers for the goods. "We are unable to say that the foundation of the contract was that these goods should be resold by the defendants to their clients in Australia."

Similarly, a contract by a Hindu father to give his daughter in marriage to the plaintiff was held by the Bombay High Court to be not frustrated simply because the girl had expressed her unwillingness to marry the plaintiff. The defendant had to pay damages for the breach.<sup>155</sup> In the same way, where the performance of a contract for the sale of grain was made more difficult by Government restrictions on sale and storage imposed subsequently;<sup>156</sup> a contract given by an authority to a contractor of the right to collect tolls at the *ghats* of a bridge and the Government subsequently prohibited the traffic of foodgrains over the bridge resulting in loss to the plaintiff;<sup>157</sup> the temporary suspension of traffic on a bridge owing to breakdown;<sup>158</sup> in a contract to supply a ship, the increase in shipping rates;<sup>159</sup> in a contract for the sale of land, the local officer's insistence that State permission for the transfer should be obtained;<sup>160</sup> the workers of toddy shops going on strike after the contractor had obtained by bidding at an auction the licence to run the shops;<sup>161</sup> in a contract for supply of machinery, the failure of the source from which the supplier sub-contracted to purchase;<sup>162</sup> failure to supply the contracted quantity in assorted variety of eucalyptus firewood owing to the forest, which was under the supplier's lease, not helping him up to the requisite quantity, aggravated further by shortage of labour and transport facility in the area, all these were things which the contractor should have considered before giving his commitments;<sup>163</sup> and, therefore, in all these cases the performance was held not to have become impossible. "Disappointed expectations do not lead to frustrated contracts."<sup>164</sup>

155. *Purshotamdas Tribhovandas v Purshotamdas Mangaldas*, ILR (1896) 21 Bom 23. See also *Amuruvvi Perumal v Sabapathi*, AIR 1952 Mad 253.

156. *Sahas Karam v Nath Mal*, AIR 1951 Ajm 65; See also *Gurdit Singh v Secy of State*, AIR 1931 Lah 347.

157. *District Board, South Kanara v G. Santhappa Naik*, AIR 1925 Mad 907: (1925) 86 IC 362.

158. *Sankaran v District Board, Malabar*, AIR 1934 Mad 85.

159. *Karl Ettlinger v Chagandas & Co*, ILR (1915) 40 Bom 301.

160. *Govindbhai Gordhanbhai Patel v Gulam Abbas Mulla Allibhai*, (1977) 3 SCC 179.

161. *State of Kerala v Paily Chandy*, 1984 KLT 260: AIR 1984 NOC 70 (Ker).

162. *MTU Asia Pte Ltd v Brightside-Woh Hup*, (1989) 1 Mal LJ 10 High Court of Singapore.

163. *Gwalior Rayon Silk Mfg (Wvg) Co v Shri Andavar & Co*, AIR 1991 Ker 134.

164. *Davis Contractors Ltd v Fareham Urban Distt Council*, 1956 AC 696, 715: (1956) 3 WLR 37 (HL), cited by *Pearl Cycle Industries Ltd v A.N. Kaul*, AIR 1964 Punj 482. Licensing of a trade subsequent to contract is not frustration. *Seth Mohan Lal v Grain Chambers Ltd*, AIR 1968 SC 772. A contract to run toddy shop, strike by toddy tappers and suppliers, S. 56 not applied. *State of Kerala v Paily Chandy*, 1984 KLT 260: AIR 1984 NOC 70 (Ker). With this should be contrasted *Punjab Sons (P) Ltd v Union of India*, AIR 1986 Del 158, where the material in question (hot dip tin) was neither available in the market, nor the Government made any arrangement for supplying it, the contractor was released from his responsibility

## Specific grounds of frustration

“The principle of frustration of contract, or of impossibility of performance is applicable to a great variety of contracts. It is, therefore, not possible to lay down an exhaustive list of situations in which the doctrine is going to be applied so as to excuse performance. The law upon the matter is undoubtedly in process of evolution.”<sup>165</sup> Yet the following grounds of frustration have become well-established.

### 1. Destruction of subject-matter

The doctrine of impossibility applies with full force “where the actual and specific subject-matter of the contract has ceased to exist”.<sup>166</sup> *Taylor v Caldwell*<sup>167</sup> is the best example of this class.” There, a promise to let out a music hall was held to have frustrated on the destruction of the hall. Another illustration is *Howell v Coupland*.<sup>168</sup>

The defendant contracted to sell a specified quantity of potatoes to be grown on his farm, but failed to supply them as the crop was destroyed by a disease.

Delivering the judgment of the Court of Appeal, MELLISH LJ said:

“Suppose the potatoes had been fully grown at the time of the contract, and afterwards the disease had come and destroyed them; according to the authorities it is clear that the performance would have been excused; and I cannot think it makes any difference that the potatoes were not then in existence. ... Here there was an agreement to sell and buy two hundred

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of supplying to the Government milk containers quoted with that material. *C.T. Xavier v P.V. Joseph*, AIR 1995 Ker 140, delay in construction of godowns for Food Corp, clause for extension of time was there, no evidence that the Corp would not have taken the godowns even if provided late, this cannot be described as impossibility so as to enable any party to get rid of the contract. *C.J. International Hotel Ltd v NDMC*, AIR 2001 Del 435, a licence land for hotel premises taken at an open auction, the licensee was not allowed to say that licence fee should be reduced because the project was not economically viable. The Authority was not restrained from taking any coercive action. *Gujarat Housing Board v Vipul Corp*, AIR 2004 Guj 319, contract for water proofing work of houses, contractor had knowledge that the houses were in possession of allottees, the court did not regard denial of access by allottees as an impossibility. *N.G. Vigneshwara Bhat v P. Srikrishna Bhat*, AIR 2006 Ker 322, vendor's failure to make out title for all the properties agreed to be sold did not frustrate the contract because the properties under the absolute ownership of the vendor were definitely transferable. *H.P. State Cooperative Bank Ltd v U.P. State Financial Corpn*, AIR 2016 HP 29, inability by a financial corporation to pay interest on its bonds is not the same as an impossibility of performance.

165. See A.L. Corbin, *Recent Developments in Contracts*, (1937) 50 Harv L Rev 549, 465–66.  
166. See McCARDIE J in *Blackburn Bobbin Co v T.W. Allen & Sons*, (1918) 2 KB 467 (CA); *Markfed Vanaspati & Allied Industries v Union of India*, (2007) 7 SCC 679, *force majeure* clause can be invoked when it pertains to the contractual obligation that has purportedly become impossible of performance.

167. (1863) 3 B&S 826: 122 ER 309.

168. (1876) 1 QBD 258 (CA). *State of A.P. v Tangudu Varaprasada Rao*, (2004) 4 ALD 528, forest suffering from natural calamity or vandalism by acts of third parties, effect upon contract and indemnity.

tons out of a crop to be grown on a specific land, that it is an agreement to sell what may be called specific things; therefore neither party is liable if the performance becomes impossible."

A parallel decision under Section 56 is that of the Madras High Court in *V.L. Narasu v P.S.V. Iyer*<sup>169</sup> where a contract to exhibit a film in a cinema hall was held to have become impossible of performance when on account of heavy rains the rear wall of the hall collapsed killing three persons and its licence was cancelled until the building was reconstructed to the satisfaction of the chief engineer. The owner was under no liability to reconstruct the hall and even if he did reconstruct and it took him some time, by that time the film would have lost its appeal.

Where the tenanted premises comprised land and building, the court said that once the structure was completely destroyed, the tenancy ceased. No right was available to the tenant to apply for possession if the landlord re-constructed the premises.<sup>170</sup>

The same result followed where a ship ran aground.<sup>171</sup> The result would also be the same where the subject-matter of the contract though intact has ceased to be available to the parties. Thus, where a ship was chartered for twelve months to run from April to April and before it could be delivered, it was requisitioned and was released only in September, the House of Lords held that the charterparty had frustrated, for a September to September term was not contemplated by the parties.<sup>172</sup> Where the parties can still perform their main obligation despite the fact that the subject-matter has gone out of their hands, frustration may not follow. Thus, where a ship was chartered for five years and three years after that, it was requisitioned by the Government, the latter paying more money than the freight agreed between the parties, it was held that the contract was not frustrated. The charterer was bound to pay the freight and that he could still pay and, therefore, he was entitled to collect the money from the Government.<sup>173</sup> Similarly, an agency for dealing with the goods "manufactured or sold" by the principal was not frustrated when the principal's factory was destroyed, for the agent could still deal with the goods sold by the principal.<sup>174</sup>

In a contract for carriage of goods by sea, a vessel sank with cargo. There was evidence to show that the vessel had started taking in water. When the vessel was discovered to be tilting, the water in the bilge was pumped out

169. AIR 1953 Mad 300.

170. *West Bengal Khadi and Village Industries Board v Sagore Banerjee*, (2003) 1 ICC 991 (Cal), S. 108(c) of the Transfer of Property Act applies only when the tenancy is not completely destroyed.

171. *Jackson v Union Marine Insurance Co Ltd*, (1874–80) All ER Rep 317.

172. *Bank Line Ltd v Arthur Capel & Co*, 1919 AC 435 (HL).

173. *Tampling S.S. Co Ltd v Anglo-Mexican Petroleum Products Co Ltd*, (1916) 2 AC 397 (HL).

174. *Turner v Goldsmith*, (1891) 1 QB 544 (CA). *S.S. International v Union of India*, (2005) 125 DLT 287, tender for supply of *Kishmish*. A large quantity of *Kishmish* was consumed after delivery without any complaint and did not become unwholesome or bad, S. 56 was held to be not applicable.

but no action was taken to go to the nearest port to have the vessel berthed and the condition of the vessel checked. Instead of that, after pumping out water, the vessel attempted to continue on its course. The court said that the sinking of the vessel could not be described as an inevitable accident. Reasonable care had not been taken to prevent the sinking of the vessel. The defence of frustration failed.<sup>175</sup>

## 2. Change of Circumstances

A contract will frustrate "where circumstances arise which make the performance of the contract impossible in the manner and at the time contemplated."<sup>176</sup> KAPUR J of the Punjab High Court in *Pameshwari Das Mehra v Ram Chand Om Prakash*<sup>177</sup> explained the principle thus: "It is clear that if there is entirely unanticipated change of circumstances the question will have to be considered whether this change of circumstances has affected the performance of the contract to such an extent as to make it virtually impossible or even extremely difficult or hazardous. If that be the case, the change of circumstances not having been brought about by the fault of either party, the courts will not enforce the contract." In that case:

A contracted to supply to B certain classes and quantities of American piece goods. The contract was *c.i.f.* Karachi. The goods arrived there after some delay. B refused to accept on the ground that both the qualities and quantities offered for delivery were not according to the particular contract. A called upon B to refer the dispute to the nominated arbitrator who was residing at Karachi. Then came partition which made it impossible for non-Muslims to go to Karachi.

Holding that the contract was not thereby frustrated, the court said: "If it was necessary for the parties to go to Karachi and to take witnesses there, the performance of the arbitration agreement would have been rendered impossible. But, as going to Karachi was not necessary, the change of circumstances did not have a material effect on the contract."<sup>178</sup>

As against this, where a ship was chartered to load a cargo but on the day before she could have proceeded to her berth, an explosion occurred in the auxiliary boiler, which made it impossible for her to undertake the voyage at the scheduled time, the House of Lords held that frustration had, in fact, occurred in the circumstances.<sup>179</sup>

175. *Ghee Seng Motor v Ling*, (1994) 1 Curr LJ 382 (Malaysia).

176. Viscount MAUGHAM in *Joseph Constantine Steamship Line Ltd v Imperial Smelting Corp Ltd*, 1942 AC 154 (HL).

177. AIR 1952 Punj 34, 38. Thus, a normal change of circumstances, such as price rise, does not frustrate the contract. *Continental Construction Co Ltd v State of M.P.*, (1988) 3 SCC 82, 87: AIR 1988 SC 1166.

178. At p. 88. *Nagnath Kaulwar & Sons v Govindram Shyamsunder*, AIR 2004 Bom 271: (2004) 3 Mah LJ 457, non-availability of wagons was held to be no excuse to a supplier of rice to fulfil his contractual commitments.

179. *Joseph Constantine Steamship Line Ltd v Imperial Smelting Corp Ltd*, 1942 AC 154 (HL).

But “there is no general liberty reserved to the courts to absolve a party from liability to perform his part of the contract merely because, on account of an unanticipated turn of events, the performance of the contract may become onerous”.<sup>180</sup> “The parties to an executory contract are often faced, in the course of carrying it out, with a turn of events which they did not at all anticipate—a wholly abnormal rise or fall in price, a sudden depreciation of currency, an unexpected obstacle to execution, or the like. Yet this does not in itself affect the bargain they have made.”<sup>181</sup> The Supreme Court laid down this principle in *Alopi Parshad & Sons Ltd v Union of India*.<sup>182</sup>

The plaintiffs were acting as the agent to the Government of India for purchasing *Ghee* for the use of army personnel. They were to be paid on cost basis for different items of work involved. The performance was in progress when the Second World War intervened and the rates fixed in peace time were entirely superseded by the totally altered conditions obtaining in war time. The agents demanded revision of rates but received no replies. They kept up the supplies. The Government terminated the contract in 1945 and the agents claimed payment on enhanced rates.

But they could not succeed. “*Ghee* having been supplied by the agents under the terms of the contract, the right of the agents was to receive remuneration under the terms of that contract.”

Law has to adapt itself to economic changes. Marginal price rise may be ignored. But when prices escalate out of all proportion from what could have been reasonably expected by the parties and making performance so crushing to the contractor as to border virtually on impossibility, the law would have to offer relief to the contractor in terms of price revision. The Supreme Court has recognised this in *Tarapore & Co v Cochin Shipyard Ltd.*<sup>183</sup>

In this case there is no room for doubt that the parties agreed that the investment of the contractor (for import of equipment and know-how, in foreign exchange) would be two crores and the tendered rates were predicated upon and co-related to this understanding. When an agreement is predicated upon an agreed fact situation, and that situation ceases to exist, the agreement, to that extent, becomes irrelevant or otiose. The rates payable to the contractor were related to the investment of Rs 2 crores by the contractor. Once the rates became irrelevant on account of circumstances beyond the control of the contractor, it was open to him to make a claim for compensation.

180. *Alopi Parshad & Sons Ltd v Union of India*, AIR 1960 SC 588: (1960) 2 SCR 793.

181. Ibid. *State of A.P. v V. Narendra Reddy*, (2003) 4 ALD 345, a licensee for sale of arrack filed a suit against the State saying that the licence had become impossible of performance because of threats of naxalites. The ground was not established and at the same time the licensee was prepared to participate in the reauction. His suit was dismissed.

182. AIR 1960 SC 588: (1960) 2 SCR 793.

183. (1984) 2 SCC 680: AIR 1984 SC 1072 at p. 715.



Another case of commercial hardship of this kind was before the House of Lords in *Davis Contractors Ltd v Fareham Urban Distt Council*.<sup>184</sup>

There was a contract to build certain houses for a council for a fixed price and to be completed within eight months. Bad weather and labour strikes intervened and it took twenty-two months to complete and at a cost much more than the contract price. The contractor claimed that the contract was discharged on account of inordinate delay and, therefore, he should be paid on *quantum meruit* basis, that is, his actual costs should be paid.

But the House of Lords did not agree with him. Lord RADCLIFFE, after reviewing the authorities and anthology of circumstances in which frustration is deemed to occur, observed: "So, perhaps, it would be simpler to say at the outset that frustration occurs whenever the law recognises that, without default of either party, a contractual obligation has become impossible of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract. 'The data for decision are, on the one hand, the terms and conditions of the contract, read in the light of the surrounding circumstances, and, on the other hand, the events which have occurred.' It is not hardship or inconvenience or material loss itself which calls the principle of frustration into play. There must be as well such a change in the significance of the obligation that the thing undertaken would, if performed, be a different thing from that contracted for. If this is the law, the appellants' case seems to be a long way from a case of frustration."

The ruling in this case was applied in *CTI Group Inc v Transclear SA*.<sup>185</sup> The defendant contracted in unqualified terms to supply a cargo of cement f.o.b. on the claimant's vessel in Far East. The defendant made arrangement with local suppliers to provide the cargo. The suppliers decided not to make the cargo available owing to the commercial pressure applied by another supplier. The defendant had no other source for supply of cement in the Far East. The question was whether the supplier's failure to make goods available constituted a frustrating event. The court did not accept the argument that this could be so because where the delivery remained physically and legally possible but the seller's suppliers chose, for whatever reason, not to make the goods available, the contract was not frustrated. Accordingly, the suppliers' choice not to make the cargo available had not discharged the defendant's obligation to procure delivery of it.

Where there was a 400 per cent escalation of prices owing to a war as compared with the original prices on which certain transformers were undertaken to be supplied on a firm basis, the contract was held to have ended.<sup>186</sup>

184. 1956 AC 696, 715; (1956) 3 WLR 37 (HL).

185. (2008) Bus LR 1729; (2008) EWCA 856.

186. *Easun Engg Co Ltd v Fertilisers and Chemicals Travancore Ltd*, AIR 1991 Mad 158.



Where the possibility of alteration of circumstances was within the contemplation of the parties at the time of the contract, they can hardly complain of any such alteration.<sup>187</sup> Thus, where a railway company accepted goods for transport and happened to convey them to a wrong destination, which on account of partition fell in Pakistan and the railways could not bring them back into India, they were not permitted to plead frustration to their liability to pay for the loss of the goods.<sup>188</sup> MEHAR SINGH J said: "When the defendant accepted the goods, there was no such legal impediment, and since the date of partition was known at that time, such a contingency cannot be said to be outside the contemplation and foresight of the parties."

The learned judge, with respect, should not have taken support of the fact "that there was no such legal impediment at the time", for in applying the doctrine of frustration the courts have to go by the impediments arising subsequently. The decision is, however, just because it was the railway's own fault that the goods were carried to a wrong point.

### 3. Non-occurrence of contemplated event

Sometimes the performance of a contact remains entirely possible, but owing to the non-occurrence of an event contemplated by both parties as the reason for the contract, the value of the performance is destroyed. *Krell v Henry*<sup>189</sup> is an apt illustration. There, a contract to hire a room to review a proposed coronation procession was held to have frustrated when the procession was postponed. For this result to follow it is necessary that the happening of the event should be the foundation of the contract. This is shown by *Herne Bay Steam Boat Co v Hutton*<sup>190</sup> which also arose from the postponement of the coronation. The Royal Naval Review was proposed to be held on the occasion. The defendant chartered a steamboat for two days "to take out a party of paying passengers for the purpose of viewing the naval review and for a day's cruise round the fleet". But the review was cancelled and the defendant had no use of the ship. Yet he was held liable to pay the unpaid balance of the hire less the profit which the plaintiff had made by the use of the ship in the ordinary course. VAUGHAN WILLIAMS LJ said: "I see nothing that makes this contract differ from a case where, for instance, a person has engaged a brake to take himself and a party to Epsom to see the races there, but for some reason or other, such as the spread of an infectious disease, the races are postponed. In such a case it could not be said that he should be relieved of his bargain. So in the present case it is sufficient to

187. See *S. Vedantacharya v Highways Deptt by South Arcot*, (1987) 3 SCC 400 where the Highway Department was not permitted to absolve itself from responsibility for an accident on the ground of the heavy rain and flood, there being nothing to show what preventive measures were taken anticipating such rain and flood.

188. *Union of India v Chanan Shah Mahesh Dass*, AIR 1955 Pepsu 51.

189. (1903) 2 KB 740 (CA).

190. (1903) 2 KB 683 (CA).

say that the happening of the naval review was not the foundation of the contract."

#### 4. Death or incapacity of party

"A party to a contract is excused from performance if it depends upon the existence of a given person, if that person perishes" or becomes too ill to perform. Thus, where the nature or terms of a contract require personal performance by the promisor, his death or incapacity puts an end to the contract. *Robinson v Davison*<sup>191</sup> is the well-known authority.

There was a contract between the plaintiff and the defendant's wife, who was an eminent pianist, that she should play the piano at a concert to be given by the plaintiff on a specified day. On the morning of the day in question she informed the plaintiff that she was too ill to attend the concert. The concert had to be postponed and the plaintiff lost a sum of money.

The plaintiff's action for breach of contract failed. The court said that under the circumstances she was not merely excused from playing, but she was also not at liberty to play, if she was unfit to do so. The contract was clearly subject to the condition of her being well enough to perform: "The whole contract is based on the assumption of the continuance of life, and on the conditions which existed at the time. That assumption is made by both; it is really the foundation of the contract. It does not require close reasoning to prove that if the foundation fails, the whole contract must fail. Here the foundation was wanting for there was on Mrs Davison's part an entire and total incapacity to do the thing contracted for."

In another case:<sup>192</sup>

A person entered into service as manager for ten years, and undertook not to undertake any professional engagement without the consent of the employer. Before the expiry of ten years he was called up for military service. After the war he undertook professional engagements and was sued by the employer for breach of contract.

It was held that the contract of service had frustrated when his services were requisitioned for military purposes and thereafter he was free from the covenants of the contract.

*APPLICATION TO INDUSTRIAL RELATIONS.*—The application of the doctrine of frustration to industrial relations was examined by the (English) National Industrial Relations Court in *Marshall v Harland & Wolff Ltd.*<sup>193</sup>

*M* was in a company's employment since 1946. In 1969 he fell ill and did not attend till April 1971 when the company retrenched him after

191. (1871) LR 6 Exch 269: 40 LJ Ex 172: 24 LT 755: (1861–73) All ER Rep 699.

192. *Morgan v Manser*, (1948) 1 KB 184.

193. (1972) 1 WLR 899.

giving usual benefits. *M* had still to undergo an operation before he could resume work.

Even so it was held that the contract of service had not frustrated. The President of the court pointed out that in considering whether further performance has become impossible, regard must be had to the terms of the employment, the nature of the illness, its duration and prospects of recovery, and the period of past employment:

Where the contract provided for sick pay, there could not be frustration if the employee appeared likely to return to work within the period in which sick pay was payable. Where the employee occupied a key post which had to be filled on a permanent basis if his absence was prolonged, it was easier to infer frustration if the employee was one of the many in the same category. Again, a relationship of long standing was not so easily destroyed as one which had but a short history.

The present contract provided that no wages were payable during sickness. It was not the company's policy to dismiss employees on the ground of sickness. There was no medical evidence that *M* was permanently incapacitated or as to how long he would be away from work. In those circumstances, there was no ground for holding that further performance of his obligation in the future would be either impossible or a thing radically different from that which he had accepted under his contract of employment. Accordingly, the contract had not frustrated.

In a similar case before the Court of Appeal:<sup>194</sup>

*S* was employed as a works manager under a five-year contract. After two years he became ill and was absent from work for five months. The employer terminated the employment after four months of absence and *S* sued for breach of contract.

It was held that a five-year term contract of service could not be deemed to have frustrated by five months' illness.

##### *5. Government, administrative or legislative intervention*

A contract will be dissolved when legislative or "administrative intervention has so directly operated upon the fulfilment of the contract for a specific work as to transform the contemplated conditions of performance".<sup>195</sup> Thus, where a vendor of land could not execute the sale-deed because he ceased to be the owner by operation of law, it was held that the contract

194. *Storey v Fulham Steel Works Co Ltd*, (1907) 24 TLR 89 (CA).

195. See *McCARDIE J in Blackburn Bobbin Co v T.W. Allen & Sons*, (1918) 2 KB 467 (CA). *Army Welfare Housing Organisation v Sumangal Services (P) Ltd*, (2004) 9 SCC 619: AIR 2004 SC 1344, contractor not liable where further construction work was stopped under Municipal intervention. *T. Lakshmipathi v P. Nithyananda Reddy*, (2003) 5 SCC 150: (2003) 5 ALT 26 (SC), building alone demolished, it did not determine lease or tenancy, contract not frustrated.

had become impossible of performance.<sup>196</sup> In another case, a contract by the State to give a monopoly was held to have become void on the enforcement of the Constitution.<sup>197</sup> Similarly, a contract between certain parties for the sale of the trees of a forest was discharged when the State of Rajasthan forbade the cutting of trees in the area.<sup>198</sup> A well-known English authority is *Metropolitan Water Board v Dick Kerr & Co Ltd.*<sup>199</sup>

By a contract made in July 1914, a firm of contractors contracted with a Water Board to construct a reservoir to be completed within six months. But by a notice issued under the Defence of the Realm Acts, the contractors were required to cease work on their contract and they stopped the work accordingly. They claimed that the effect of the notice was to put an end to the contract.

The House of Lords held that the interruption created by the prohibition was of such a character and duration so as to make the contract when resumed a different contract from the contract when broken off, and that the contract had ceased to be operative.<sup>200</sup>

But an intervention of a temporary nature which does not uproot the foundation of the contract will not have the dissolving effect. This is shown by the decision of the Supreme Court in *Satyabrata Ghose v. Mugneeram Bangur & Co.*<sup>201</sup>

The defendant company started a scheme for the development of a tract of land into a housing colony. The plaintiff was granted a plot on payment of earnest money. The company undertook to construct the roads and drains necessary for making the lands suitable for building and residential purposes and as soon as they were completed, the purchaser was to be called upon to complete the conveyance by payment of the balance of the purchase money. But before anything could be done, a considerable portion of the land was requisitioned by the State during the Second World War for military purposes:

The company attempted to cancel the contract on the ground that by reason of the supervening events its performance had become impossible. MUKHERJEA J held that the contract was not frustrated. The learned judge said: "Undoubtedly the commencement of the work was delayed but was the

196. *Shiam Sunder v Durga*, AIR 1966 All 185; *Rozan Mian v Tahera Begum*, (2007) 12 SCC 175; AIR 2007 SC 2883, transfer of a particular type of tenancy was prohibited by an Act enforced during pendency of the suit. The Supreme Court held that the transfer became impossible of performance. No specific relief could be allowed.

197. *Hamara Radio and General Industries v State of Rajasthan*, AIR 1964 Raj 205.

198. *Man Singh v Khazan Singh*, AIR 1961 Raj 277.

199. 1918 AC 119 (HL).

200. See also *C. Czarnikow Ltd v Centrala Handlu Zagraniczne Rolimpex*, 1979 AC 351: (1978) 3 WLR 274 (HL), the contract of a Government Monopoly Corporation ended on ban on exports. *Syed Khursheed Ali v State of Orissa*, AIR 2007 Ori 56, beef could not be supplied under the contract because of the Orissa Prevention of Cow Slaughter Act, 1960, excused from performance, there was no volition or intentional failure of supply.

201. AIR 1954 SC 44: 1954 SCR 310.

delay going to be so great and of such a character that it would totally upset the basis of the bargain and the commercial object which the parties had in view? The requisition orders, it must be remembered, were, by their very nature, of a temporary character....”<sup>202</sup>

“If there was a definite time-limit agreed to by the parties within which the construction work was to be finished, it could be said with perfect propriety that delay for an indefinite period would make the performance of the contract impossible within the specified time and this would seriously affect the object and purpose of the venture. But where there is no time-limit whatsoever in the contract, nor even an understanding between the parties on that point and when during the war the parties could naturally anticipate restrictions of various kind which would make the carrying out of these operations more tardy and difficult than in times of peace, we do not think that the order of requisition affected the fundamental basis upon which the agreement rested or struck at the roots of the adventure.”

The effect of an administrative intervention has to be viewed in the light of the terms of the contract, and, if the terms show that the parties have undertaken an absolute obligation regardless of administrative changes, they cannot claim to be discharged. This has been so held by the Supreme Court in *Naihati Jute Mills Ltd v Khyaliram Jagannath*.<sup>203</sup>



CASE PILOT

There was an agreement to purchase raw jute to be imported from East Pakistan (now Bangladesh). The buyer was to supply the import licence within November, failing which it was to be supplied within December at the pain of a little more price and if he failed in December he was to pay the difference between the contract and market prices. The buyer applied for a licence which was refused because he had stock in his mill sufficient for two months. He applied again. He was advised this time that the rules had been changed and to obtain a licence he must show that he had used an equal quantity of Indian jute. Thus the buyer failed to supply the licence and was sued for breach. He pleaded frustration caused by the change in Government policy.

But he was held liable. SHELAT J pointed out that if the Government had completely forbidden imports, Section 56 would have applied. But the policy of the Government was that the licensing authority would scrutinise the case of each applicant on its own merit. Referring to the terms of the contract, the learned judge said:<sup>204</sup> “These clauses clearly indicate that the appellants were conscious of the difficulty of getting the licence in time.

202. *Ibid* at p. 49. Followed in *Mugneeram Bangur & Co v Gurbachan Singh*, AIR 1965 SC 1523: (1965) 2 SCR 630. *Nirmala Anand v Advent Corpn (P) Ltd*, (2002) 5 SCC 481: AIR 2002 SC 2290, agreement for purchase of a flat in a building constructed on a land leased out by the Municipality. The builder cancelled the deal saying that the Municipality had terminated the lease deed. The facts however showed that there was a possibility of renewal. The relief of specific performance was not refused to the buyer.

203. AIR 1968 SC 522: (1968) 1 SCR 821.

204. *Ibid* at p. 528; (1968) 1 SCR 821, 830.

The question would depend upon whether the contract which the appellants entered into was that they would make their best endeavours to get the licence or whether the contract was that they would obtain it or else be liable for breach of that stipulation. There is nothing improper or illegal for a party to take upon himself an absolute obligation to obtain a permit or a licence and in such a case if he took the risk, he must be held bound to his stipulation.”

The Learned Judge relied upon the following observation of Lord SUMNER in *Bank Line Ltd v Arthur Capel & Co*:<sup>205</sup> “Where the contract makes provision (that is, full and complete provision, so intended) for a given contingency, it is not for the court to import into the contract some other different provisions for the same contingency called by different name.”

Where the intervention makes the performance unlawful, the courts will have no choice but to put an end to the contract. This kind of situation was before the Supreme Court in *Boothalinga Agencies v V.T.C. Poriaswami Nadar*.<sup>206</sup>

The defendant had a licence to import chicory for manufacturing coffee powder. The licence was subject to the condition that he would use the chicory only in his factory. He agreed to sell the whole shipload to the plaintiff. Before the arrival of the ship, the sale of such imported goods was banned.

The contract was accordingly held to have become void. “It was, however, argued on behalf of the respondent that, in any event, the appellant could have purchased chicory from the open market and supplied it to the respondent in terms of the contract.” RAMASWAMI J rejected this argument:

Under the contract the quality of chicory to be sold was the chicory of specific description—“Egberts chicory, packed in 495 wooden cases, each case containing 2 tins of 56 lb nett”. It is manifest that the contract was for the sale of certain specific goods and it was not open to the appellant to supply chicory of any other description.<sup>207</sup>

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205. 1919 AC 435 (HL).

206. AIR 1969 SC 110: (1969) 1 SCR 65. *CIT v A.K. Menon*, (1996) 6 Bom CR 564, penalties and interest under the Income Tax Act not allowed to be levied on a person who could not pay tax amount in advance because of restrictions imposed upon him under the Special Court (Trial of Offences Relating to Transactions in Securities) Act, 1992.

207. *B.S. Vedera v Union of India*, AIR 1969 SC 118. *Malikarjunappa Basavalihgappa Mamle Desai v Siddalingappa*, (1973) 3 SCC 180: AIR 1973 SC 190. Frustration does not apply to licences. See *Sunnam Satish v State*, AIR 1980 AP 18. An auction for the sale of trust property was held to have been frustrated on a stay order being issued by a court. *Shanti Vijay and Co v Princess Fatima Fouzia*, (1979) 4 SCC 602: AIR 1980 SC 17. Contracts for export of silver were deemed to have ended with the ban on export of silver. *Union of India v C. Damani & Co*, 1980 Supp SCC 707: AIR 1980 SC 1149. Frustration by the Government taking over an oil concession. *B.P. Exploration Co (Libya) Ltd v Hunt (No. 2)*, (1979) 1 WLR 783 (QB). Frustration by the court staying the performance of a contract. *Shanti Vijay and Co v Princess Fatima Fouzia*, (1979) 4 SCC 602: AIR 1980 SC 17.

Where Development Authority allotted land to a builder for housing development, but Forest Authority did not permit because the land was in the ridge area of the protected forest, the contract was held to have ended by impossibility. The builder was allowed refund of the entire money paid under the contract with 6 per cent interest.<sup>208</sup>

#### 6. Intervention of war

Intervention of war or warlike conditions in the performance of a contract has often created difficult questions. The closure of the Suez Canal following the Anglo-French war with Egypt, for instance, interrupted the performance of many contracts. One such case was *Tsakioroglou & Co Ltd v Noblee & Thorl GMBH*.<sup>209</sup> The following statement of facts was given by Lord REID:

The appellants agreed to sell to the respondents three hundred tons of Sudan groundnuts *c.i.f.* Hamburg. The usual and normal route at the date of the contract was *via* Suez Canal. Shipment was to be in November/December, 1956, but, on November 2, 1956, the Canal was closed to traffic and it was not reopened until the following April. It is stated that the appellants could have transported the goods *via* the Cape of Good Hope. The appellants refused to ship goods *via* the Cape. The question now is whether by reason of the closing of the Suez route, the contract had been ended by frustration.

The appellant's argument was that it was an implied term of the contract that shipment should be via Suez. But it was held that such a term could not be implied. The customary or usual route via the Suez Canal being closed, the appellants were bound [by the Sale of Goods Act, 1893, S. 32(2)] to ship the groundnuts by a reasonable and practical route and, though the appellants might be put to greater expense by shipping the groundnuts via the Cape of Good Hope, that did not render the contract fundamentally or radically different, and there was not, therefore, frustration of the contract.<sup>210</sup>

If the intervention of war is due to the delay caused by the negligence of a party, the principle of frustration cannot be relied upon.<sup>211</sup>

If there are more than one ways of performing a contract and the war cuts off only one of them, the party is still bound to perform by the other way, however inconvenient or expensive. This appears from the decision of the Privy Council in *Twentsche Overseas Trading Co Ltd v Uganda Sugar Factory Ltd*.<sup>212</sup> There was a contract for supplying "Krupps" steel rails. The rest of the facts appear from the following words of Lord WRIGHT: "The

208. *DDA v Kenneth Builders & Developers Ltd*, 2016 SCC OnLine SC 627: (2016) 230 DLT 706.

209. 1962 AC 93: (1961) 2 WLR 633.

210. See also *Ocean Tramp Tankers Corp v VO Sorfracht, The Eugenia*, (1964) 2 QB 226: (1964) 2 WLR 114, which is another Suez case of the same kind.

211. *Gambhir Mull Mahabirprasad v Indian Bank Ltd*, AIR 1963 Cal 163.

212. AIR 1945 PC 144.

appellant claimed that the rails specified under the contract were to be rails manufactured by a German firm and by that firm only. On this they based their claim to be excused from their failure to deliver the goods because to do so would have involved a dealing with alien enemies due to the outbreak of World War II and hence the performance of the contract became impossible and illegal."

Their Lordships held that it was not open to the supplier to invoke the doctrine of frustration. There was nothing in the contract which called for the rails to be obtained from Germany only. The reference to "Krupps" did not indicate a source of supply, but merely a specification of the rails. There were many other sources of supply, and the contract left the supplier with a free hand in the matter.

In a case before the Patna High Court,<sup>213</sup> the further performance of a contract of life insurance had become impossible because the insurer was a German company and on the outbreak of war its business was closed by the Government of India and the disposal of pending policies was handed over to a firm of chartered accountants. The assured was accordingly allowed to recover the money paid by him under the policy. In a Calcutta case, a contract of carriage by river was intercepted by the enemy seizing the boat along with cargo during hostilities between India and Pakistan. The court allowed the carrier the plea of impossibility.<sup>214</sup>

## 7. Application to leases

**ENGLISH CASES.**—The question whether the doctrine of frustration applies to a lease of land is not yet finally settled in England. In the leading case of *Crickelwood Property & Investment Trust Ltd v Leighton's Investment Trust Ltd*<sup>215</sup> which came before the House of Lords, the decision was unanimous that on the facts of the case, irrespective of any controversy, frustration would not have arisen because a lease for 99 years cannot be said to have been upset by a few years' disturbance, but contradictory opinions were expressed.

A building lease was executed for ninety nine years, more rent being payable after erection of buildings. But before any could be erected and while the lease had still 90 years to run, building activity was suspended by the Government because of the war.

Viscount SIMON LC said:

The lease at the time had more than ninety years to run, and though we do not know how long the present war, and the emergency regulations which have been made necessary by it, are going to last, length of the interruption so caused is presumably a small fraction of the whole term.

213. *A.F. Ferguson & Co v Lalit Mohan Ghose*, AIR 1954 Pat 596.

214. *Basanti Bastralaya v River Steam India Navigation Co Ltd*, AIR 1987 Cal 271.

215. 1945 AC 221 (HL).

Here, the lease itself contemplates that rent may be payable although no building is going on, and I cannot regard the interruption which has arisen as such as to destroy the identity of the arrangement or to make it unreasonable to carry out the lease according to its terms as soon as the interruption in building is over.

But his Lordship was not prepared to accept the view that because a lease is more than a contract and amounts to an estate, therefore, it can never end prematurely by frustration, for example, where the subject-matter of the lease is swallowed by some vast concussion of nature or buried in the depth of the sea. "Suppose, for example", his Lordship continued, "that legislation were subsequently passed which permanently prohibited private building in the area, or dedicated it as an open space forever, why should this not bring to an end the currency of a building lease, the object of which is to provide for the erection on the area, for the combined advantage of the lessor and lessee of buildings which it would now be unlawful to construct."

Referring to the previous authorities, Viscount SIMON LC characterised it as erroneous to suppose that there is authority binding on the House of Lords to the effect that a lease cannot in any circumstances be ended by frustration. In *Matthey v Curling*.<sup>216</sup>

There was the demise of a house for twenty-one years. The lesser had to keep the building in repair, to insure and in case of any destruction by fire etc. to expend the insurance money in rebuilding. In 1918 the military authorities took possession of the premises and remained in possession until the expiry of the lease. In February, 1919, the house was destroyed by fire and in March the terms of the lease expired. It was held by the House of Lords affirming the majority decision of the Court of Appeal, (ATKIN LJ having dissented) that the lessee was liable both for repairs and for rent even during the period of dispossession.

Commenting upon this case, Viscount SIMON LC said: "The decision there was that requisitioning by the Government was no answer to a claim on the covenant for rent, any more than ouster by a trespasser would be: the remedy of the tenant was against the Government for compensation. Equally, destruction by fire, after the Government had requisitioned the place, left the tenants still liable on his covenant to deliver up in proper condition, for the tenant could have covered the risk by insurance. His Lordship also pointed out that the Court of Appeal was mistaken about *Matthey v Curling* as a clear authority that the doctrine of frustration cannot be applied to a demise of real property. His Lordship quoted with approval the statement from the dissenting judgment of ATKIN LJ in which his Lordship said that there is no legal absurdity in implying a term that a lease shall be determined absolutely on the happening of an event which in an ordinary contract works as a frustration. Lord WRIGHT also expressed the same view.

216. (1922) 2 AC 180 (HL).

But Lords RUSSEL and GODDARD expressed the contrary view. Lord RUSSEL proceeded as follows: "A lease is much more than a contract. It creates and vests in the lessee an estate or interest in the land, a chattel interest, it is true, but a vested estate or interest nonetheless." As was said by LUSH J in *London & Northern Estates Co v Schlesinger*:<sup>217</sup> "It is not correct to speak of this tenancy as a contract and nothing more. A term of years was created by it and vested in the appellant, and I can see no reason for saying that because this Order (the lessee being a German was ordered not to stay in the premises during the war) disqualified him from personally residing in the flat it affected the chattel interest which was vested in him by virtue of the agreement. In my opinion, it continues vested in him still...."

"When a contract is frustrated it is because what is called the 'venture' or 'undertaking' which the parties have contracted to engage in, can no longer be carried out. The court in such circumstances declares the contract to be no longer binding on the parties. That is the end of the matter. But when a lease is in question, it is the lease which is the 'venture' or 'undertaking' upon which the parties have embarked. The contractual obligations thereunder of each party are merely obligations which are incidental to the relationship of landlord and tenant created by the demise and which necessarily vary with the character and duration of the particular lease. It may well be that circumstances may arise during the currency of the term which render it difficult, or even impossible, for one party or the other to carry out some of its obligations as landlord and tenant—circumstances which might afford a defence to a claim for damages for their breach—but the lease would remain."

"The position would, therefore, seem to be that unless the matter is decided by the House of Lords, the decisions of the Court of Appeal represent the law and their effect is that "the doctrine is excluded in the case of a lease".

In the still subsequent case of *National Carriers Ltd v Panalpina (Northern) Ltd*<sup>218</sup> the House of Lords have reiterated that the doctrine of frustration was in principle applicable to leases, though the cases in which it could properly be applied were likely to be rare. Restating the basis of the application of the doctrine of frustration, their Lordships said that the frustration of a contract occurs when the nature of the outstanding rights and obligations are so significantly damaged by some supervening event from what the parties could reasonably have contemplated at the time of the execution that it would be unjust to hold them to the performance. Quite naturally, such a change in the rights and obligations under a lease is likely to be of rare occurrence. The facts of the case were:

A warehouse was demised to the defendant for a period of ten years. The premises were not to be used for any other purpose than warehousing

217. (1916) 1 KB 20.

218. 1981 AC 675: (1981) 2 WLR 45 (HL).

unless it was with the lessor's consent. The only vehicular access to the warehouse was by a street which the local authority closed because of the dangerous condition of a derelict Victorian warehouse opposite to that demised to the defendants. The period between the closure of the street and its reopening after demolition of the Victorian-warehouse was likely to be about 20 months. During that period the demised warehouse was rendered useless for the defendants' purposes. They refused to pay any further rent as they claimed that the lease had frustrated.

But they were held liable. The nature of the transaction and the obligations created by it had not significantly changed. Having regard in particular to the likely length of continuance of the lease after the interruption of user in relation to the term originally granted, on the facts the defendants had failed to raise a triable issue as to the applicability of the doctrine of frustration.

*INDIAN CASES.*—In India the question was considered by the Supreme Court in *Raja Dhruv Dev Chand v Raja Harmohinder Singh*,<sup>219</sup> where SHAH J (afterwards CJ) at once observed: "Authorities in the courts in India have generally taken the view that Section 56 of the Contract Act is not applicable when the rights and obligations of the parties arise under a transfer of property under a lease".

It was one of the cases arising out of the partition of the country into India and Pakistan. The lease in question was that of an agricultural land for one year only. The rent was paid and the lessee was given possession. Before the land could be exploited for any crops, came partition which left the land in Pakistan and the parties migrated to India. The action was to recover the rent paid.

But no such recovery was allowed. SHAH J who spoke on behalf of himself and RAMASWAMI and MITTER JJ pointed out that completed transfers are completely outside the scope of Section 56.

In a case before the Allahabad High Court,<sup>220</sup> the roofs of a premises which was leased out collapsed owing to their dilapidated condition and heavy rains and required new construction, that was not taken to be a frustration of the lease.

On the other hand, where on account of an event beyond the parties' control, the lessor is not able to transfer possession to the lessee, the lessee would be entitled to take back his rent. This was so held by the Punjab High Court in *Gurdashan Singh v Bishen Singh*.<sup>221</sup> To this extent the Supreme Court approved the decision, but the observation of the High Court that "the broad principle of frustration of contracts applies to leases" was

219. AIR 1968 SC 1024: (1968) 3 SCR 339.

220. *Shyam Kumari v Ejaz Ahmad Ansari*, AIR 1977 All 376.

221. (1962) 2 Punj 5 (FB).

rejected, SHAH J saying: “We are unable to agree with that observation.” The learned judge continued:

Under a lease of land there is a transfer of right to enjoy that land. If any material part of the property be wholly destroyed or rendered substantially and permanently unfit for the purpose for which it was let out, because of fire, tempest, floods, violence of any army or a mob, or other irresistible force, the lease may at the option of the lessee be avoided. This rule is incorporated in Section 108(c) of the Transfer of Property Act. Where the property leased is not destroyed or rendered substantially and permanently unfit, the lessee cannot avoid the lease because he does not or is unable to use the land for the purpose for which it is let out to him.<sup>222</sup>

In the subsequent case of *Sushila Devi v Hari Singh*,<sup>223</sup> the Supreme Court held that: “In the instant case there is no concluded contract since no deed was written or registered. It was an agreement to lease and that came within the scope of Section 56. There was frustration of the contract as the parties could not go to Pakistan to give or take possession.”

The Jammu and Kashmir High Court allowed in *Hari Singh v Dewani Vidyawati*<sup>224</sup> the recovery of rent paid in advance under a lease which could not be completed on account of partition. The recovery was allowed under Section 65 as benefits received under a contract which became void.

The impossibility must be such that kills the contract itself and not merely one that keeps the contract alive and capable of being performed at a further date. The contract in this case was for waterproofing. The work was assigned to the contractor without the wishes of house allottees. The allottees were already in possession. They did not allow the contractor to do the work. The court held that it could not be said that performance had become impossible. The arbitral tribunal rightly awarded damages to the contractor. Security deposit was ordered to be refunded and damages awarded covered miscellaneous expenses and wages paid to idling labour.<sup>225</sup>

## Theories of frustration

Many possible explanations have been put forward as a justification for the doctrine of frustration as a part of the law of contract. Two theories are most well-known.

### 1. Theory of implied term

The theory of implied term was explained by Lord LOREBURN in *F.A. Tamplin Steamship Co Ltd v Anglo-Mexican Petroleum Products Co Ltd*<sup>226</sup> in these words:

222. See also *Mahadeo Prosad Shaw v Calcutta Dyeing & Cleaning Co*, AIR 1961 Cal 70.

223. (1971) 2 SCC 288 at pp. 291–92; AIR 1971 SC 1956.

224. AIR 1960 J&K 91.

225. *Gujarat Housing Board v Vipul Corp*n, AIR 2004 Guj 319.

226. (1916) 2 AC 397, 408.

A Court can and ought to examine the contract and the circumstances in which it was made, not of course to vary, but to explain it, in order to see whether or not from the nature of it the parties must have made their bargain on the footing that a particular thing or state of things would continue to exist. And if they must have done so, then a term to that effect will be implied, though it be not expressed in the contract.... It is in my opinion the true principle, for no Court has absolving power, but it can infer from the nature of the contract and the surrounding circumstances that a condition which was not expressed was a foundation on which the parties contracted. ... Were the altered conditions such that, had they thought of them, they would have taken their chances of them, or such that as sensible men they would have said: "If that happens, of course, it is all over between us"?

This explanation of the doctrine of frustration has been constantly cited in a large number of decisions. But it has also been criticised as something unreal. For instance, Lord WRIGHT said in a case:<sup>227</sup> "To my mind the theory of the implied condition is not really consistent with the true theory of frustration. It has never been acted on by the court as a ground of decision, but is merely stated as a theoretical explanation." "The court has formulated the doctrine by virtue of its inherent jurisdiction, just as it has developed the rules of liability for negligence, or for the restitution or repayment of money where otherwise there would be unjust enrichment. I find the theory on the basis of the rule in the pregnant statement of Lord SUMNER that the doctrine of frustration is really a device by which the rules as to absolute contracts are reconciled with the special exceptions which justice demands".<sup>228</sup> In another case<sup>229</sup> his Lordship said: "In ascertaining the meaning of the contract and its application to the actual occurrences, the court has to decide, not what the parties actually intended but what as reasonable men they should have intended. The court personifies for this purpose the reasonable man."

## 2. Just and reasonable solution

In a subsequent case<sup>230</sup> DENNING LJ attempted to explain the doctrine of frustration on a different basis. He said: "The court really exercises a qualifying power—a power to qualify the absolute, literal or wide terms of the contract—in order to do what is just and reasonable in the new situation. The day is done when we can excuse an unforeseen injustice by saying to the sufferer 'it is your own folly, you ought not to have passed that form of words, you ought to have put in a clause to protect yourself'. We no longer credit a party with the foresight of a Prophet or his lawyer with the draftsmanship of a Chalmers." But this statement was not approved when the case

227. *Denny, Mott & Dickson Ltd v James B. Fraser & Co Ltd*, 1944 AC 265, 275 (HL).

228. *Hirji Mulji v Cheong Yue S.S. Co Ltd*, 1926 AC 497 (PC).

229. *Joseph Constantine Steamship Line Ltd v Imperial Smelting Corp Ltd*, 1942 AC 154 (HL).

230. *British Movietone news Ltd v London & District Cinemas Ltd*, 1952 AC 166 (HL).

went before the House of Lords. The observation of Lord LOREBURN that “no court has an absolving power”, was re-emphasised. Viscount SIMON said: “The principle remains the same. Particular applications of it may greatly vary and theoretical lawyers may debate whether the rule should be regarded as arising from implied term or because the basis of the contract no longer exists. In any view it is a question of ‘construction’ as Lord WRIGHT pointed out in *Joseph Constantine Steamship Line Ltd v Imperial Smelting Corp*n Ltd<sup>231</sup> and as has been repeatedly asserted by other masters of law.”<sup>232</sup>

### Theories not applicable in India

Referring to the theories B.K. MUKHERJEA J of the Supreme Court said in *Satyabrata Ghose v Mugneeram Bangur & Co*<sup>233</sup> “These differences in the way of formulating legal theories really do not concern us so long as we have statutory provision in the Indian Contract Act. In deciding cases in India, the only doctrine that we have to go by is that of supervening impossibility or illegality as laid down in Section 56 of the Contract Act, taking the word ‘impossible’ in its practical and not literal sense. It must be borne in mind, however, that Section 56 lays down a rule of positive law and does not leave the matter to be determined according to the intention of the parties.”

### Effects of frustration

“It is well-settled that if and when there is frustration the dissolution of the contract occurs automatically. It does not depend, as does rescission of a contract, on the ground of repudiation or breach, or on the choice or election of either party. It depends on the effect of what has actually happened on the possibility of performing the contract.”<sup>234</sup>

#### 1. Frustration should not be self-induced

Explaining the principle that frustration should not be self-induced, Lord WRIGHT said in *Maritime National Fish Ltd v Ocean Trawlers Ltd*.<sup>235</sup>

“The essence of ‘frustration’ is that it should not be due to the act or election of the party. There does not appear to be any authority which has been decided directly on this point.” There is, however, a reference to the question in the speech of the Lord SUMNER in *Bank Line Ltd v Arthur Capel & Co*.<sup>236</sup> What he says is: “I think it is now well-settled that the principle of frustration of an adventure assumes that the frustration arises without

231. 1942 AC 154 (HL).

232. *British Movietonews Ltd v London & District Cinemas Ltd*, 1952 AC 166 (HL).

233. AIR 1954 SC 44: 1954 SCR 310.

234. Per Lord WRIGHT in *Denny, Mott & Dickson Ltd v James B. Fraser & Co Ltd*, 1944 AC 265 (HL). Cited by MUKHERJEA J in *Satyabrata Ghose v Mugneeram Bangur & Co*, AIR 1954 SC 44: 1954 SCR 310.

235. 1935 AC 524 (PC).

236. 1919 AC 435 (HL).

blame or fault on either side. Reliance cannot be placed on a self-induced frustration.”<sup>237</sup>

In *Maritime National Fish Ltd v Ocean Trawlers Ltd*<sup>238</sup> the facts were:

The appellants hired the respondents’ trawler, called the “*St. Cuthbert*” to be employed in fishing industry only. Both parties knew that the trawler could be used for that purpose only under a licence from the Canadian Government. The appellants were using five trawlers and, therefore, applied for five licences. Only three were granted and the Government asked the appellants to name three trawlers and they named trawlers other than the *St. Cuthbert*. They then repudiated the charter and pleaded frustration in response to the respondents’ action for the hire.

The Judicial Committee of the Privy Council held that the frustration in this case was the result of the appellants’ own choice of excluding the respondents’ ship from the licence and, therefore, they were not discharged from the contract.<sup>239</sup>

In another similar case, the contract was to export 1500 tons of sugar beet pulp pellets with a further option for the same quantity. The sellers obtained an export licence for 3000 tons. They also contracted with another buyer to supply him 1500 tons. But the Government refused to grant any further licences. They shipped the whole agreed quantity to the first buyer.<sup>240</sup> They were now left with the export licence for 1500 tons only, but were under two obligations, one to supply 1500 tons to the first buyer under the option given to him and other under the contract with the second buyer for the same quantity. As a face saving device they apportioned the supply between the two buyers giving about half to either. The second buyer sued for breach of contract.<sup>241</sup> The suppliers pleaded frustration. They were held liable. The Court of Appeal found no legal authority justifying the proposition that where a seller has a legal commitment to A and a non-legal commitment to B and he can honour the obligation to A or to B but not to both, he is justified in partially honouring both obligations.<sup>242</sup> The court referred to the principle stated in the American Uniform Commercial Code<sup>243</sup> that in such a situation the seller may allocate supplies in any manner which is reasonable and fair, but found no basis for importing the principle into English law. There is, however, an English authority to the effect that if the seller had been under a legal duty, he would have been justified in making fair apportionment. The court said that when a supplier has many contracts

237. *Sushila Devi v Hari Singh*, (1971) 2 SCC 288: AIR 1971 SC 1956.

238. 1935 AC 524 (PC).

239. Followed in India in *Jwala Prasad v Jwala Bank Ltd*, AIR 1957 All 143 and considered: *V.L. Narasu v P.S.V. Iyer*, AIR 1953 Mad 300.

240. *Satyabrata Ghose v Mugneeram Bangur & Co*, AIR 1954 SC 44, 48: 1954 SCR 310.

241. *Maritime National Fish Ltd v Ocean Trawlers Ltd*, 1935 AC 524 (PC).

242. *Pancommerce S.A. v Veecheema B.V.*, (1983) 2 Lloyd's Rep 304 (CA).

243. Para 2-615.

to fulfil, but only has enough of the goods to fulfil one of them, then, if he reasonably appropriates what he has to that one, he can rely on *force majeure* as to others. Thus, there is no principle of law preventing one party to a contract taking advantage of its own acts to defeat the other's rights unless the party is in breach of duty in so acting. Where the defendant company having the right to do so and lawfully exercising that right, sold its subsidiary with the result that the employees' stock options lapsed, the defendant company was held not liable for the lapse because it was under no duty not to sell its subsidiary.<sup>244</sup>

In order to attract the principle that a party is not entitled to rely on his own act in not fulfilling a condition subsequent and thereby bringing a contract to an end, the act has to amount to a breach of duty owed to the other party under the contract. If a term cannot be implied into a contract that a party would not do an act which, if done, would prevent the fulfilment of a condition precedent or would cause a condition subsequent to be fulfilled, the contract takes effect according to its tenor.

Applying this principle to the case of a company which offered shares to its own employees and to those of its subsidiary and after an employee of a subsidiary had accepted the offer, the company's subsidiary was sold to a bidder and the employee was informed that the scheme lapsed but he sued the company for breach of contract, the court came to the conclusion that the company was not, by reason of the scheme, under a duty not to deal with the undertaking of the subsidiary in a way that would frustrate the scheme.<sup>245</sup>

## 2. Frustration operates automatically

Frustration operates automatically to discharge the contract "irrespective of the individuals concerned, their temperaments and failings, their interest and circumstances".<sup>246</sup> "The legal effect of frustration does not depend on their intention or their opinions, or even knowledge, as to the event."<sup>247</sup> "The belief, knowledge and intention of the parties are evidence, but evidence only on which the court has to form its conclusion whether the changed circumstances destroyed altogether the basis of the adventure and its underlying object."<sup>248</sup> This is particularly true of Indian law as Section 56 of the Contract Act "lays down a rule of positive law and does not leave the matter to be determined according to the intention of the parties."

244. *Thompson v ASDA-MFI, Group plc*, (1988) 2 WLR 1093; *Alghussein Establishment v Eton College*, (1988) 1 WLR 587 (HL).

245. *Thompson v ASDA-MFI, Group plc*, (1988) 2 WLR 1093.

246. Lord LOREBURN in *Davis Contractors Ltd v Fareham Urban Distt Council*, 1956 AC 696, 715: (1956) 3 WLR 37 (HL).

247. Lord LOREBURN in *ibid*, citing from *Dahl v Nelson*, (1881) LR 6 AC 38, *per* Lord WATSON.

248. MUKHERJEA J in *Satyabrata Ghose v Mugneeram Bangur & Co*, AIR 1954 SC 44: 1954 SCR 310.

A case, however, shows that in certain circumstances frustration may be waived by one party and then the other will be bound by the contract. In *HR & S Sainsbury Ltd v Street*:<sup>249</sup>

There was the sale of 275 tons (5 per cent more or less) of feed barley to be grown on seller's land. The crop amounted to only 140 tons. The seller resold it to another and contended that he had the right to do so because the contract had ended by frustration.

But he was held liable for breach of contract. There was frustration only to the extent of crop failure. The buyer could waive it and claim delivery of whatever little crop the seller's land had produced.<sup>250</sup>

The Supreme Court has laid down that frustration puts an end to the liability to perform the contract. It does not extinguish the contract for all purposes. For example, whether the doctrine of frustration would apply or not has to be decided within the framework of the contract and, if the contract contains an arbitration clause, the arbitrator could decide the matter of frustration.<sup>251</sup>

### 3. Adjustment of rights

The rights of the parties are adjusted under Section 65 of the Act.

**S. 65. Obligation of person who has received advantage under void agreement, or contract that becomes void.**—When an agreement is discovered to be void, or when a contract becomes void, any person who has received any advantage under such agreement or contract is bound to restore it, or to make compensation for it, to the person from whom he received it.

#### *Illustrations*

- (a) A pays B 1000 rupees in consideration of B's promising to marry C, A's daughter. C is dead at the time of the promise. The agreement is void, but B must repay A the 1000 rupees.
- (b) A contracts with B to deliver to him 250 maunds of rice before the first of May. A delivers 130 maunds only before that day, and none after. B retains the 130 maunds after the first of May. He is bound to pay A for them.
- (c) A, a singer, contracts with B, the manager of a theatre, to sing at his theatre for two nights in every week during the next two months, and B engages to pay her a hundred rupees for each night's performance. On the sixth night, A wilfully absents herself from the theatre, and B, in consequence, rescinds the contract. B must pay A for the five nights on which she had sung.
- (d) A contracts to sing for B at a concert for 1000 rupees, which are paid in advance. A is too ill to sing. A is not bound to make compensation to B for the loss of the profits which B would have made if A had been able to sing, but must refund to B the 1000 rupees paid in advance.

249. (1972) 1 WLR 834.

250. See G.D. Goldberg, "Is Frustration Invariably Automatic?", (1972) 88 LQR 464.

251. *Naihati Jute Mills Ltd v Khyaliram Jagannath*, AIR 1968 SC 522; (1968) 1 SCR 821. Liability under S. 65 also survives. *Bombay Dyeing & Mfg Co Ltd v State of Bombay*, AIR 1958 SC 328: 1958 SCR 1122.

The effect of the principle laid down in the section is that when the parties have entered into an apparently valid contract and some benefits have been passed under it, and subsequently the contract is either discovered to be void or becomes void, the party who has received the benefits must restore them to the other.<sup>252</sup> Thus, the section does not apply to a contract which the parties knew at the time of making it to be void.<sup>253</sup> The section also does not apply to a case where the benefits are passed at a time when the contract has, though unknown to the parties, already ceased to be enforceable. This was the position in *Jagadish Prosad Pannalal v Produce Exchange Corp Ltd.*<sup>254</sup>

There was a contract for the sale of one wagon of maize starch at the rate of Rs 77 per cwt., the control price being Rs 78. The goods were delivered on January 3 and paid for. A few days earlier, viz. on December 16, a new order was passed by the Government making Rs 48 as the price and this was to apply to all contracts in which delivery was to be given on or after January 1. The buyer brought an action to recover the difference between the revised control price and the price he paid.

The court agreed with him to this extent that the contract had become void by the change in the control price and, therefore, neither party was compellable to perform, but that the buyer, having paid up, was not entitled to any refund under Section 65. For this section to apply the advantage must have been received under "contract", whereas, in the present case, the excess price was paid after the contract had already become void and ceased to be enforceable.<sup>255</sup>

#### *Discovered to be void*

The first part is concerned with an agreement which never amounted to a contract, it being void *ab initio*. But the parties discovered this at a later stage. "The word 'discovered' connotes the pre-existence of that which is discovered". This will cover cases of "initial mistake". Where for example, money is paid for the sale of goods, which unknown to the parties, have already perished at the time, the money is refundable. The principle will apply whether the agreement is void by reason of law or by reason of facts.<sup>256</sup>

252. Action for recovery or restitution of amount paid has to be filed within three years from the date on which contract ceases to be enforceable, *Amri Devi v Ridmal*, AIR 1998 Raj 25.

253. *Joginder Singh v Registrar of Coop Societies*, AIR 1965 J&K 39. See also *Naibati Jute Mills Ltd v Khyaliram Jagannath*, AIR 1968 SC 522: (1968) 1 SCR 821. Subsequent restrictions not rendering the contract void.

254. ILR (1945) 2 Cal 41: AIR 1946 Cal 245.

255. *Rama Iyer v Jacob*, (2003) 3 KLT (SN), excavation work, 36 per cent completed, further stopped by Government intervention, plaintiff entitled to recover only such amount for which working had been completed. *Polymat India (P) Ltd v National Insurance Co Ltd*, (2005) 9 SCC 174: AIR 2005 SC 286, terms of the policy of insurance could not be departed from.

256. *Uttamchand v Mohandas*, AIR 1964 Raj 50. This principle was also applied to a case in which certain non-existent vehicles happened to be insured by mistake. The premium paid was held to be refundable, *New India Assurance Co Ltd v Itty Kurian*, (1997) 2 KLT 830.

Thus, for example, where a minor gave a shop under a partnership to the defendant, the agreement being void, it was held that he could recover back the shop. "The intention of Section 65 is to prevent a party to a void agreement to retain benefits received under it."<sup>257</sup> Similarly, consideration given on a promissory note which was not enforceable for inadequacy of stamps, was held to be refundable.<sup>258</sup> Likewise, the money paid under a contract with a municipality not executed in the manner laid down by the Municipal Act, was held to be refundable.<sup>259</sup> Payment made in advance to a contractor under a contract which is not in accordance with Article 299(1) of the Constitution relating to Government contracts has been allowed by the Orissa High Court to be recovered back under Section 65 of the Contract Act.<sup>260</sup> Payment received by a person for proposed sale of land which he had no right to sell, had to be returned by him to the other party.<sup>261</sup> Taxes realised by a contractor under the authority of State were held to be refundable to the tax-payers when it turned out that the levy itself was invalid.<sup>262</sup> Money paid to a person for purchasing his right of reversion, which is not transferable, being merely an expectancy, was held by the Privy Council to be refundable with 6 per cent interest from the date of suit.<sup>263</sup> Sir LAWRENCE JENKINS examined the scope of the section: "The section deals with (a) agreements and (b) contracts. The distinction between them is apparent from Section 2. By clause (e) every promise and every set of promises forming the consideration for each other is an agreement, and by clause (h) an agreement enforceable by law is a contract. Section 65, therefore, deals with (a) agreements enforceable by law, and (b) with agreements not so enforceable. By clause (g) an agreement not enforceable by law is said to be void."

"An agreement, therefore, discovered to be void is one discovered to be not enforceable by law, and on the language of the section, would include

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The court followed *Kuju Collieries Ltd v Jharkhand Mines Ltd*, (1974) 2 SCC 533: AIR 1974 SC 1892.

257. In such cases, the party seeking relief has to restore the benefits, if any, obtained by him. Thus a minor seeking restoration of his lands disposed of by his mother was required to refund the sale price of which he had the benefit. *Devinder Singh v Shiv Kaur*, AIR 1970 Punj 549. *Rashamoy Chowdhury v Anil Krishna Dawn*, (1998) 1 Cal LJ 295, where a partnership was discovered to be void, the property contributed by a partner was allowed to be recovered.
258. *Mohd Jamal Sahab v Munwar Begam*, AIR 1964 AP 188.
259. *Kishangarh Municipality v Maharaja Kishangarh Mills Ltd*, AIR 1961 Raj 6.
260. *State of Orissa v Rajballav Misra*, AIR 1976 Ori 19.
261. *Orissa SEB v Indian Metals & Ferro Alloys Ltd*, AIR 1991 Ori 59.
262. *Town Area Committee v Rajendra Kumar*, AIR 1978 All 103: 1978 ALR 78. The holder of a forged promissory note cannot recover anything under the note, but he can recover his money under S. 65 if he himself was not a party to the forgery. *Brij Basi v Moti Ram*, AIR 1982 All 323. Non-compliance of the requirements of the U.P. Municipalities Act renders the contract void *ab initio*. S. 65 applied giving the Municipality the right to recover Tehbazari dues collected by the contractor. *Ishwar Dayal Hingwasia v Rath Municipality*, AIR 1980 All 143.
263. *Harnath Kaur v Indar Bahadur Singh*, (1922-23) 50 IA 69 PC: AIR 1922 PC 403.

an agreement that was void in total sense from its inception as distinct from a contract that becomes void."

Applying these principles to the facts of the case their Lordships observed that the agreement was manifestly void from its inception but the parties were not able to know of this fact till the demand for the property was resisted.

Where the Orissa High Court found that the plaintiff who advanced money to the defendant for supply of paddy was not aware on the date of the agreement that it was in violation of law,<sup>264</sup> his suit for refund of money was allowed.<sup>265</sup> The Supreme Court allowed recovery under the category "discovered to be void" of the amount of earnest money which was paid for purchasing a piece of land. The agreement turned out to be void because the seller thought he was receiving the price at the rate of per *kanal* whereas the buyer was under the impression that he was paying the price per *bigha*.<sup>266</sup> Where it was discovered that the party who had agreed to sell property and had received advance, had no title to the property, the party receiving the advance was held to be under an obligation to refund the amount. The contract was void *ab initio* but discovered by the parties subsequently. The obligation to refund exists even where there is no provision in the agreement to that effect. The obligation is founded on the equitable principle of restitution and prevention of unjust enrichment.<sup>267</sup> A lady advocate acting as an Assistant District Counsel on the request of the District Magistrate was allowed to recover her remuneration for the working period even though the appointment was discovered to be void under Section 24(2) of the Criminal Procedure Code, 1973.<sup>268</sup>

The party to a void contract would still be entitled to institute a suit for specific enforcement and in the alternative to pray for refund of money paid under it. Rejection of the plaint was not proper.<sup>269</sup>

A Zila Parishad awarded to the highest bidder the contract of collecting entry fee from vehicles. The contractor did not account for to the Parishad for a part of the collection and took shelter behind the illegality of such authorisation. The court allowed recovery but not in the manner of recovering as arrears of land revenue.<sup>270</sup>

264. Orissa Rice and Paddy Control Order, 1965.

265. *Fakir Chand Seth v Dambarudhar Bania*, AIR 1987 Ori 50, following the observations of the Supreme Court in *Kuju Collieries Ltd v Jharkhand Mines Ltd*, (1974) 2 SCC 533: AIR 1974 SC 1892 and dissenting from *Bhaskarao Jageshwarrao Buty v Saru Jadharao Tumble*, AIR 1978 Bom 322.

266. *Tarsem Singh v Sukhmander Singh*, (1998) 3 SCC 471: AIR 1998 SC 1400.

267. *M. Venkatesh v Kishore Jataram*, (1999) 2 Kant LJ 535.

268. *Indu Mehta v State of U.P.*, AIR 1987 All 309.

269. *Govind Goverdhanas Daga v Field Mining & Ispat Ltd*, (2009) 6 Mah LJ 398.

270. *Surendra Kumar Rai v Zila Parishad Jhansi*, AIR 1997 All 387. S. 65 was held to be not applicable to a situation in which at the time of entering into the agreement the parties were aware of the fact that the agreement was opposed to a particular provision of law. The respondent was not entitled to recover anything from the petitioner. *Oriental Insurance Co Ltd v V.D. Jhunjhunwala*, (2001) 91 DLT 496.

*Pari delicto*

The principle has also been held to apply in cases where a contract is void by reason of “unlawful object”, but the parties were not aware of it. Thus, for instance, in a case<sup>271</sup> before the Rajasthan High Court:

The parties made a forward contract in hydrogenated groundnut oil, not aware of the existence of an order issued under the Defence of India Rules prohibiting such contracts.

The court held that “the parties are not in *pari delicto*, and, therefore, it is a contract which is subsequently discovered to be void. The purchaser who has advanced money under the contract is entitled to a refund of it.”<sup>272</sup>

The doctrine of *pari delicto* was stated in the following words in *Onkarmal v Banwarilal*.<sup>273</sup>

The principle behind the doctrine of *pari delicto* is that where each party is equally at fault, the law favours him who is actually in possession, or that where both parties are equally culpable, the law will leave them where it finds them and will not engage itself to determine the rights as between them. But this principle is subject to well-known exceptions, one of which is that it will not apply where the parties are not or cannot be said to be really in *pari delicto*.<sup>274</sup>

Thus, there are at least two exceptions in which the benefits passed under an agreement which is void by reason of illegality of object can be recovered.

Firstly, where the parties are not at equal fault, the less guilty may recover anything that he has given to the other under the contract. Where a woman was induced by an insurance agent to pay premiums upon an illegal and void policy, she was held entitled to recover, as she was innocent.<sup>275</sup>

The doctrine of *pari delicto* is not designed to reward the wrong-doer or to penalise the wronged by denying to the victim access to justice. The doctrine is attracted only when none of the parties is a victim and both parties have voluntarily and by their free will joined hands to flout the law for their mutual gain. Applying this principle to the landlord-tenancy relationship THAKKAR J of the Supreme Court held that advancing a sum of money by way of loan by the tenant to the landlord in order to get possession of premises under an unlawful agreement is an exploitation of a needy person and, therefore, he was entitled to have the advance adjusted towards rent as agreed.<sup>276</sup> Section 65 is not attracted where a negotiable instrument

271. *Ram Singh v Jethanand Wadhumal & Co*, AIR 1964 Raj 232.

272. See also *Fakir Chand Seth v Dambarudhar Bania*, AIR 1987 Ori 50, advance payment for paddy in ignorance of a control order, allowed to be recovered.

273. AIR 1962 Raj 127. Ss. 32 and 56 do not permit conditions to be read into the contract. *V.C.K. Bus Service Ltd v RTA*, AIR 1957 SC 489; 1957 SCR 663.

274. Cited in *Ram Singh v Jethanand Wadhumal & Co*, AIR 1964 Raj 232.

275. *Hughes v Liverpool Victoria Legal Friendly Society*, (1916) 2 KB 482.

276. *Mohd Salimuddin v Misri Lal*, (1986) 2 SCC 378; AIR 1986 SC 1019 following *V.S. Rabi v Ram Chambeli*, (1984) 1 SCC 612; AIR 1984 SC 595; (1984) 2 SCR 290.

is rendered void by material alteration in inserting a date in an undated instrument.<sup>277</sup>

Secondly, where no part of the illegal purpose has been executed, that is, the agreement is still executory, any benefits passed under the agreement may be recovered back. In a case before the Patna High Court:<sup>278</sup>

Where in a contract of marriage which was illegal, the father of the bride refused to perform the marriage, he was held entitled to the refund of the money paid by him to the father of the bridegroom.

### *Quantum meruit claims*

Claims under the well-known English law doctrine of *quantum meruit* have been allowed by the courts under this section. The Supreme Court observed in *State of Madras v Gannon Dunkerley & Co*<sup>279</sup> that a claim for *quantum meruit* is a claim for damages for breach of contract. The value of the material used or supplied is a factor which furnishes a basis for assessing the amount of compensation. The claim is not for price of goods sold and delivered but for damages. That is also the position under Section 65. In another case<sup>280</sup> reasonable compensation was awarded on the implication of a contract. It will not displace an express stipulation on the point.

In a subsequent case, the Supreme Court explained the requirements of the claim. The original contract must be so discharged by the opposite party that the plaintiff is entitled to treat himself as free from the obligation of further performance and he must have elected to do so. The remedy is not available to the party who breaks the contract even though he might have partly performed it. The remedy is restitutory, it is a recompense for the value of the work done by the plaintiff in order to restore him to the position which he would have been in if the contract had never been entered into. In this respect it is different from a claim for damages which is a compensatory remedy. The court accordingly did not allow the claim of a contractor for extra payment on the ground that he had to procure the raw material from a longer distance than that represented in the tender documents.<sup>281</sup> The material was in fact available within the stated distance, but its removal required permission of Cantonment Authorities which the contractor could not manage to get.<sup>282</sup>

Explaining the nature of justice that Section 65 strives for, the Supreme Court has observed:<sup>283</sup>

“We do not have the slightest doubt that net profits realised by the company as a result of its various business activities can never be the

277. *Jayantilal Goel v Zubeda Khanum*, AIR 1986 AP 120.

278. *Dharindhar v Kanhaiji Sahay*, AIR 1949 Pat 250.

279. AIR 1958 SC 560: 1959 SCR 379.

280. *Alopi Parshad & Sons Ltd v Union of India*, AIR 1960 SC 588: (1960) 2 SCR 793.

281. *Puran Lal Sah v State of U.P.*, (1971) 1 SCC 424.

282. See further, *Srinivas & Co v Inden Biselers*, (1971) 3 SCC 725: AIR 1971 SC 2224.

283. *State of Rajasthan v Associated Stone Industries*, (1985) 1 SCC 575, 580: AIR 1985 SC 466.

measure of compensation to be awarded under Section 65. It is not as if Section 65 works in one direction only. If one party to the contract is asked to disgorge the advantage received by him under a void contract, the other party may ask him to restore the advantage received by him. The restoration of the advantage and the payment of compensation have necessarily to be mutual. In *Govindram Seksaria v Edward Radbone*<sup>284</sup> the Privy Council pointed out that the result of Section 65 was that each of the parties became bound to restore to the other any advantage which the restoring party had received under the contract. As a result of the contract being void, the State could at the most recover from the contractor the value of the rough stone excavated from the quarries. But then it would have to make good to the company the expenditure incurred by it in quarrying operations and extraction of the rough stone.”

The contract was for the grant of a quarry. It was found to be void because the parties were mistaken about the application of income tax laws in the area.

#### *Becomes void*

The second type of situation covered by Section 65 is where a valid contract is made in the beginning, but it subsequently becomes either unlawful or impossible of performance. Any benefits which have been passed under the contract from one party to other must be restored. This is subject to the expenses which have already been incurred by the other party in the performance of the contract. Where a contract for purchase of granite stones became inoperative by reason of the seller's delay in obtaining permit from the Mining Department for removal of the material, the purchaser became entitled to refund of the whole of the money paid by him. No interest was allowed because he had himself deposited the money with some delays.<sup>285</sup>

*ENGLISH LAW.*—The principles of English law before the Law Reform (Frustrated Contracts) Act, 1943, were those laid down in the two coronation cases, one of them is, *Krell v Henry*<sup>286</sup> where the court held that the rent which had been paid before the contract to hire premises became void by reason of the postponement of the procession was not refundable and the outstanding rent was not recoverable. The courts left the parties where they were. They also did not like to disturb the rights which the parties had acquired before the contract became void. Of this the illustration is

284. (1946–47) 74 IA 295: AIR 1948 PC 56. *Confederation of Real Estate Developers Assn of India v State of M.P.*, 2015 SCC OnLine MP 2839: AIR 2015 MP 25, a case of unjust enrichment caused by an illegal levy of a municipal tax. An order was passed directing refund of the amount collected with interest at 9 per cent p.a.

285. *Pallava Granite Industries India (P) Ltd v A.P. Mineral Development Corp Ltd*, (2005) 4 ALD 230. *Tulsabai v Rajani*, (2010) 6 Mah LJ 371, agreement to sell land, earnest money paid, agreement became void because of the Collector's refusal to permit sale, liability to refund earnest money or to pay compensation.

286. (1903) 2 KB 740 (CA).

*Chandler v Webster*.<sup>287</sup> The plaintiff sued for refund of the rent which he had paid in advance and the landlord counter-claimed for the balance which was due. ROMER LJ stated the principle and said: “Applying this to the facts here, as soon as it was ascertained that the procession, though no fault of either of the parties, could not take place, they were immediately free from any subsequent obligation under the contract, but the contract could not be considered as rescinded *ab initio*. That being so, many legal rights previously accrued to either of the parties remained, and could not be disturbed, and one of those rights was the right of the defendant to be paid £ 141.15 s.”

The hardship that this principle is likely to cause was to a certain extent mitigated by the House of Lords in *Fibrosa Spolka Akeyjna v Fairbairn Lawson Combe Barbour Ltd.*<sup>288</sup> Lord RUSSELL OF KILLOWEN at once observed that *Chandler v Webster* was wrongly decided. Their Lordships accordingly allowed the £ 1000 to be recovered which were paid in advance for purchasing a machinery and the performance having been rendered illegal by the intervention of war. His Lordship continued:

The money paid was recoverable, as having been paid for a consideration which had failed. The rule that on frustration the loss lies where it falls cannot apply in respect of moneys paid in advance when the consideration moving from the payee for the payment has wholly failed, so as to deprive the payer of his right to recover moneys so paid as moneys received to his use; but the rule will, unless altered by legislation, apply in all other respects.

*LAW REFORM (FRUSTRATED CONTRACTS) ACT (ENGLISH).*—The expected legislation came within a year. Now the rights of parties whose contract has ended by frustration are adjusted under the provisions of the Law Reform (Frustrated Contracts) Act, 1943. The main provisions of the Act are as follows:

All sums of money which have been paid under a frustrated contract shall be refundable and those which are still payable shall cease to be payable. If any party has incurred expenses before the time of discharge in the performance of the contract, the court may, if it thinks just to do so, allow him to deduct such expenses from the refundable deposit or allow him to recover. The same principle will apply to any benefits received other than money. In estimating the amount of expenses the court may take into account the reasonable overhead expenses and the work or services personally performed

287. (1904) 1 KB 493; (1904) 73 LJ KB 401 (CA).

288. 1943 AC 32 (HL). *Commr, Kadayanallur Panchayat Union v A. Puthuran Padayachi*, (2006) 2 CTC 392 (Mad), plaintiff obtained at auction the right to fishing in a pond and made payment according to auction rules. The auction was not confirmed. There was no water in the pond due to failure of rains. The decree directing refund of auction price held sustainable. *Baldev Singh v Keshwa Nand*, (2011) 2 ICC 414 (P&H), under an agreement to sell land, the seller received earnest money from the purchaser, right then the government started the process of acquiring the land in question, held, the contract was frustrated, the purchaser became entitled to refund of his earnest money.

by the party. Benefits received under an insurance policy are not to be taken into account unless there is an express obligation to insure.

### APPROPRIATION OF PAYMENTS [SS. 59–61]

When a debtor owing several distinct debts to one person, makes a payment, which is not sufficient to discharge all the debts, the question arises to which particular debt the payment is to be applied. The Act, in Sections 59 to 61, lays down the underlying principles.<sup>289</sup>

**S. 59. Application of payment where debt to be discharged is indicated.**—Where a debtor, owing several distinct debts to one person, makes a payment to him, either with express intimation, or under circumstances implying, that the payment is to be applied to the discharge of some particular debt, the payment, if accepted, must be applied accordingly.

#### *Illustrations*

(a) *A owes B, among other debts, 1000 rupees upon a promissory note, which falls due on the first June. He owes B no other debt of that amount. On the first June A pays to B 1000 rupees. The payment is to be applied to the discharge of the promissory note.*

(b) *A owes to B among other debts, the sum of 567 rupees. B writes to A and demands payment of this sum. A sends to B 567 rupees. This payment is to be applied to the discharge of the debt of which B had demanded payment.*

**S. 60. Application of payment where debt to be discharged is not indicated.**—Where the debtor has omitted to intimate, and there are no other circumstances indicating to which debt the payment is to be applied, the creditor may apply it at his discretion to any lawful debt actually due and payable to him from the debtor, whether its recovery is or is not barred by the law in force for the time being as to the limitation of suits.

**S. 61. Application of payment where neither party appropriates.**—Where neither party makes any appropriation, the payment shall be applied in discharge of the debts in order of time, whether they are or not barred by the law in force for the time being as to the limitation of suits. If the debts are of equal standing, the payment shall be applied in discharge of each proportionately.

#### 1. Appropriation by debtor

The first principle is laid down by Section 59 which confers the right of appropriation upon the debtor. If the debtor owes several distinct debts to the same creditor and makes payment, he has the right to request the creditor to apply the payment to the discharge of some particular debt. If the creditor accepts the payment, he is bound by the appropriation.<sup>290</sup> This

289. *Jahar Roy v Premji Bhimji Mansata*, (1977) 4 SCC 562: AIR 1977 SC 2439.

290. Where the creditor accepted a conditional payment, he was not allowed to repudiate the condition, *Kapurchand Godha v Mir Nawab Himayatalikhan Azamjah*, AIR 1963 SC 250: (1963) 2 SCR 168.

principle was laid down as early as (1816) in *Clayton, re*<sup>291</sup> and has since been incorporated in the section and also followed in a number of cases. This principle applies to several distinct debts and not to a single debt payable by instalments.<sup>292</sup> This set of sections is applicable only in cases where more than one debts are due from the debtor to the creditor. They are not attracted when there is only one debt, or, as in this case, the debt has become merged into a decree.<sup>293</sup> The debtor may exercise this right and may specify his appropriation expressly or his intention may be implied from surrounding circumstances indicating that his intention at the time of payment was to appropriate the amount deposited by him to a particular debt or to the account of that debt.<sup>294</sup> The payment of a money decree was directed to be in monthly instalments. The judgment debtor remitted monthly instalments with a covering letter that the amount be appropriated towards principal. The bank did not refuse it and remained silent about it. The bank became bound by the appropriation. He could not appropriate the payments first towards interest and costs.<sup>295</sup>

These sections contain a general rule for appropriation of payments towards several distinct debts and not towards various heads of one debt.<sup>296</sup> It was not applied to a case in which the principal and interest amount were due on a single debt. The rule applicable in such cases is that payment is first applied to wipe out interest and the balance is appropriated towards principal.<sup>297</sup> An arbitration award was passed against the respondent for the principal sum with future interest. The award was challenged under Section 34 of the Arbitration and Conciliation Act, 1996. During pendency of such proceeding the respondent deposited certain amount in the court. The deposit was recorded as representing the principal amount due and payable under the award. The court said that the fact that the appellant made no objection did not mean that he had accepted the appropriation. He therefore had the right to appropriate it towards the interest amount which was due till that date.<sup>298</sup>

291. (1816) 1 Mer 572: 15 RR 161.

292. *Munno Bibi v CIT*, AIR 1952 All 514.

293. *Gurpreet Singh v Union of India*, (2006) 8 SCC 457; *Haribhai S. Watane v Raju D. Borkar*, (2004) 4 AIHC 2728 (Bom), rent paid by tenant to landlord could be appropriated towards other dues because the tenant did not indicate any appropriation.

294. *Prem Nath Kapur v National Fertilizers Corp of India Ltd*, (1996) 2 SCC 71.

295. *Smithaben H. Patel v Industrial Credit and Development Syndicate*, AIR 1997 Kant 188; *Delhi State Coop Bank Ltd v DSCO Coop Industrial Society Ltd*, (2001) 91 DLT 555.

296. *Industrial Credit & Development Syndicate v Smithaben H. Patel*, (1999) 3 SCC 80: AIR 1999 SC 1036. The rules apply before the stage of decree and not to the execution of court decree. *Haryana Urban Development Authority v Devinder Kaur*, AIR 2002 NOC 268 (P&H), compensation amount for land acquisition deposited by the Collector at his discretion, the claimant not allowed to take the benefit of S. 60 and claim appropriation of that amount.

297. *Punjab National Bank v Surinder Singh Mandyal*, AIR 1996 HP 1. The court followed *Meghraj v Bayabai*, (1969) 2 SCC 274: AIR 1970 SC 161.

298. *Leela Hotels Ltd v Housing & Urban Development Corp Ltd*, (2012) 1 SCC 302.

## 2. Appropriation by creditor

The second principle is laid down in Section 60, which enables the creditor to make appropriation. If the debtor makes payment without any appropriation, the creditor may use the payment at his discretion to wipe out any debt which is due. He may, for example, use it in payment of a time-barred debt,<sup>299</sup> or in payment of a debt which carries simple or lesser interest.<sup>300</sup>

Where a mortgagor deposited some amount in the court without indicating whether it was for principal or interest, the court held that the ordinary principle that such money should first be applied to interest and costs and then to principal, would apply.<sup>301</sup>

## 3. Appropriation by law

The third principle is in Section 61. The section applies when neither party makes an appropriation. In such a situation the law gets the right to appropriate the payment and the law prefers to wipe out the debts in the order of time in which they were incurred. The section says: “When neither party makes any appropriation the payment shall be applied in discharge of the debts in order of time, whether they are or are not (time-barred). ... If the debts are of equal standing, the payment shall be applied in discharge of each, proportionally.”

## ASSIGNMENT OF CONTRACTS

Section 37 which enables parties to dispense with performance should also enable them to assign their contractual obligations. “Assignment” means transfer of contractual rights or liability by a party to the contract to some other person who is not a party.<sup>302</sup> For example, if A owes B Rs 500 and B owes C a like amount, B has the right to receive from A and is under

299. *Kamaleshwari Prasad v Gangadhar Mal*, AIR 1940 Pat 52. *State of Gujarat v Bank of Baroda*, AIR 1997 Guj 130, the debtor while making payment into his bank account did not indicate the particular loan to which he wanted the payment to be applied. Appropriation by the bank held to be proper. *PNB Dharamshala v Prem Sagar Chaudhary*, AIR 1996 HP 86, absence of instruction by judgment-debtor as to manner of appropriation, decree-holder entitled to appropriate under S. 60.

300. *Rameshwar Koer v M. Mehidi*, ILR (1898) 26 Cal 39. S. 60 cannot be applied independently of S. 59. It gives discretion to the creditor and not to the judgment debtor, *Industrial Credit & Development Syndicate v Smithaben H. Patel*, (1999) 3 SCC 80: AIR 1999 SC 1036. *Waterbase Ltd v K. Ravindra*, 2003 Cri LJ 967 (AP), prosecution for dishonour of cheque, when the accused owed large sums to the complainant, any amount paid subsequently could be appropriated towards any other amount of a lawful debt at the choice of the complainant as envisaged in S. 60 and not merely against the amount of the dishonoured cheque.

301. *Meghraj v Bayabai*, (1969) 2 SCC 274: AIR 1970 SC 161.

302. See *R.K. Associates v Channappa*, AIR 1993 Kant 247, change of name of firm, old firm assigned the right to purchase a land to the new firm, which paid the price, assignee firm could enforce the sale and demand arbitration in terms of the provisions in the agreement. *Zoroastrian Coop Housing Society Ltd v Coop Societies (Urban)*, (2005) 5 SCC 632: AIR 2005 SC 2306, prohibition of assignment as a part of the contract, valid.

liability to pay C. B can ask A to pay directly to C and if A accepts, that will be an assignment of B's right to C.

### Assignment of liabilities

An important principle affecting assignments is that the burden of or liability under a contract cannot be assigned. The promisor has the right to insist that performance shall be the responsibility of the promisee.<sup>303</sup> The promisor may have contracted with him by reason of the personal confidence which he reposed in him and, therefore, the promisor, can object to the contract being performed by any other person. This is more particularly true of cases in which the engagement is of personal nature, such as, the engagement to sing or to paint. In such cases there is no question of vicarious performance. In other cases it should not matter to the promisor whether the performance is offered by the promisee himself or by someone else acting for him, provided, of course, that the promisee is responsible for the performance by his agent.<sup>304</sup> Explaining this in *Davies v Collins*,<sup>305</sup> Lord GREENE MR said: "In many contracts all that is stipulated for is that the work shall be done and the actual hand to do it need not be that of the contracting party himself; the other party, will be bound to accept performance carried out by somebody else. The contracting party, of course, is the only party who remains liable. He cannot assign his liability to a sub-contractor, but his liability in those cases is to see that the work is done, and if it is not properly done, he is liable."<sup>306</sup>

A vicarious performance is not an assignment in the real sense of the word. "It is quite a mistake to regard that as an assignment of the contract, it is not."

Where with the consent of the promisor, the promisee drops out and some other person takes over his obligation, that is also not an assignment. It is a novation, that is, change of parties with mutual assent. In the words of VENKATARAMA AIYAR J of the Supreme Court:<sup>307</sup> "As a rule obligations under a contract cannot be assigned except with the consent of the promisee, and when such consent is given, it is really a novation resulting in a substitution of liabilities."<sup>308</sup>

303. *Robson & Sharpe v Drummond*, (1831) 2 B & Ad 303.

304. See, for example, *British Waggon Co v Lea & Co*, (1880) LR 5 QBD 149 (DC). The party who actually performs has a right to ask the other party not to pay or to stop paying the main contractor till his dispute with the main contractor is resolved. *Yab Kee Seong v Teguh Bina*, (1992) 1 CLJ 525 High Court of Shah Alam.

305. (1945) 1 All ER 247.

306. This principle has been accepted by the Supreme Court in *Khardah Co Ltd v Raymon & Co (India) (P) Ltd*, AIR 1962 SC 1810: (1963) 3 SCR 183 where at p. 201, VENKATARAMA AIYAR J said; "The contract in question is one for the sale of goods. It is of no consequence to the buyer as to who delivers the goods. What matters to him is that the goods delivered should be in accordance with the specifications."

307. In *Khardah Co Ltd v Raymon & Co (India) (P) Ltd*, AIR 1962 SC 1810: (1963) 3 SCR 183.

308. *Ibid* at p. 202.

### Assignment of rights

“On the other hand, rights under a contract are assignable unless the contract is personal in its nature or the rights are incapable of assignment either the law or under an agreement between the parties.” The intention of the parties is to be gathered from the nature of the agreement and the surrounding circumstances. The leading authority is the decision of the Supreme Court in *Khardah Co Ltd v Raymon & Co (India) (P) Ltd.*<sup>309</sup>

The dispute arose out of a contract for the purchase by a mill of Pakistani raw jute from a dealer, who failed to supply the goods as agreed.

The court held that the contract for the purchase of foreign jute was not assignable because the goods had to be imported under a licence which was not transferable and which also required the utilisation of the imported raw material only by the mill in question. The only other question was whether the dealer could assign his right to the price on delivery of the goods. The court conceded that ordinarily there is nothing personal about a contract for the sale of goods. The court further pointed out that “it is settled law that an arbitration clause does not take away the right of a party to assign if it is otherwise assignable”.<sup>310</sup> In the opinion of the court the rights of the unpaid seller also do not stand in the way of the assignability of a contract. There was no provision in the contract prohibiting assignment, but even so the court held that the contract involved so many personal obligations on the part of the seller, which strongly suggested that the intention of the parties was that neither of them should assign the contract.<sup>311</sup> The court also took occasion to point out: “There is in law a clear distinction between assignment of rights under a contract by a party who has performed his obligations thereunder, and assignment of a claim for compensation which one party has against the other for breach of contract. The latter is a mere claim for damages which cannot be assigned in law, the former is a benefit under an agreement, which is capable of assignment.”

The rights under a lottery ticket are assignable. Explaining this, TULZAPURKAR J said:<sup>312</sup>

A sale of lottery ticket confers on the purchaser thereof two rights (*a*) a right to participate in the draw and (*b*) a right to claim a prize contingent upon his being successful in the draw. Both would be beneficial interests in movable property, the former “*in praesenti*”, latter in future depending on a contingency lottery tickets, not as physical articles, but as slips of paper or memoranda, evidence, not one but both these beneficial interests

309. AIR 1962 SC 1810: (1963) 3 SCR 183.

310. Vide *Shayler v Woolf*, 1946 Ch 320 (CA) and RUSSEL ON ARBITRATION (16th Edn) 65.

311. *Namasivaya Gurukkal v Kadir Ahmad*, ILR (1894) 17 Mad 168. Contra: *Jeffer Meher Ali v Budge Jute Mills Co*, ILR (1906) 33 Cal 702; *Delhi Cloth & General Mills Co Ltd v Harnam Singh*, AIR 1955 SC 590: (1955) 2 SCR 402, 425.

312. *H. Anraj v Govt of T.N.*, (1986) 1 SCC 414, 432, 433: AIR 1986 SC 63.

in moveable property which are obviously capable of being transferred, assigned or sold and on their transfer, assignment or sale, both these beneficial interests are made over to the purchaser for a price.

The matter arose out of the attempt of the T.N. Government to subject the sale of lottery tickets to Sales Tax. Such tickets being goods within the meaning of the Sale of Goods Act, 1930, the State was held to be competent to do so. Dealing with agreements which are in the nature of grants, the court said: "It is well settled that rights and benefits arising thereunder, unless of a personal nature, partake of the character of personality as opposed to reality and, therefore, movable property capable of being assigned or transferred."<sup>313</sup>

Another illustration of a contract involving personal element and, therefore, incapable of being assigned is to be found in the decision of the Court of Appeal in *Kemp v Baerselman*.<sup>314</sup>

The defendant agreed to supply a cake manufacturer with all the eggs that he might require for a year and the latter was not to purchase elsewhere. Deliveries were to be made at three different places and payment was to be by drawing bills of exchange on the manufacturer. The manufacturer's business was taken over by a company in which he was the principal shareholder, but even so the defendant refused to continue with the supplies.

It was held that the contract, being of personal nature in that it involved the personal creditworthiness of the buyer as to the mode of payment, was not capable of being assigned.

The Central Government assigned a piece of land to its own corporate undertaking with rights, liberties and privileges one of which was exemption from land revenue. It was held that the assignee became entitled to the exemption as a successor in interest of the Central Government.<sup>315</sup>

### *Unilateral cancellation of sale deed*

It is not possible for the vendor to make a deed of cancellation of the sale deed made and registered earlier and get it registered, even if the ground is that full consideration was not received by the vendor. Such deed amounts to rescission of the contract. It would require an order of the court under Section 31 of the Specific Relief Act, 1963.<sup>316</sup>

313. Quoting SALMOND'S JURISPRUDENCE (12th Edn) 412, para 108, under the heading "Proprietary rights". See *Darlington Borough Council v Wiltshire Northern Ltd*, (1995) 1 WLR 68 (CA), the assignee's right to recover damages for breach of contract would be as extensive as that of the assignor. The case involved the assignment of rights in a building under construction and the action by the assignee was for defective construction.

314. (1906) 2 KB 604: (1906) 75 LJ KB 873 (CA).

315. *SAIL v State of M. P.*, (1999) 4 SCC 76: AIR 1999 SC 1630.

316. *E.R. Kalavian v Inspector General of Registration*, AIR 2010 Mad 18; *G.D. Subramaniam v Sub-Registrar, Sidco Nagar*, (2009) 1 CTC 709, a sale cannot be unilaterally cancelled, registration of any such cancellation deed was held liable to be set aside.

### Effect and formalities of assignment

#### *Consideration*

In the first place, an assignment requires some consideration between the assignor and assignee. In the absence of any consideration between them, the assignment will be revocable by the assignor.<sup>317</sup> But when an assignment made as a gift has been completed by fulfilling the essential formalities, it cannot be revoked. This is true of all gifts. This is borne out by the following statement of TURNER LJ.<sup>318</sup> "In order to make a voluntary settlement valid and effectual, the settlor must have done everything, which according to the nature of the property comprised in the settlement, was necessary to be done in order to transfer the property and render the settlement binding upon him."

#### *Subject to equities*

Secondly, the title of the assignee shall be subject to all equities that exist at the time between the assignor and assignee, or that arise up to the time that the notice of assignment is given to the debtor.<sup>319</sup> Where, for example, the assignor had induced by fraud the other party to contract with him, the other party will have the same right of rescission against the assignee as he would have had against the assignor. But the assignee will not be affected by any equity of personal nature between the assignor and assignee. For example, the right to claim damages for the fraud committed by the assignor cannot be used to defeat the right of the assignee.<sup>320</sup>

#### *Notice of assignment*

Thirdly, notice of assignment should be given to the debtor. Such a notice is useful from several points of view. It binds the debtor. In the absence of a notice, the debtor can make payment to the assignor himself and that will be a good discharge. Another advantage of giving notice is that the assignee will not be affected by any equity that may arise between the assignor and the debtor after notice. Notice is also important from the point of view of priorities. If, for example, the assignor makes more than one assignments of the same claim, the assignee who gives notice of the assignment to him first in point of time will have priority over the other, even if the assignment to him came later in time.

317. *Glegg v Bromley*, (1912) 3 KB 474. See PARKER J at p. 491.

318. *Milory v Lord*, (1862) 4 De GF & J 264, 274: (1862) 31 LJ Ch 798: 7 LT 178.

319. For example, after an effective assignment, a garnishee order issue against the assignor was held to be not effective on a bank balance which already stood assigned to the assignee. *Tan Way Boom v Omar Marican Holdings*, (1990) 2 Curr LJ 700 High Court, Penang.

320. *Stoddart v Union Trust Ltd*, (1912) 1 KB 181 (CA).

## DISCHARGE BY AGREEMENT

### Contracts which need not be performed

Section 62 provides that “if the parties to a contract agree to substitute a new contract for it, or to rescind or alter it, the original contract need not be performed”.

**S. 62. Effect of novation, rescission and alteration of contract.**—If the parties to a contract agree to substitute a new contract for it, or to rescind or alter it, the original contract need not be performed.

#### *Illustrations*

- (a) A owes money to B under a contract. It is agreed between A, B and C that B shall thenceforth accept C as his debtor, instead of A. The old debt of A to B is at an end, and a new debt from C to B has been contracted.
- (b) A owes B 10,000 rupees. A enters into an agreement with B and gives B a mortgage of his (A's) estate for 5000 rupees in place of the debt of 10,000 rupees. This is a new contract and extinguishes the old.
- (c) A owes B 1000 rupees under a contract. B owes C 1000 rupees. B orders A to credit C with 1000 rupees in his books, but C does not assent to the agreement. B still owes C 1000 rupees, and no new contract has been entered into.

### Novation

When the parties to a contract agree to substitute the existing contract with a new contract, that is called *novation*.<sup>321</sup> In the well-known case of *Scarf v Jardine*<sup>322</sup> Lord SELBORNE explained the meaning and effect of novation in the following words:

...there being a contract in existence, some new contract is substituted for it either between the same parties or between different parties, the

321. Where the parties change only a part of the contract and the new contract is so inconsistent with the existing contract that they cannot stand together, there is no good novation. *Lata Construction v Rameshchandra Ramniklal*, (2000) 1 SCC 586: AIR 2000 SC 380. *United Bank of India v Ramdas Mahadeo Prashad*, (2004) 1 SCC 252: (2004) 1 CLJ 147, a memorandum of understanding does not amount to novation as envisaged under this section. The respondents had already committed a breach of contract, they could hardly seek to enforce the contract. *CITI Bank N.A. v Standard Chartered Bank*, (2004) 1 SCC 12: AIR 2003 SC 4630: (2003) 117 Comp Cas 554, novation cannot be brought about unilaterally. It requires consent of both parties. There was no evidence of any tripartite arrangement under which the third party was to take over liability. The case was rather governed by S. 63 under which a promisee can unilaterally accept an altered position and discharge the other party from liability. The party had accepted dishonoured bonds knowingly and voluntarily. *Vijaykumar Khandre (Dr) v Prakash Khandre*, AIR 2002 Kant 145, a returned candidate was a licensed contractor and was holding several contracts with the Government. He tried to hand them over to others but a tripartite agreement could not be proved. Hence disqualification remained. *Jay Karnataka News Printers Ltd v Syndicate Bank*, (2001) 2 BC 27 (Kar DB), substitution of new contract for the old is the very essence of novation, mere deposit of amount by a third party towards liquidation of the outstanding amount cannot constitute novation between lender and borrower. *Polymat India (P) Ltd v National Insurance Co Ltd*, (2005) 9 SCC 174: AIR 2005 SC 286, terms of contract reduced to writing, could not be changed without mutual agreement, amendments in the approved proposal not agreed to by the insurer, ineffective.

322. (1882) LR 7 AC 345, 351.

consideration mutually being the discharge of the old contract. A common instance of it in partnership cases is where upon the dissolution of a partnership the persons who are going to continue in business agree and undertake as between themselves and the retiring partner, that they will assume and discharge the whole liabilities of the business, usually taking over the assets; and if, in that case, they give notice of that arrangement to a creditor, and ask for his accession to it, there becomes a contract between the creditor who accedes and the new firm to the effect that he will accept their liability instead of the old liability, and on the other hand, that they promise to pay him for that consideration.

Hence novation is of two kinds, namely:

- (1) a novation involving change of parties; and
- (2) a novation involving substitution of a new contract in place of the old.

### 1. Change of parties

The first illustration to Section 62 is a case of novation by change of parties. If *A* is a debtor and the creditor agrees to accept *B* in his place as the debtor, the original contract between the creditor and *A* is at an end.<sup>323</sup> A novation of this kind usually takes place when a new partner is admitted into an existing firm or when a partner retires from a firm and the new firm as constituted after admission or retirement accepts the liabilities of the old firm and this is approved by the persons dealing with the firm. Concurrence of all the parties is necessary.<sup>324</sup> All the parties to the earlier contract have to give their consent. One or more of the parties to the novated contract must be new persons who undertake the responsibility under the new contract.<sup>325</sup>

### Novation and rescission

An order of arrest of the supplier's vessel was passed in an Admiralty suit. The plaintiff made an out of court settlement with the owner of the vessel. Under a subsequent agreement, the debtor agreed to pay not only the amount claimed in the suit but costs and interest also. The payment under the agreement was guaranteed by a third party. It was held that the existence

323. *Shrikant v Vasantrao*, (2006) 2 SCC 682: AIR 2006 SC 918, after an election, a contract of the returned candidate with the State was transferred to a statutory corporation, contract with State ended.

324. *Bhaskaruni Venkatanarayana v Bhaskaruni Lakshmibayamma*, AIR 1929 Mad 309. *Godan Namboothiripad v Kerala Financial Corp*n, AIR 1998 Ker 31, hire-purchase, default in payment, seller seized the vehicle, a third person undertook to pay the unpaid balance and got the vehicle released, the original debtor ceased to be the debtor. *SBI v T. R. Seethavarma*, (1994) 2 KLT 18: AIR 1995 Ker 31, the court has to see not only whether the new debtor has consented to assume liability but also whether the creditor has accepted the liability of the new debtor.

325. *Sasidaran v India Cements Capitals Ltd*, (2011) 1 MWN (Civil) 561, promise was found to be not a party to the new agreement, hence no novation. *Colgate Palmolive India Ltd v T.J. George*, (2011) 1 LW 732 (Mad), after novation, the parties cannot fall back upon the old contract. Damages were not to be awarded on the terms of the old agreement.

cause of action became substituted by a new cause arising out of the agreement. Admiralty claim was no longer maintainable. The vessel became the property of the defendant free from liability to the plaintiff.<sup>326</sup>

## 2. Substitution of new agreement

When the parties to a contract agree to substitute a new contract for it, the original contract is discharged and need not be performed. It is necessary for the application of this principle that the original contract must be subsisting and unbroken. The substitution of a new contract is not possible after there has been a breach of the original contract. An early illustration is *Manohur Koyal v Thakur Das Naskar*.<sup>327</sup>

The plaintiff sued to recover the sum of Rs 1173 due on a bond. After the due date of the bond, the plaintiff agreed to accept Rs 400 in cash and a new bond of Rs 700 payable by instalments. Subsequently the defendant neither gave Rs 400 nor the bond.

The plaintiff thereupon sued him on the original bond. The Calcutta High Court held that the original contract was discharged, not by *novation*, but by breach, and the plaintiff was entitled to sue for the breach of the original contract.

Another illustration is provided by a case in which an engineering contract for extraction of coal became affected by major slides leading to stoppage. Another area was allotted to the petitioner in place of the affected area. He accepted it though it was less than the original allotted area. The court said that original contract became discharged. Tenders could validly be invited for that area.<sup>328</sup>

The petitioner was appointed in response to an advertisement but placed at a lower scale than that mentioned in the advertisement. He accepted his placement. He then claimed the promised pay scale. He was not allowed to do so. The principle of novation applied. The appointment and acceptance at the lower scale substituted the original proposed scale.<sup>329</sup>

A contractor's bill was lying unpaid for about 4½ years. For that reason he was exposed to huge losses and grave economic duress. He settled his claim under a memorandum of understanding under which he accepted payment in full and final satisfaction. He then raised a dispute and sought arbitration for claiming interest on late payment. It was held that the memorandum of understanding had put an end to the original contract and therefore the contractor could not claim arbitration in terms of the original contract.<sup>330</sup>

326. *MJR Steels (P) Ltd v Chrisomar Corpns*, AIR 2007 NOC 234 (Cal) (DB).

327. ILR (1887–88) 15 Cal 319.

328. *BGR Mining & Infra (P) Ltd v Singareni Collieries Co Ltd*, AIR 2012 AP 71.

329. *Nagendra Kumar Brijraj Singh v Hindustan Salts Ltd*, (2001) 1 GCD 532.

330. *Lloyds Steel Industries Ltd v Oil & Natural Gas Corpns Ltd*, AIR 1997 Bom 337. The court followed *Damodar Valley Corpns v K.K. Kar*, (1974) 1 SCC 141; AIR 1974 SC 158; *Union of India v Kishorilal Gupta & Bros*, AIR 1959 SC 1362; (1960) 1 SCR 493; *VO Chidambaranar Port Trust v PSA Sical Terminals Ltd*, 2015 SCC OnLine Mad 2905; AIR

In the words of the Supreme Court in *Lata Construction v Rameshchandra Ramniklal*<sup>331</sup> as spoken by S. SAGHIR AHMAD J:

“One of the essential requirements of novation, as contemplated by Section 62, is that there should be complete substitution of a new contract in place of the old. It is in that situation that the original contract need not be performed. Substitution of a new contract in place of the old contract which would have the effect of rescinding or completely altering the terms of the original contract has to be by agreement between the parties. The substituted contract should rescind or alter or extinguish the previous contract. But if the terms of the two contracts are inconsistent and they cannot stand together, the subsequent contract cannot be said to be in substitution of the earlier contract.”

The contract in the case was to provide a flat. A subsequent contract between the parties provided that the rights of the buyer under the original contract would be extinguished only on payment by him of the stipulated amount. He failed to make the payment. It was held that he could invoke the terms of the original contract and claim before the Consumer Commission that there was a deficiency in service on the part of the builder.

It is further necessary that the new agreement should be valid and enforceable. Thus, where an existing mortgage was replaced by a new agreement of mortgage, the new agreement being not enforceable for want of registration, it was held that the parties were still bound by the original mortgage.<sup>332</sup> In a contract to provide land free of encumbrances for a housing project, the site had to be given up because of the inability to remove hutment occupation of the land and the rates had to be increased because of the escalated price of the new site, the Bombay High Court held that it amounted to novating the old with a new contract.<sup>333</sup>

It has also been pointed out in a judgment of the Calcutta High Court that “Section 62 requires an agreement which necessarily implies consideration”.<sup>334</sup> It is also obvious that there cannot be unilateral alteration of a

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2015 Mad 175, the contract provided that the place of arbitration would be at Tuticorin. The arbitrator with the consent of the parties decided to sit at Chennai. The agreement was not altered. Held, the place for questioning the award was to be Tuticorin, proceedings at Chennai were of no consequence.

331. (2000) 1 SCC 586: AIR 2000 SC 380 at p. 383. *Mcdermott International Inc v Burn Standard Co Ltd*, (2005) 10 SCC 353, tripartite agreement between head, intermediate and sub-contractor, under which the intermediate contractor, at the instance of the head contractor, varied the terms, sub-contractor complied with the altered terms without protest, this amounted to acceptance by silence.

332. See for example, *Shanker Lal Damodhar v Ambalal Ajaipal*, AIR 1946 Nag 260.

333. *Andheri Bridge View Coop Housing Society v Krishnakant Anandrao Deo*, AIR 1991 Bom 129.

334. *Union of India v Kishori Lal Gupta & Bros*, AIR 1953 Cal 642, 644, contract which is terminated by agreement, puts an end to its arbitration clauses also. *Dadri Cement Co v Bird and Co (P) Ltd*, AIR 1974 Del 223, a Division Bench held that the parties by entering into the new arrangement intended to substitute the original contract of sale by substituted arrangement consisting of the agreement, the deed of guarantee, the deed of pledge and the

contract. Where the parties had fixed by mutual agreement the rates of hiring a cinema hall, one of them was not allowed subsequently to alter them unilaterally.<sup>335</sup> T.V. operators, who were being subjected to revised rates, were held bound to pay new rates at the expiry of five years period for which the sanction was already in existence.<sup>336</sup>

In an already concluded construction contract, requiring that 10 per cent would be paid to the contractor in advance subject to the condition that he would submit a bank guarantee, this being not there in the original contract, was held to be not such a condition as would alter the very nature of the original contract.<sup>337</sup>

An alteration of the entire design of the rail overbridge was held to be a substantial alteration of the plan itself amounting to converting the same into a completely new project. Such an alteration could not fall into the increase or decrease clause of the contract. It was wrong on the part of the government to invite new tenders at the cost of the contractor. The government was ordered to pay for the work already done by the contractor.<sup>338</sup>

It was opined by their Lordships of the Privy Council as far back as the year 1893 in *Commercial Bank of Tasmania v Jones*<sup>339</sup> that “novation of debt operates as a complete release of the original debtor and cannot be construed as a mere covenant not to sue him.”

Where there was a provision in the original contract giving parties the option to terminate the contract and the parties by means of a supplementary contract agreed to postpone the termination, it was held that this did not amount to novation of the contract.<sup>340</sup>

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irrevocable power of attorney. The substitution operated to bring about novation of the original contract and that the original contract of sale became inoperative and unenforceable.

335. *Magnum Films v Golcha Properties (P) Ltd*, AIR 1984 Del 162. A settlement under S. 62 puts an end to the whole contract including arbitration clauses. *Vipinbhai R. Parekh v Western Rly*, AIR 1984 Guj 41. Where the original agreement containing an arbitration clause was substituted by a new agreement, the arbitration clause in the earlier agreement was not allowed to be resorted to. *Visakhapatnam Port Tract v Uma Constructions*, (1988) 25 Reports 126 (AP). Where the suitor agreed to accept less sum than claimed by him, the compromise brought an end to the original contract and whatever was due under it including interest. *Central Bank of India v V. Guruviah Naidu*, AIR 1992 Mad 139. *Hindustan Petroleum Corp v University of Hyderabad*, AIR 2003 NOC 448 (AP), contract in writing, novation would have to be in writing, mere disclaimer not sufficient to prove novation. In this case, the terms stated that prices ruling on the date of delivery would be applicable. Seller demanded full payment which was made, delivery to be made in 34 months which could not be done. The buyer agreed to accept late deliveries. The court said that he was bound to pay prices prevailing on actual dates of delivery. There was a price hike in the meantime.

336. *Subramanian v Kerala SEB*, (2003) 2 KLT 38.

337. *Devi Enterprises v State of UP*, AIR 2009 NOC 1213 (All). *Shriram Engg Co v State of Chattisgarh*, AIR 2015 Chh 183, the contractor performed only the profitable part of the contract and left unfinished the part which was less profitable. Rescission of contract after due information to the contractor was held to be proper.

338. *Union of India v Tantia Construction (P) Ltd*, (2011) 5 SCC 697. He could not have been required to do a new project at old rates.

339. 1893 AC 313 (PC).

340. *Unikol Bottlers Ltd v Dhillon Kool Drinks*, AIR 1995 Del 25.

Where the rights under the old contract are kept alive even after the second agreement, then there is no substitution of the contract and hence no novation.<sup>341</sup>

In a supply contract, an escalation of price, or reduction in quantity of supply order, or extension of date of supply has been held as not amounting to novation. It has been so reiterated by the Supreme Court.<sup>342</sup>

#### *No effect upon arbitration clause*

Where the signature to a settlement agreement were procured by coercion, it was held that the arbitration clause in the original agreement did not become discharged. The dispute was of a nature which was arbitrable under the original contract. It made no difference that a settlement agreement was entered into between the parties.<sup>343</sup>

**S. 67. Effect of neglect of promisee to afford promisor reasonable facilities for performance.**—If any promisee neglects or refuses to afford the promisor reasonable facilities for the performance of his promise, the promisor is excused by such neglect or refusal as to any non-performance caused thereby.

#### *Illustrations*

A contracts with B to repair B's house.

B neglects or refuses to point out to A the places in which his house requires repair.

A is excused for the non-performance of the contract, if it is caused by such neglect or refusal.

#### **Interdependent promises**

Where promises are interdependent so that one party cannot perform without cooperation of the other, if the latter does not provide reasonable facilities for performance, the former is excused from his obligation to perform. The illustration appended to the section is based upon *Makin v Watkinson*.<sup>344</sup> Another illustration is *Ellon v Topp*.<sup>345</sup>

An infant was placed by his father under a master to learn his three trades. Subsequently the master gave up one of his trades. The apprentice gave up his training for that reason.

The master sued for breach. The court came to the conclusion that the contract was on the basis of picking up three trades and the abandonment of one would not leave it to be the same contract. "If the master is not ready to teach in the very trade which he has stipulated to teach, the apprentice is not bound to serve. If, on the other hand, the apprentice had left the training

341. *H.R. Basvaraj v Canara Bank*, (2010) 12 SCC 458.

342. *Purbanchal Cables & Conductors (P) Ltd v Assam SEB*, (2012) 7 SCC 462: (2012) 4 SCC (Civ) 245.

343. *S.K. Sharma v Union of India*, AIR 2009 NOC 2057 (Del).

344. (1870) LR 6 Exch 25.

345. (1851) 6 Ex 424.

without any justification, the master would be free from any further obligation. It is evident that the master would not be liable for not teaching the apprentice if the apprentice will not be taught.”<sup>346</sup>

### Rescission and restoration

The section also permits the parties to rescind their contract. The Supreme Court allowed the parties to rescind under this section a contract for sale of forest coupes because of the substantial variance between the particulars of quantity and quality of timber held out at the time of the auction and the timer actually available. The contractor was allowed refund of his deposit. But no compensation was allowed to him for his loss because the contract contained a clause against compensation in such circumstances.<sup>347</sup>

Where an old contract is rescinded and is replaced by a new one, the old one will not revive only for the reason that there has been a failure to keep the new promise. The parties may, however, by mutual consent, restore the original and then the original will revive and become binding on the parties.<sup>348</sup>

Where the relationship between the parties was purely contractual and wholly non-statutory and the parties had by agreement ended their contractual obligations long back, it was held that if there was any dissatisfaction about the matter, it could have been resolved by reopening the settlement. Writ jurisdiction under Article 226 of the Constitution was not available in such matters.<sup>349</sup>

## REMISSION OF PERFORMANCE

Section 63 allows a party to a contract to dispense with the performance of the contract by the other party, or to extend the time for performance or to accept any other satisfaction instead of performance.

**S. 63. Promisee may dispense with or remit performance of promise.**—Every promisee may dispense with or remit, wholly or in part, the performance of the promise made to him, or may extend the time for such performance or may accept instead of it any satisfaction which he thinks fit.

### *Illustrations*

- (a) A promises to paint a picture for B. B afterwards forbids him to do so. A is no longer bound to perform the promise.
- (b) A owes B 5000 rupees. A pays to B and B accepts in satisfaction of the whole debt, 2000 rupees paid at the time and place at which the 5000 rupees were payable. The whole debt is discharged.

346. *Raymond v Minton*, (1866) LR 1 Exch 244. *Municipal Corp of Chandigarh v Shantikunj Investment (P) Ltd*, (2006) 4 SCC 109: AIR 2006 SC 1270, allotment of commercial plots, instalment delayed, charge of interest and penalty as provided in the conditions of allotment, valid. There was no requirement that all amenities should be first provided before demanding instalments.

347. *Syed Israr Masood v State of M.P.*, (1981) 4 SCC 289: AIR 1981 SC 2010.

348. *R.N. Kumar v R.K. Soral*, (1988) 2 SCC 508, 511: AIR 1988 SC 1205.

349. *Biren Poddar v SBI*, (1995) 2 BLJR 912 (Pat).

- (c) A owes B 5000 rupees. C pays to B 1000 rupees, and B accepts them, in satisfaction of his claim on A. This payment is a discharge of the whole claim.
- (d) A owes B, under a contract, a sum of money, the amount of which has not been ascertained. A, without ascertaining the amount gives to B, and B, in satisfaction thereof, accepts the sum of 2000 rupees. This is a discharge of the whole debt, whatever may be its amount. (e) A owes B 2000 rupees and is also indebted to other creditors. A makes an arrangement with his creditors, including B, to pay them a<sup>350</sup>[composition] of eight annas in the rupee upon their respective demands. Payment to B of 1000 rupees is a discharge of B's demand.

The effect of the provision is that the party who has the right to demand the performance of a contract may—

- (1) remit or dispense with it, wholly or in part; or
- (2) extend the time for performance; or
- (3) accept any other satisfaction instead of performance.<sup>351</sup>

### Acceptance of less sum

The acceptance of a less sum of money where more is due, is a good discharge of the whole of the liability. The Supreme Court decision in *Kapurchand Godha v Mir Nawab Himayatalikhan Azamjah*<sup>352</sup> illustrates this:

The liability was above twenty-seven lakhs of rupees. Hyderabad having been taken over, a committee was appointed to clear matters. It offered twenty lakhs to the creditor in full satisfaction and he accepted it. Afterwards the creditor sued the debtor for the balance.

S.K. DAS J held that the facts of the case are completely covered by Section 63 and illustration (c) thereof. The appellant having accepted the payment in full satisfaction of his claim was not entitled to sue. The court also relied upon Section 41 which provides that when a promisee accepts performance from a third person, he cannot afterwards sue the promisor.

Similarly, in *Hari Chand Madan Gopal v State of Punjab*<sup>353</sup> the Supreme Court held: "The Government had decided to recover only 40 per cent and no more. The Government's decision would amount to remitting a part of the debt due by the appellants. Therefore, the Government cannot ask to recover more than 40 per cent."

There must be proof that less sum has been accepted. Where the railways sent a cheque for an amount less than what was claimed by a party and, though the party retained the cheque, he did not issue any receipt that he was accepting it in full and final satisfaction and neither did he stop

350. This word was *substituted* for the word "compensation" by S. 2 and Sch. II of the Amending Act, 1891 (XII of 1891).

351. The whole thing is linked with promisee's conduct. *CIT v Shantilal (P) Ltd*, (1983) 3 SCC 561: AIR 1983 SC 952..

352. AIR 1963 SC 250: (1963) 2 SCR 168.

353. (1973) 1 SCC 204: AIR 1973 SC 381.



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pursuing his matter, it was held that there was no evidence of an agreement to accept less sum.<sup>354</sup>

### *Acceptance of payment under protest and additional work*

The contractor accepted the amount mentioned in the final bill under protest. The contractor company had performed additional work on the directions of the Department. The court said that the contractor was entitled to additional amount (or by way of damages) as per the terms of the agreement. The mere fact that the contractor had accepted the final bill, it could not be deprived of its right to claim damages for the additional work which was a provable fact.<sup>355</sup>

### **Waiver**

To “dispense with” means that the party entitled to claim performance may waive it. The Supreme Court has already laid down<sup>356</sup> that waiver is the abandonment of a right which normally everybody is at liberty to waive. “A waiver is nothing unless it amounts to a release. It signifies nothing more than an intention not to insist upon the right.”<sup>357</sup>

An extension of time for performance by mutual consent is not the same thing as a waiver. This distinction was emphasised by the Supreme Court in *M. Sham Singh v State of Mysore*.<sup>358</sup>

*M* was granted scholarship by the State for higher studies in the United States upon a bond that he would serve the State on his return, provided that the State offered him a job within six months of his return, failing which the bond was to be taken as waived. If *M* failed to comply he was to refund the scholarship money. On his request the State agreed to an extension of his stay in the States for practical training for one year. During this year he came to India for a domestic visit, but was allowed by the State to rejoin his practical training. On completion of his training he joined service in the United States and the State claimed refund of the scholarship money. He pleaded waiver on the part of the State.

The court held that there was no waiver whatsoever and *M* was liable to refund. The extension was mutually agreed upon and there was no conduct on the part of the State showing an intention to waive.

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354. *Union of India v Gangaram Bhagwandas*, AIR 1977 MP 215.

355. *R.L. Kalathia & Co v State of Gujarat*, (2011) 2 SCC 400: AIR 2011 SC 754; *National Insurance Co Ltd v Boghara Polyfab (P) Ltd*, (2009) 1 SCC 267: AIR 2009 SC 170, application for arbitration cannot be rejected on the ground that a settlement agreement or discharge voucher was executed by the claimant especially when he was disputing validity of the agreement. An undated receipt which was obtained in full and final settlement as condition for releasing the claim in return for a lesser amount was held to be unfair and illegal.

356. *Waman Shrinivas Kini v Ratilal Bhagwandas & Co*, AIR 1959 SC 689.

357. *Jagad Bandhu Chatterjee v Nilima Rani*, (1969) 3 SCC 445, 446: (1970) 2 SCR 925, 926.

358. (1973) 2 SCC 303: AIR 1972 SC 2440.

The party who has waived compliance with a particular requirement may in circumstances and by giving reasonable notice withdraw his waiver. The Court of Appeal recognised this in *Charles Rickards Ltd v Oppenheim*.<sup>359</sup>

The contract was to supply a car chassis and to build a body on it within seven months, time being of the essence of the contract. The bodywork was entrusted to a third person who was to take his instructions directly from the buyer. The contractor could not deliver within time and the buyer liberally extended time until after about two months he gave notice that if the car was not delivered within 4 weeks, he would be unable to accept it. Delivery was offered still three months after this.

It was held that the buyer had the right to make time as of the essence again by giving reasonable notice and that the notice given by him was reasonable. He had rightfully rescinded the contract and was entitled to damages for breach.

Such notice must in all the circumstances of the case give a reasonable opportunity to the other party to perform his part of the contract. If time is not otherwise of an essence of the contract, the notice cannot make it so. A party cannot unilaterally amend the terms of the contract.<sup>360</sup>

Waiver is indeed an instance of the application of the principle of promissory estoppel. In the words of Lord DENNING:<sup>361</sup> "The principle of waiver is simply this: If one party, by his conduct, leads another to believe that strict rights arising under the contract will not be insisted upon, intending that the other should act on that belief, and he does act on it, then the first party will not afterwards be allowed to insist on the strict legal rights when it would be inequitable for him to do so. There may be no consideration moving from him who benefits by the waiver. There may be no detriment to him by acting on it. There may be nothing in writing. Nevertheless, the one who waives his strict rights cannot afterwards insist on them. His strict rights are at any rate suspended so long as the waiver lasts. He may, on occasion be able to revert to his strict legal rights for the future by giving reasonable notice in that behalf, or otherwise making it plain by his conduct that he will thereafter insist upon them. But there are cases where no withdrawal is possible. It may be too late to withdraw; or it cannot be done without injustice to the other party. In that case he is bound by his waiver. He will not be allowed to revert to his strict legal rights. He can only enforce them subject to the waiver he has made."

"Instances of these principles are ready to hand on contracts for the sale of goods: A seller may, by his conduct, lead the buyer to believe that he is not insisting on the stipulated time for exercising an option.<sup>362</sup> A buyer may by requesting delivery, lead the seller to believe that he is not insisting on the

359. (1950) 1 KB 616 (CA).

360. *Bebzadi v Shaftesbury Hotels Ltd*, 1992 Ch 1: (1991) 2 WLR 1251 (CA).

361. *Allan W.J. & Co Ltd v El Nasr Export & Import Co*, (1972) 2 QB 189: (1972) 2 WLR 800.

362. *Burner v Moore*, (1904) 1 Ch 305.

contractual time for delivery.<sup>363</sup> A seller may accept a less sum for his goods than the contracted price, thus, inducing the buyer to believe that he will not enforce payment of the balance. In none of these cases does the party who acts on the belief suffer any detriment. It is not a detriment, but a benefit to him, to have an extension of time or to pay less, or as the case may be. Nevertheless he has conducted his affairs on the basis that he has that benefit and it would not be equitable now to deprive him of it."

In this case, a contract for sale of goods contained a stipulation for bank credit for the price in a certain manner. But the offer made by the confirming bank did not comply, in several respects, with what the sellers were entitled to require. For example, the confirming bank's offer was in terms of sterling currency. The sellers accepted it by sending their invoices and drafts etc. Afterwards the sterling was devalued and Tanzanian currency was not and the seller wanted to enforce his right as to payment in Tanzanian currency. But he was not allowed to do so. MEGAW LJ said: "It was not a concession for a specific period of time or one which the seller could operate for as long as they chose and thereafter unilaterally abrogate, any more than the buyers would have been entitled to alter the terms of the credit or to have demanded a refund from the sellers if, after his credit had been partly used, the relative values of the currencies had changed in the opposite way."<sup>364</sup>

### Extension of time

Section 63 also permits a party to extend time for performance. The Supreme Court has pointed out in *Keshavlal Lallubhai Patel v Lalbhai Trikumal Mills*<sup>365</sup> that the promisee cannot by unilateral act extend the time of performance of his own accord and for his own benefit. Consent of the other party is necessary.

The Privy Council held, in a case, that any of these things may be done without agreement and, therefore, also without consideration.<sup>366</sup> The commonest illustration is the release of a debt. A creditor may accept a less sum of money than what is due, in satisfaction of the whole debt. Another

363. *Charles Rickards Ltd v Oppenheim*, (1950) 1 KB 616 (CA).

364. An auction sale of scrap held by the Railway Administration was subsequently revoked and the auction purchaser accepted refund of his deposit. Held, acquiescence and no further right. *Mohd Usman v Union of India*, AIR 1982 Raj 100. *CITI Bank N.A. v Standard Chartered Bank*, (2004) 1 SCC 12: AIR 2003 SC 4630: (2003) 117 Comp Cas 554, acceptance of alternative scheme of investment, binding. *E.A. Thirugnanam v V.P. Rajagopal*, (2006) 1 CTC 809 (Mad), the purchaser of property sought refund of price which meant that he had given up his right to recover property. *Bhagawati Oxygen Ltd v Hindustan Copper Ltd*, (2005) 6 SCC 462: AIR 2005 SC 2071, continued acceptance of sub-standard oxygen and short supply without protest amounted to waiver of the right to insist upon original terms.

365. AIR 1958 SC 512: 1959 SCR 213.

366. *Firm Chhunna Mal Ram Nath v Firm Mool Chand Ram Bhagat*, (1927-28) 55 IA 154: AIR 1928 PC 99, 102, overruling the decision of Bombay High Court in *Abaji Sitaram Modak v Trimbak Municipality*, ILR (1904) 28 Bom 66. Approved by the Supreme Court in the case cited in *M. Sham Singh v State of Mysore*, (1973) 2 SCC 303: AIR 1972 SC 2440.

illustration is the decision of the Madras High Court in *Mathew Henry Abraham v Lodge "Goodwill"*:<sup>367</sup>

The plaintiff was the holder of a promissory note executed in his favour by the defendants. He agreed to abandon his claim if the "Lodge Goodwill" which was burnt down was resuscitated. The building was completed.

His subsequent claim upon the promissory note was dismissed. One of the important questions was whether a conditional remission of this kind was within the scope of the section. The court said: "The illustrations appended to the section are no doubt cases in which performance is dispensed with unconditionally. But the words of the section itself are wide enough to cover conditional releases, and there is no reason to think that the Indian Legislature contemplated a departure on this point from the English law under which a release contingent on the happening of a future event is a good release. The point on which Section 63 differs from the English law is that it does not require consideration to support a release while under English law a release without consideration is a *nudum pactum*."

The same difference between English and Indian laws was stated by the Calcutta High Court in *Manohur Koyal v Thakur Das Naskar*.<sup>368</sup> The court said: "It is quite clear that Section 63 not only modifies but is in direct antagonism to the law in England. It was laid down, as pointed out in the case of *John Weston Foakes v Julia Beer*,<sup>369</sup> that for the last pretty nearly three hundred years it has been the law in England that if A owes B five thousand rupees, and B consents to take two thousand rupees in payment of the debt that is what is called a *nudum pactum*, and that B after taking two thousand rupees can subsequently bring his action for the unpaid three thousand rupees. The law in this country by virtue of Section 63<sup>370</sup> of the Contract Act is different."

An important difference between Sections 62 and 63 is that the former, which provides for *novation*, requires an agreement based on some consideration. But Section 63 requires neither. Under this section, the promisee may before breach gratuitously release the promisor from the obligation to perform the promise.<sup>371</sup> The promisee may after breach gratuitously release the promisor from his liability arising on such breach.<sup>372</sup> As against this,

367. ILR 34 Mad 156.

368. ILR (1887-88) 15 Cal 319.

369. (1884) LR 9 AC 605.

370. See also *Ishaq Abdul Karim v Madan Lal*, AIR 1965 All 34; *Shyamnagar Tin Factory (P) Ltd v Snow White Food Product Co Ltd*, AIR 1965 Cal 541.

371. *Jitendra Chandra Roy Chowdhury v S.N. Banerjee*, AIR 1943 Cal 181, 184 and 187.

372. See *Manohur Koyal v Thakur Das Naskar*, ILR (1887-88) 15 Cal 319, 325-27 and also *Govindji Vathal Lal Bhojam v Gujarat Housing Board*, (1982) 1 SCC 412 where a works contract was prematurely terminated on account of unsatisfactory performance and subsequently the balance work was allotted to the same contractor for an agreed lump sum. The Department was not afterwards permitted to make any deductions for the earlier unsatisfactory performance.

under Section 62 *novation* agreement must be made before the breach of the original promise.

### ACCORD AND SATISFACTION

The accord is an agreement made after breach whereby some consideration other than his legal remedy is to be accepted by the party not in fault, followed by performance of the substituted consideration. The liability arising out of breach of contract may be discharged by accord and satisfaction. The validity of accord and satisfaction must be judged by the general law of contract quite apart from the provisions of Sections 62 and 63. The principle and effect of accord and satisfaction were thus explained in a decision of the Privy Council:<sup>373</sup>

“The receipt given by the appellants and accepted by the respondents and acted upon by both proves conclusively that all the parties agreed to a settlement of all their existing disputes by the arrangement formulated in the ‘receipt’. It is a clear example of what used to be well-known in Common Law pleading as ‘accord and satisfaction by a substituted agreement’. No matter what were the respective rights of parties *inter se*, they are abandoned in consideration of the acceptance by all of a new agreement. The consequence is that when such an accord and satisfaction takes place the prior rights of the parties are extinguished. They have, in fact, been extinguished by the new rights; and the new agreement becomes a new departure and the rights of all the parties are fully represented by it.”<sup>374</sup>

A contracting party in respect of his obligation towards another is released from such obligation if there is an accord and satisfaction between the two parties. The obligation need not be executed and can be executory.<sup>375</sup> In *P.K. Ramaiah & Co v NTPC*<sup>376</sup> the Supreme Court held that in view of the full and final settlement of the claim, there was an accord and satisfaction and there was no existing arbitrable dispute. Where a claim for damages was settled by the Railway by sending a cheque in full and final payment and which was to be returned if not acceptable, but the claimant encashed

373. *Payana Reena Layana Saminathan Chetty v Pana Lana Pana Lana Palaniappa Chetty*, (1913–14) 41 IA 142: 18 CWN 617, 619–20 (PC).

374. The question whether there has been an accord and satisfaction arises out of contract and can be referred to arbitration. *BHEL v Amar Nath*, (1982) 1 SCC 625.

375. *Amusu Properties v Muruchadayah*, (1989) 1 MLJ 451 (Ipoh) High Court of Ipoh.

376. 1994 Supp (3) SCC 126. See also *Nathani Steels Ltd v Associated Constructions*, 1995 Supp (3) SCC 324, parties arrived at a settlement in respect of their dispute. *Lloyds Steel Industries Ltd v Oil & Natural Gas Corp Ltd*, AIR 1997 Bom 337, payment due under a contract, accepted in full and final satisfaction under a memorandum of understanding, held, rights under the old contract ceased. *Kelkar & Kelkar v Indian Airlines*, (1996) 2 Bom CR 303, full and final settlement, payment made and accepted, no dispute left for reference to arbitration. *Camara Municipal de Bardez v V.M. Salgaonkare Irmao Ltd*, (1996) 5 Bom CR 434, rejection of the contractor's final bill on the ground that there had already been final payment was held to be wrongful because there was a factual dispute.

the cheque in protest stating that objections to encashment may be communicated within 10 days, it was held that because there was no reply from Railway, there was no mutually agreed accord and satisfaction.<sup>377</sup>

An example of accord and satisfaction is to be seen in *Kapurchand Godha v Mir Nawab Himayatalikhan Azamjah*.<sup>378</sup> The plaintiff after some initial protest expressed readiness to accept the sum sent in full satisfaction of his claim and discharge the promissory note making endorsement of full satisfaction and received the payment. In these circumstances it was held that the case was completely covered by Section 63 of the Contract Act. Another example is the decision in *Snow View Properties Ltd v Punjab & Sind Bank*.<sup>379</sup> The bank launched recovery proceedings against the borrower but compromised it if the borrower paid a certain sum of money. The borrower accepted it and paid the amount. The claim of the bank ended by accord and satisfaction. The bank was required by the court to return to the borrower his mortgage and hypothecation documents.

In a claim under a fire insurance policy, the policy holder accepted an amount by way of full and final satisfaction of his claim on the basis of the second surveyor report. The insurance company was held to be discharged from its liability.<sup>380</sup>

Where the creditor agreed that if a lesser sum than due was paid by the debtor before the specified date, it would be accepted in full satisfaction of all claims, but the debtor paid still lesser sum within the specified date, the court said that the debtor could not insist that his payment should be recorded as full satisfaction of all the claims.<sup>381</sup>

An illegal contract cannot support an accord and satisfaction.<sup>382</sup>

#### *Estoppel: Acceptance of final bill*

Where a contractor accepted the final bill without any objection and under the terms of the contract, such act had binding efficacy against him, it was held that the claim of the contractor for additional payments and damages raised two years after acceptance of the final bill was barred by estoppel.<sup>383</sup>

377. *Union of India v Navilakha & Sons*, AIR 1997 Bom 209. The court followed *Union of India v Babulal Uttamchand Bhandari*, 1967 SCC OnLine Bom 62: AIR 1968 Bom 294, where the cheque sent in full and final payment by the Railway was encashed by the claimant without even notifying that he would claim the balance amount, the claim for the balance was allowed. Payment of shorter amount could not be equated with full payment without proper acceptance. *Food Corporation of India v Ratanlal N. Gwalani*, AIR 2004 MP 215: (2004) 2 CCC 393 (MP), final bill was accepted without protest, plea was not taken in the written statement against it, not allowed to be raised in appeal. The appeal was allowed in part for reducing interest from 12 to 9 per cent.

378. AIR 1963 SC 250: (1963) 2 SCR 168.

379. AIR 2010 Cal 94.

380. *Salima Jabeen v National Insurance Co Ltd*, AIR 1999 J&K 110.

381. *Saraswat Trading Agency v Union of India*, AIR 2002 Cal 51: (2002) 1 ICC 1038.

382. *Union Carbide Corpn v Union of India*, (1991) 4 SCC 584: AIR 1992 SC 317.

383. *Govt of Gujarat v R.L. Kalathia & Co*, AIR 2003 Guj 185.

The Supreme Court has laid down that unless, while accepting the final bill the contractor unequivocally declares that he would not raise any further claim, he would not be stopped or precluded from doing so. The mere acceptance of the final bill did not have the effect of preventing the contractor from raising other claims.<sup>384</sup> Any settlement between the parties also does not have that effect unless the contract becomes a closed chapter under the settlement. If not, the arbitration clause in the contract remains and could be activated if the aggrieved party has anything more to claim.<sup>385</sup> The settlement was signed “without prejudice”. Explaining the meaning of this phrase, the Supreme Court said: “The classic definition of the phrase ‘without prejudice’ is contained in the judgment of LINDLEY LJ in *Walker v Wilsher*.<sup>386</sup> They (the words ‘without prejudice’) mean without prejudice to the position of the writer of the letter if the terms he proposes are not accepted. If the terms proposed in the letter are accepted a complete contract is established and the letter, although written ‘without prejudice’, operates to alter the old state of things and to establish a new one.”<sup>387</sup>

### MATERIAL ALTERATION

“Good faith is a continuing obligation inasmuch as even after entering into the contract, no material alteration can be made by a party in the terms of the contract without the consent of the other.”<sup>388</sup> Where a contract is embodied in a deed and the party who has the custody of the deed alters it without the consent of the other in a material particular, the effect would exactly be the same as that of cancelling the deed. Both parties will be discharged from their respective obligations. The meaning of the expression “material alteration” was considered by the Supreme Court in *Kalianna Gounder v Palani Gounder*.<sup>389</sup>

384. *Bharat Coking Coal Ltd v Annapurna Construction*, (2003) 8 SCC 154: AIR 2003 SC 3660.

385. *NTPC Ltd v Reshma Constructions, Builders & Contractors*, (2004) 2 SCC 663: AIR 2004 SC 1330: (2004) 1 KLT 1065. *Remuka Datla v Solvay Pharmaceutical B.V.*, (2004) 1 SCC 149: AIR 2004 SC 321, a very specific settlement drawn under court order, contract ended. *Cauvery Coffee Traders v Hornor Resources (International) Co Ltd*, (2011) 10 SCC 420, full and final settlement was received after acceptance of reduced price for sub-standard material supplied. The contractor became bound by estoppel, not entitled to anything after settling and receiving payment for the final bill. A party cannot be permitted to blow hot and cold at the same time, fast and loose or approve and reprobate. *Food Corporation of India v Ratanlal N. Gwalani*, AIR 2004 MP 215: (2004) 2 CCC 393 (MP), no pleading and nor issue before the trial court that final payment was accepted under accord and satisfaction, it could not be raised for the first time before the High Court. *Food Corporation of India v Ratanlal N. Gwalani*, AIR 2004 MP 215: (2004) 2 CCC 393 (MP), defence of estoppel by acceptance of final bill without protest, not raised in written statement, not allowed to be raised in appeal.

386. (1889) LR 23 QBD 335 (CA).

387. *NTPC Ltd v Reshma Constructions, Builders & Contractors*, (2004) 2 SCC 663: AIR 2004 SC 1330.

388. *United India Insurance Co Ltd v M.K.J. Corp*, (1996) 6 SCC 428: AIR 1997 SC 408.

389. (1970) 1 SCC 56: AIR 1970 SC 1942.

A memorandum of agreement for the sale of land under which Rs 2000 were paid in advance was with the plaintiff. The defendant refused to convey the land and pleaded that the plaintiff had altered the deed by adding the words that the seller shall "clear the debts and execute the sale deed free from encumbrance".

The plea was dismissed because the alleged alteration could not be proved, but SHAH J took opportunity to point out: "Even if it be assumed that the sentence regarding encumbrances was written after the deed was executed it will not invalidate the deed. Ordinarily, when property is agreed to be sold for a price, it would be the duty of the vendor to clear it of all encumbrances before executing the sale deed. The alteration, if any, cannot therefore be regarded as material."

As observed in HALSBURY'S LAWS OF ENGLAND:<sup>390</sup> "A material alteration is one which varies the rights, liabilities or legal position of the parties as ascertained by the deed in its original state, or otherwise varies the legal effect of the instrument as originally expressed."<sup>391</sup>

The same principle has been acted upon where, without the consent of the other parties, the word "partner" was deleted from a deed, the date of payment was changed from 1st to 10th and the word "and" was substituted by "or". The party making such alterations was not permitted to put the deed in the action.<sup>392</sup> Alteration of an agreement by the purchaser of land for accommodating two signatures of witnesses and to make it acceptable as a sacrosanct document was held to have discharged the agreement.<sup>393</sup> This judgment was reversed by the Supreme Court on appeal. The court said that the two independent persons were introduced as marginal witnesses. Such a change did not affect the validity or enforceability of the agreement. It was not a material alteration. It did not have the effect of avoiding the agreement.<sup>394</sup>

Materiality of the *unilateral amendment* is the most important factor. In a contract containing an arbitration clause, the Government made the unilateral amendment to the effect that the arbitral award must be reasoned. The alteration was held to be not binding upon the parties. The Government was not allowed to avoid the award on the ground that the award was without a statement of reasons.<sup>395</sup>

390. Vol II, 3rd Art. 599 at p. 368.

391. Applied by the Privy Council in *Nathu Lal v Gomti Kuar*, (1939–40) 67 IA 318.

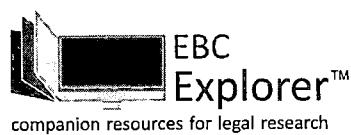
392. *Loonkaran Sethiya v Ivon E. John*, (1977) 1 SCC 379: AIR 1977 SC 336. An immaterial alteration does not discharge. *M.S. Anirudhan v Thomco's Bank Ltd*, AIR 1963 SC 746: (1963) 1 SCR 63: (1963) 33 Comp Cas 185.

393. *Sardar v Ram Khilona*, AIR 1998 All 268.

394. *Ram Khilona v Sardar*, (2002) 6 SCC 375: AIR 2002 SC 2548.

395. *Build India Construction System v Union of India*, (2002) 5 SCC 433: AIR 2002 SC 2437.

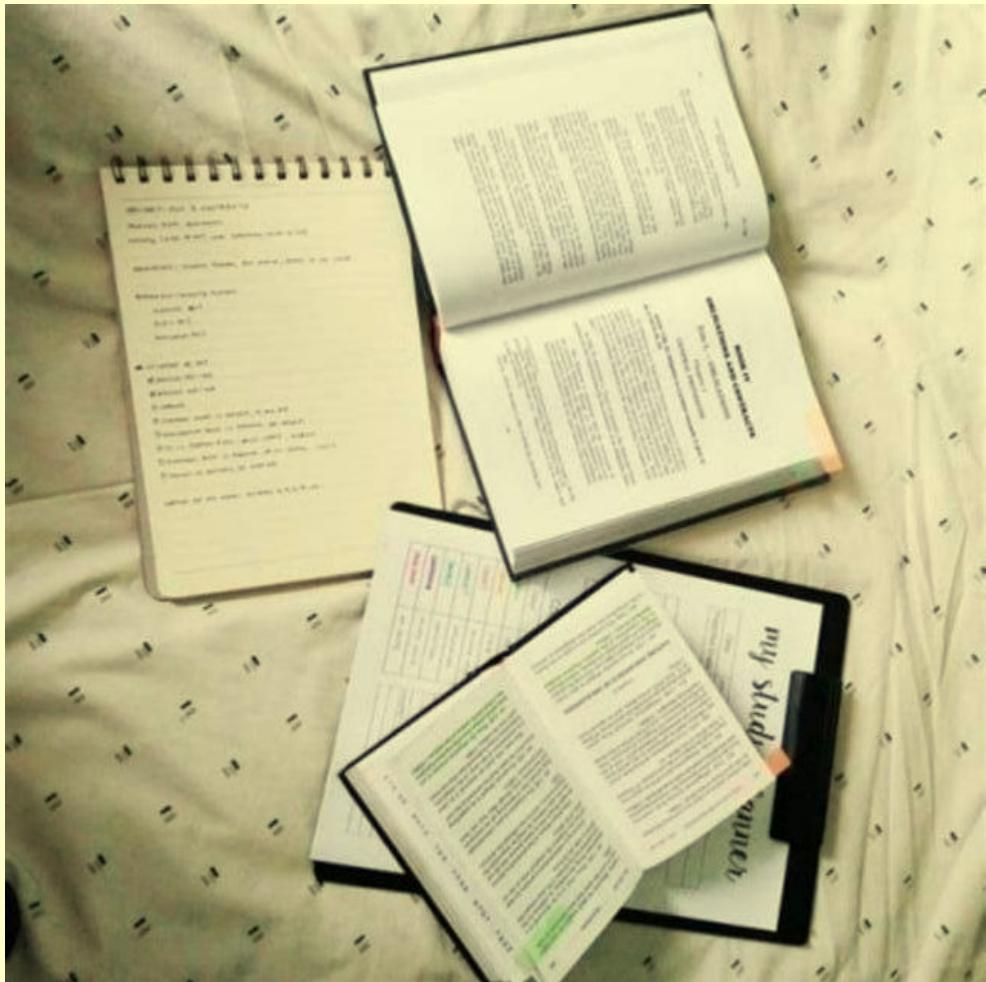
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**The following cases from this chapter are available through EBC Explorer™:**

- *Alopi Parshad & Sons Ltd v Union of India*, AIR 1960 SC 588: (1960) 2 SCR 793
- *Easun Engg Co Ltd v Fertilisers and Chemicals Travancore Ltd*, AIR 1991 Mad 158
- *Kapurchand Godha v Mir Nawab Himayatalikhan Azamjahan*, AIR 1963 SC 250: (1963) 2 SCR 168
- *Naihati Jute Mills Ltd v Khyaliram Jagannath*, AIR 1968 SC 522: (1968) 1 SCR 821
- *Punj Sons (P) Ltd v Union of India*, AIR 1986 Del 158
- *Satyabrata Ghose v Mugneeram Bangur & Co*, AIR 1954 SC 44: 1954 SCR 310

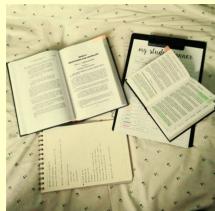




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# Discharge by Breach

## DISCHARGE BY BREACH

“A breach of contract occurs when a party thereto renounces his liability under it, or by his own act makes it impossible that he should perform his obligations under it or totally or partially fails to perform such obligations.”<sup>1</sup> The failure to perform or renunciation may take place when the time for performance has arrived or even before that. Thus, breach is of two kinds, namely:

- (1) anticipatory breach, and
- (2) present breach.

## ANTICIPATORY BREACH

### Meaning

“An anticipatory repudiation occurs when, prior to the promised date of performance, the promisor absolutely repudiates the contract.”<sup>2</sup> It is an announcement by the contracting party of his intention not to fulfil the contract and that he will no longer be bound by it. This kind of anticipatory renunciation has certain effects upon the rights of the parties.

### Effect upon rights

#### *Innocent party excused from further performance*

In the first place, the other party is excused from performance or from further performance. The obligation under the original contract comes to an

1. This definition of breach appears in *Associated Cinemas of America, Inc v World Amusement Co*, (1937) 201 Minn 94 (Minnesota SC); Collected from Shepherd and Wellington, CONTRACTS AND CONTRACT REMEDIES (4th Edn, 1957) 805. *Chowgule & Co Ltd v Rizvi Estates and Houses (P) Ltd*, (1997) 4 Bom CR 648, premises were handed over to the builder for development. For years (over six years) the builder commenced no work, contract broken by him by abandonment. Liability fixed in the contract at Rs 10,000 per month for breach was reduced to Rs 3000. *U.P. State Sugar Corpn v Mahalchand M. Kothari*, (2005) 1 SCC 348: AIR 2005 SC 61, breach of contract on the part of receiver of property.
2. See *A Suggested Revision of the Contract Doctrine of Anticipatory Repudiation*, (1954) 64 Yale Law Journal 85. It is necessary that the refusal should have been communicated to the other party and should make the intention not to perform quite explicit. *Dhanraj Mills Ltd Liability Co v Narsingh Prasad Boobna*, AIR 1949 Pat 270: (1949) 27 Pat 723; *E.E. Master v Garret & Taylor Ltd*, (1931) 131 IC 220: AIR 1931 Rang 126. *Pratap Constructions v State of Jharkhand*, (2005) 1 BLJR 492 (Jhar), premature cancellation of transportation contract without any justification, the court said that the cancellation was not justified.

end and is replaced by operation of law by another obligation, namely to pay money damages. The only legal nexus that remains between the parties is to pay the damages which are assessed according to the old obligation but the old obligation no longer exists as an obligation.<sup>3</sup>

### *Options of injured party*

*IMMEDIATE RIGHT OF ACTION.*—Secondly, it entitles the injured party to an option either to sue immediately or to wait till the time the act was to be done. That an anticipatory breach gives an immediate right of action was recognised as early as (1853) in *Hochester v De La Tour*:<sup>4</sup>

The plaintiff was a courier. He was engaged by the defendant to accompany him on a tour to commence on June 1, 1852. Nearly a month before this date the defendant wrote to the plaintiff that he had changed his mind, and declined his services. The plaintiff sued him for damages for breach. The defendant's counsel very powerfully contended that there could be no breach of the agreement before the day when the performance was due.

But Lord CAMPBELL CJ ruled out the objection. His Lordship said: "It cannot be laid down as universal rule that, where by agreement an act is to be done at a future date, no action can be brought for a breach of the agreement till the day for doing the act has arrived. If a man promises to marry a woman on a future day, and before that day marries another woman, he is instantly liable to an action for breach of promise of marriage.<sup>5</sup> If a man contracts to execute a lease on and from a future day for a certain term, and before that day executes a lease to another person for the same term, he may be immediately sued for breaking the contract.<sup>6</sup> So, if a man contracted to sell and deliver specific goods on a future day and before the day he sells and delivers them to another, he is immediately liable to an action at the suit of the person with whom he first contracted to sell and deliver....<sup>7</sup> It seems strange that the defendant, after renouncing the contract, and absolutely declaring that he will never act under it, should be permitted to object that

3. *Moschi v Lep Air Services Ltd*, 1973 AC 331: (1972) 2 WLR 1175 (HL). A party cannot by refusing to accept repudiation create liability in perpetuity. See *Pusapati Krishna Murthy Raju v A.P. SEB*, (1996) 4 An LT 822, electricity permanently disconnected within 2 years whereas the supply was agreed to be for a term of 10 years. The court allowed recovery of minimum charges only for a period of 5 years and not for the whole period of 10 years.

4. Court of Queen's Bench, (1853) 2 Ellis and Blackburn 678: 95 RR 747: 118 ER 922. *Nannier v N.M. Rayalu Iyer*, AIR 1926 Mad 778: ILR (1925) 49 Mad 781, grounds of refusal to accept goods cannot afterwards be changed. *British and Beningtons Ltd v N.W. Cacher Tea Co*, 1923 AC 48, 62, total refusal; *Narasimha Mudali v Narayanaswami Chetty*, 1925 SCC OnLine Mad 157: (1925) 22 LW 637; *Bhai Jawahar Singh v Secy of State*, AIR 1926 Lah 292, repudiation conclusive against party. A right of this kind was in recognition even before the Contract Act. *Mansuk Das v Rangayya Chetti*, 1 Mad HC 162 and in subsequent case also. *Steel Bros & Co Ltd v Dayal Khatao & Co*, ILR (1923) 47 Bom 924.

5. *Short v Stone*, (1846) 8 QB 358: 15 LJ QB 143.

6. *Ford v Tiley*, 6 B&C 325.

7. *Bowdell v Parsons*, (1808) 10 East 359: 103 ER 811.

faith is given to his assertion, and that an opportunity is not left to him of changing his mind .... The man who wrongfully renounces a contract into which he has deliberately entered cannot just complain if he is immediately sued for a compensation in damages by the man whom he has injured."

*ANTICIPATORY BREACH OF A CONTINGENT CONTRACT.*—Even when the performance of a contract is conditional upon the happening of a contingency, an immediate action for damages will lie, if before the happening of the contingency, the promisor disables himself from performance. *Frost v Knight*<sup>8</sup> is the well-known illustration.

The defendant promised to marry the plaintiff on the death of his father. The father still living, the defendant announced his intention of not fulfilling his promise on his father's death, and broke off the engagement. The plaintiff, without waiting for the father's death, at once brought an action for the breach.

The defendant contended that a breach could only arise on the happening of the contingency. But COCKBURN CJ held that "the case falls within the principle of *Hochester v De La Tour*<sup>9</sup> and that consequently, the present action is well brought". His Lordship said that when a contracting party announces his intention not to fulfil the contract, the contract should be taken to be broken as all its incidents "and the damages consequent on non-performance being assessed at the earliest moment, many of the injurious effects of such non-performance may possibly be averted or mitigated.... To hold that the aggrieved party must wait until the time fixed for marrying shall have arrived would have the effect of aggravating the injury, by preventing the party from forming any other union, and by reason of advancing age rendering the probability of such a union constantly less".<sup>10</sup> In another case<sup>11</sup> of this kind, a ship was the subject-matter of a charter-party. One of the terms was that if the ship was requisitioned for war purposes, the hire would not be payable during the period of requisition. The ship was requisitioned and during that period the shipowner sold her away. This was regarded as repudiation because by selling off the ship, he had made it beyond his power to restore it back under the charterparty.

#### *Consequences of aggrieved party waiting for performance*

The option is with the aggrieved party to sue at once or wait for performance.<sup>12</sup> "The promisee, if he pleases, may treat the notice of intention as

8. (1872) LR 7 Exch 111.

9. (1853) 2 E&B 678: 22 LJ QB 455.

10. *Per* COCKBURN CJ in *Frost v Knight*, (1872) LR 7 Exch 111.

11. *Omnium D'Enterprises v Sutherland*, (1919) 1 KB 618: 120 LT 265. A bank cannot unilaterally terminate an overdraft arrangement even if it is temporary. It was no justification to say that the arrangement had already lasted for 4 years or that the customer was not required to execute any formal document. *Indian Overseas Bank v Naranprasad Govindlal Patel*, AIR 1980 Guj 158.

12. *Forcometal SARL v Mediterranean Shipping Co SA*, 1989 AC 788 (HL).

inoperative, and await the time when the contract is to be executed, and then hold the other party responsible for all the consequences of non-performance; but in that case he keeps the contract alive for the benefit of the other party as well as his own; he remains subject to all his obligations and liabilities under it, and enables the other party not only to complete the contract, if so advised, notwithstanding his previous repudiation of it, but also to take advantage of any supervening circumstance which would justify him in declining to complete it.”<sup>13</sup> The acceptance of the repudiation must be made clear to the repudiating party. “An act of acceptance of a repudiation requires no particular form: a communication does not have to be couched in the language of acceptance. It is sufficient that the communication or conduct clearly or unequivocally conveys to the repudiating party that the aggrieved party is treating the contract as at an end. The aggrieved party need not personally, or by an agent, notify the repudiating party of his intention to treat the contract as at an end. It is sufficient that the fact of the acceptance comes to the aggrieved party’s attention, for example, notification by an unauthorised broker or other intermediary may be sufficient.”<sup>14</sup>

If the aggrieved party does not accept the repudiation and leaves the contract alive, the consequences will be as follows:

*PARTY REPUDIATING MAY CHOOSE TO PERFORM.*—Firstly, the party repudiating the contract may nevertheless choose to perform when the time comes and the promisee will be bound to accept the same.<sup>15</sup> The party keeping the contract alive is not absolved from tendering further performance of his own obligation under the contract. Accordingly, if a repudiation by anticipatory breach is followed by affirmation of the contract the repudiating party would escape liability if the affirming party is subsequently in breach of contract. In this case the charterer refused to load the ship but the owner of the ship affirmed that the contract was still alive and yet failed to make the ship ready to load on the day specified, he became liable for breach of contract.<sup>16</sup>

*PREMATURE TERMINATION OF CONTRACT OF EMPLOYMENT.*—The principle is applicable to premature termination of a contract of employment.<sup>17</sup> If the employee does not accept the repudiation, the contract remains alive whether he is permitted to perform his duties or not. A managing director was removed before the expiry of his three-year term and was sought to be

13. Once the aggrieved party has exercised the option the party in default cannot say that contract still subsists. *Jhandoo Mal Jagan Nath v Phul Chand Fatesh Chand*, AIR 1925 Lah 217.

14. *Vitol S.A. v Norelf Ltd*, 1996 AC 800: (1996) 3 WLR 105 (HL). Here the buyer confronted with falling prices and some delay in the loading of the ship, repudiated the contract. The seller received the notice of repudiation after the ship had sailed away. He did nothing further and sold the goods to another party. This was held to be a sufficient acceptance of the repudiation.

15. *Phul Chand Fateh Chand v Jugal Kishore Gulab Singh*, AIR 1927 Lah 693.

16. *Fercometal SARL v Mediterranean Shipping Co SA*, 1989 AC 788 (HL).

17. Contracts of employment are no exception to the general rule. See *Thomas Marshall (Export) Ltd v Guinle*, 1979 Ch 227 and *Gunton v Richmond-Upon-Thames London Borough Council*, 1981 Ch 448: (1980) 3 WLR 714 (CA).

replaced by another appointee. He did not accept the termination. The court said that no injunction could be granted to him to prevent the employer from committing breach of contract of personal service the performance of which cannot be specifically enforced. But where a contract of personal service contains both positive and negative covenants either express or implied, an injunction to enforce the negative covenant is often granted. As such, the injunction to enforce the positive covenant, *i.e.* to employ the plaintiff as managing director was not allowed. However, the injunction to enforce the implied negative covenant, *i.e.* not to appoint someone else until the expiration of the plaintiff's period was allowed.<sup>18</sup>

An employment is also the subject-matter of a contract. Unless it is governed otherwise by a statute or rules framed under it, the provisions of the Contract Act would be applicable to the formulation and termination of a contract of employment. Subject to certain exceptions, even specific performance of such a contract by way of a direction for reinstatement of a dismissed employee is also permissible in law.<sup>19</sup>

Termination of the contract occurs not on the date when the repudiatory act is done, but from the time the party who is sinned against elects to treat the wrongful act of the other as a breach of the contract.<sup>20</sup>

**NEGATIVE INJUNCTION.**—This is the other side of the old principle of *Lumley v Wagner*<sup>21</sup> where it was considered as well-settled that the courts have jurisdiction to forbid the infringement of a negative stipulation, even though it is necessary to a positive covenant for the performance of personal services. In that case, the defendant had agreed that she would sing at the plaintiff's theatre for three months and would not sing elsewhere during that period. This negative side of the covenant was enforced. Such a negative may, perhaps, produce a positive response to go to the opening at hand when all other theatres are fore-closed. "Thus injunctions have been issued in the case of agreements not to sing elsewhere than at the plaintiff's theatre, not, during the period of employment, to engage in any business similar to that carried on by the employer<sup>22</sup>, and not, during the period of employment, to act as a film artiste for any motion picture company other than the employers."<sup>23</sup>

**WHERE NEGATIVE INJUNCTION NOT ISSUED.**—The cases in which a negative injunction would not be issued were explained in a case where an injunction

18. *Datu Abdullah bin Ahmad v Syarikat Permodalan Kebangsaan*, (1990) 2 Cur LJ 48.

19. *Bank of India v O.P. Swarnakar*, (2003) 2 SCC 721: AIR 2003 SC 858.

20. *Per Bowen LJ in Boston Deep Sea Fishing & Ice Co v Ansell*, (1888) LR 39 Ch D 339, 365 (CA). The Privy Council case of *Jerome Francis v Municipal Councillors of Kuala Lumpur*, (1962) 1 WLR 1411 (PC), must be viewed in its proper perspective.

21. (1852) 1 De GM & G 604.

22. *William Robinson & Co Ltd v Heuer*, (1898) 2 Ch 451 (CA).

23. *Warner Bros Pictures Inc v Nelson*, (1937) 1 KB 209; *Marco Productions Ltd v Pagola*, 1945 KB 111. The quotation is from *Cheshire & Fifoot, LAW OF CONTRACT* (9th Edn, 1976) 615–16.

was sought against the boxer who was leaving and the manager who was taking him in.<sup>24</sup> The court said:

Where a third party induced a breach of a contract for personal services between a master and a servant or a manager and a performer and the contract involved the servant or performer exercising some special skill or talent and contained both positive and negative obligations by the servant or performer (e.g. not to enter into an agreement with any other master or manager), the court ought not to enforce the performance of the negative obligations if enforcement of them would have the effect of compelling the servant or performer to perform his positive obligations under the contract. Whether the grant of an injunction would be held to result in compulsion directed towards the servant or performer depended on the court taking a realistic approach on the facts of each case, to the probable effect of an injunction on the psychological, material or physical need of the servant or performer to maintain his skill or talent, but compulsion would be more readily inferred where a longer term injunction was sought by the master or manager or where the third party was the only other available master or manager for the servant or performer or where the original master or manager was likely to seek injunctive relief against anyone else who attempted to replace him as master or manager. Furthermore, the court would be less likely to grant an injunction where the contract of service contained obligations of mutual trust and confidence between the master and servant or manager and performer and the servant or performer had genuinely lost confidence in the master or manager. Moreover, since damages as an alternative remedy to an injunction were invariably assessed by the court it ought not to be assumed that an award of damages for inducing breach of a contract for personal services would always be an inadequate alternative to the grant of an injunction. On the other hand, having regard to the sanctity of contracts, the court ought to scrutinise most carefully and even sceptically any claim by the servant or performer that he was under the human necessity of maintaining his skill or talent or that his trust in the master or manager had been betrayed or that his confidence in him had genuinely gone. On the facts, the grant of the injunctions sought would have the effect of compelling the boxer to perform his positive obligations under the contract if he was to maintain his skill or talent as a boxer when he had genuinely lost confidence in the plaintiff's ability to act as his manager. The injunctions had, therefore, rightly been discharged.

*DISCHARGE BY ANY OTHER EVENT MAY BENEFIT BOTH.*—Secondly, if while the contract is lying open, some event happens which discharges the contract otherwise than by repudiation, for example, by supervening impossibility or frustration, the promisor would also be entitled to take the advantage of

24. *Warren v Mendy*, (1989) 1 WLR 853 (CA).

the changed circumstances. The most appropriate illustration is *Avery v Bowden*.<sup>25</sup>

The defendant chartered the plaintiff's ship and agreed to load it with a cargo at Odessa within forty-five days. On arrival of the ship there the defendant told the captain that he had no cargo for him and requested him to go away. The captain, however, stayed there in the hope that the defendant would fulfil his contract. But, before the expiry of forty-five days, a war broke out which rendered the performance illegal. The plaintiff then brought an action for breach.

It was held that the contract had ended by frustration and not by breach. It was open to the captain to accept the renunciation and in that case "he would have had a right to maintain an action on the charterparty to recover damages equal to the loss he had sustained from breach of the contract on the part of the defendant". But he continued to insist upon having a cargo in fulfilment of the charterparty and, therefore, the contract was still open when the war intervened.

Where no other event intervenes to discharge the contract otherwise, the innocent party who kept waiting up to the last day of performance, may now sue for breach.<sup>26</sup>

*DATE OF ASSESSMENT OF DAMAGES.*—Thirdly, in case the anticipatory repudiation is accepted, damages for breach would be assessed at the time when repudiation takes place. In *Ramgopal v Dhanji Jadhavji Bhatia*.<sup>27</sup>

The defendants, the owners of a ginning mill, contracted with the plaintiff, a cotton merchant, to use half the mill's working capacity for ginning his cotton. But the defendant repudiated the contract before any cotton was supplied or ginned.

The plaintiff was held entitled to recover the estimated loss of profits at the time of repudiation. Lord SUMMER said: "This was a case of anticipatory breach. The contract was repudiated almost as soon as it was made, and, the intended operation being thus baulked, the plaintiff was entitled to measure his damages as they then stood and could not be required by the defendants to buy the cotton, which they had announced in advance they would not gin for him."

Where, on the other hand, the promisee does not accept the anticipatory repudiation, damages will be assessed at the time fixed for performance and the promisee takes the risk of market rate falling and in the meantime

25. (1855) 5 E & B 714: 25 LJ QB 49: 103 RR 695: 119 ER 647: 27 LJ 119.

26. *Clea Shipping Corp v Bulk Oil International Ltd*, (1984) 1 All ER 129, the owner kept waiting up to the last day of the time charterparty. *Ishwarappa v Arunkumar*, 2004 AIR Kant HCR 2273: AIR 2004 Kant 417, an ordinary power of attorney for construction of house was held to be revocable because the agent was not authorised to spend anything from pocket or to raise loans.

27. (1927-28) 55 IA 299: AIR 1928 PC 200; *Millet v Van Heek & Co*, (1921) 2 KB 369 (CA).

he will have to take all reasonable steps to keep his loss to the minimum.<sup>28</sup> Thus, the law is as stated in plain and simple terms in the speech of Viscount SIMON LC in *Heyman v Darwins Ltd*:<sup>29</sup>

...repudiation by one party standing alone does not terminate the contract. It takes two to end it, by repudiation, on the one side, and acceptance of the repudiation, on the other.

Whether the other party accepts is a matter for his option; if he does not, the contract remains alive, as was emphasised by the House of Lords in *White & Carter (Council) Ltd v McGregor*.<sup>30</sup>

A contract for display advertisement for 3 years of a motor garage business was struck between advertisement contractors and the agent of the garage owner, but the latter repudiated the contract by writing a letter of cancellation. The contractors refused this request and displayed the advertisement. The contract provided for annual payments and in default the payment for all the three years was to become due. Accordingly, the contractors claimed full payment.

The House of Lords held that the contractors were only claiming what was due to them under the contract and, therefore, were entitled to it. They had the right to reject the repudiation. Lord HODSON considered the principle to be well-established:

It is settled as a fundamental rule of the law of contract that repudiation by one of the parties to a contract does not itself discharge it ....

In *Howard v Pickford Tool Co Ltd*<sup>31</sup> ASQUITH LJ said: "An unaccepted repudiation is a thing writ in water and of no value to anybody: It confers no legal rights to any sort or kind." It follows that, if, as here, there was no acceptance, the contract remains alive for the benefit of both parties and the party who has repudiated can change his mind but it does not follow that

28. *Mackertich v Nobo Coomar Roy*, ILR (1903) 30 Cal 477. Where the contract was to be performed in instalments, the date of each instalment would be the day for taking the differences in market and contract prices. *Brown v Muller*, (1872) LR 7 Exch 319. *Roper v Johnson*, (1873) LR 8 CP 167.

29. (1942) AC 356, 361. Similarly, it has been held by the Supreme Court in *State of Kerala v Cochin Chemical Refineries Ltd*, AIR 1968 SC 1361: (1968) 3 SCR 556, that by refusing to advance the loan which the State had undertaken to advance, its obligation to purchase groundnut cake from the company came to an end. The contract does not terminate unless the repudiation is accepted by the other party.

30. 1962 AC 413: (1962) 2 WLR 17 (HL).

31. (1951) 1 KB 417. For a study of this case see Nienaber, *The Effect of Anticipatory Repudiation: Principle and Policy*, (1962) Camb LJ 213; Tabachunik, *Anticipatory Breach of Contract*, 1972 Current Legal Problems, 149. The Supreme Court of India has held in *Aslbing v L.S. John*, (1984) 1 SCC 205: AIR 1984 SC 988, that whatever implications the acceptance by the other party may have for remedial purposes, so far as the repudiating party is concerned he becomes free from the contract to the same extent as if the contract has ended. The disqualification, if any, for election purposes by virtue of the contract would immediately end. *Magnum Films v Golcha Properties (P) Ltd*, AIR 1984 Del 162, unilateral alteration of terms amounts to breach.

the party at the receiving end of the proffered repudiation is bound to accept it before the time for performance and is left to his remedy in damages for breach.

#### *Premature termination of lease*

Where a three-year use of premises on lease was terminated by the lessee before the expiry of the period, the court allowed the lease-money for the unexpired period by way of damages, the specific enforcement being not possible.<sup>32</sup>

#### *What constitutes acceptance of repudiation*

In a case<sup>33</sup> where the buyers refused to accept the cargo because of delay in loading and the seller remained silent about the matter and the question was whether the repudiation had been accepted, the court explained the requirement of acceptance as follows:

“It is this ability of the innocent party to choose between acceptance of the repudiation and affirmation of the contract, courses attended by immediate and differing consequences, that makes it necessary, as it has repeatedly been held, for the choice of the former to be clear and unequivocal. While in human affairs, a choice may be made by thought, word or deed, it can only be manifested by word or deed. A choice, however resolute, which gains no expression outside the bosom of the chooser cannot be clear and unequivocal in the sense that the law requires. Silence and inaction, being in the generality of cases equally consistent with an affirmation of the contract, cannot constitute acceptance of a repudiation.”

#### *What amounts to repudiation*

In considering whether there has been a repudiation of a contract by a party, the whole conduct of that party has to be assessed objectively in order to see whether there was an intention to abandon and refuse performance of the contract. Repudiation is a drastic conclusion which should only be held to arise in clear cases of a refusal, in a manner going to the root of the contract to perform contractual obligations.<sup>34</sup> Every minor irregularity in

32. *Food Corporation of India v Babulal Agarwal*, AIR 1998 MP 23.

33. *Vitol S.A. v Norelif Ltd*, 1996 AC 800: (1996) 3 WLR 105 (HL).

34. See the observation of Lord WILBERFORCE in *Woodar Investment Devp Ltd v Wimpey Construction UK Ltd*, (1980) 1 WLR 277 (HL). Applying this to the facts of the case, the court held that a party giving notice of rescission in terms of the provisions of the contract for purchasing land entitling him to rescind the contract if the land came under compulsory acquisition under a statutory power, would not amount to repudiation even if there was a mistaken notion as to the legal position of acquisition. The decision in *Nottingham Building Society v Eurodynamics Systems plc*, 1995 FSR 605 (CA) also shows the importance of contract terms in the matter of repudiation. The contract was for supply of computer software. The contract provided that the supplier would deliver up the software and other documentation (including source codes) inspite of any termination of the contract by the purchaser. The supplier failed to maintain delivery time-schedule until he was provided with further funds which the purchaser could not do, and demanded delivery up of the software and documentation. The court

the performance of a contract cannot be seized upon as a repudiation so as to put a premature end to the contract. The court has to take into account the effect of the breach upon the contract as a whole. Thus, in a contract for the supply of 100 tons of flock of Government standard to be delivered by instalments, the sixteenth delivery was below the standard and the buyer attempted to treat this as a repudiation, but the court held that the seller's conduct did not show an intention to throw away the contract and, therefore, the buyer should have to be content with damages for defective goods.<sup>35</sup> Lord HEWART CJ concluded:

With the help of these authorities we deduce that the main tests to be considered... are, first the ratio quantitatively which the breach bears to the contract as a whole, and, secondly, the degree of probability or improbability that such a breach will be repeated. On the first point the delivery complained of amounts to no more than 1½ tons out of a contract for 100 tons. On the second point, our conclusion is that the chance of the breach being repeated is practically negligible.... The delivery complained of was an isolated instance out of twenty satisfactory deliveries actually made both before and after the instalment objected to; we hold that it cannot reasonably be inferred that similar breaches would occur in regard to subsequent deliveries.

Similarly, in a contract for supply of iron by two instalments, payment to be made within fourteen days of delivery, the buyer claimed reduction in price on account of the delay in the first delivery and the seller treating this as repudiation refused to make further deliveries, it was held that the conduct complained of did not amount to an intimation of an intention to abandon and altogether refuse performance of the contract.<sup>36</sup>

In a subsequent case,<sup>37</sup> the Court of Appeal pointed out "that to constitute repudiation, a breach of contract must go to the root of the contract.... This constitutes the test even where there are recurring breaches—producing different results according to the degree of non-compliance.... Notice that a breach is likely to occur or recur cannot, of course, be treated as being a repudiation unless it would have that effect when it did occur or recur."<sup>38</sup>

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said that there was no repudiation on the part of the purchaser and he was entitled under the contract terms to a mandatory injunction for the supply. See also *Saphena Computing v Allied Collection Agencies*, 1995 FSR 616 DC, where the contract for supply of software for debt collection business was terminated by mutual consent, yet litigation arose because of copyright problems in the material already supplied. *Vaswani v Italian Motors (Sales and Services) Ltd*, (1996) 1 WLR 270, here a car was booked at a stated price with some money deposited in advance. The seller asked the buyer to pay the increased price and on his refusal to do so, forfeited the advance. The Privy Council held that the terms of the contract did not permit recovery of increased price, but that there was no repudiation on the part of the supplier, the buyer was bound to take the vehicle at the booked price.

35. *Maple Flock Co Ltd v Universal Furniture Products (Wembley) Ltd*, (1934) 1 KB 148 (CA).

36. *Freeth v Burr*, (1874) 43 LJ CP 91.

37. *Decro-Wall International SA v Practitioners in Mktg Ltd*, (1971) 1 WLR 361 (CA).

38. In *M.P. Mines Ltd v Rai Bahadur Shriram Durga Prasad (P) Ltd*, (1972) 3 SCC 180: AIR 1971 SC 1983, the Supreme Court held that where the samples of manganese to be supplied

Applying this test to the facts of the case before him, his Lordship held that repeated delay in payment ranging from 2 to 20 days and averaging 8 days and causing a nominal loss to the plaintiff which he could have debited to the defendant's account but did not do so, such defaults even if repeated could not go to the root of the contract. The plaintiffs, a French firm, were marketing their goods in the United States through the defendant firm.

Failure to perform as the occasion arises under the contract may entitle, depending upon the terms of the contract, the other party to treat that as a repudiation.

A shipping contract incorporated the rules requiring sellers to have the cargo ready for delivery at any time within the contract period. The buyers gave a proper notice of their readiness to take the load. The sellers failed to deliver the cargo on presentation of buyers' vessel. The buyers took this failure as a repudiation and terminated the contract.<sup>39</sup>

It was held that the rule in question imposed an additional obligation on the sellers to have the cargo ready for the buyers to begin loading without delay or interruption as soon as the vessel was ready to load the cargo in question. The justification for this rule is that mercantile contracts are concluded with a reasonably long period of delivery and at a price which presupposes the buyers' right to call for delivery at any time having given reasonable notice. That was a valuable option which the buyers would lose if the sellers were entitled to deliver whenever they were willing and able to do so within the delivery period. Accordingly, the sellers were in breach of their obligation. This entitled the buyers to put an end to the contract. They were allowed to recover by way of damages the difference between the market price of the replacement cargo and the original contract price and loss of dispatch.

In an agreement for sale of certain shares at a price to be fixed by a third party valuer, the Supreme Court held that a challenge to the valuation did not amount to a repudiation of the contract. Such challenge is only an attempt to ensure a fair price. An act to constitute repudiation must be such as indicates an intention to refuse to perform the contract and to set the other party free from performing his part.<sup>40</sup>

Section 39 of the Indian Contract Act gives expression to the doctrine of anticipatory breach.

**S. 39. Effect of refusal of party to perform promise wholly.**—When a party to a contract has refused to perform, or disabled himself from performing his promise in its entirety, the promisee may put an end to the contract, unless he has signified, by words or conduct, his acquiescence in its continuance.

under a contract were to be approved by both parties, the seller's default in giving the opportunity to the buyer to check them was a breach on his part.

39. *Compagnie Commerciale Sucres Et Denrees v C. Czarnikow Ltd*, (1990) 1 WLR 1337 (HL). The term was in accordance with Rule 14(1) of the RSA rules.

40. *Claude-Lila Parulekar v Sakal Papers (P) Ltd*, (2005) 11 SCC 73: (2005) 124 Comp Cas 685.

*Illustrations*

- (a) A, a singer, enters into a contract with B, the manager of a theatre, to sing at his theatre two nights in every week during the next two months, and B engages to pay her 100 rupees for each night's performance. On the sixth night A wilfully absents herself from the theatre. B is at liberty to put an end to the contract.
- (b) A, a singer, enters into a contract with B, the manager of a theatre, to sing at his theatre two nights in every week during the next two months, and B engages to pay her at the rate of 100 rupees for each night. On the sixth night, A wilfully absents herself. With the assent of B, A sings on the seventh night. B has signified his acquiescence in the continuance of the contract, and cannot now put an end to it, but is entitled to compensation for damage sustained by him through A's failure to sing on the sixth night.

### Breach in entirety

The party in default must have refused altogether to perform the contract and the refusal must go to the whole of the contract, otherwise the other party would not be justified in putting an end to the contract. Thus, in *Rash Behary Shaha v Nirttya Gopal Nundy*:<sup>41</sup>

A agreed to purchase from B under two contracts 300 tons of sugar to be delivered at different dates. A having failed to take delivery under the first contract, B claimed to rescind both contracts.

The Calcutta High Court held that as there was no refusal on the part of A to perform his promise in its entirety within the meaning of Section 39, B was not entitled to rescind the contract. The decision of the same court in *Schiller v Sooltan Chand*<sup>42</sup> emphasises the same point.

There was a contract for the sale of 200 tons of linseed oil in April and May, to be paid for on delivery. Some deliveries were made and the plaintiffs made part payment for the same withholding the balance for adjustment of their claims. But the defendants, taking that as an anticipatory repudiation, refused to make further supplies and the plaintiffs sued them for the breach.

It was held that the withholding of a part payment under a *bona fide* claim cannot be regarded as a refusal to perform the contract in its entirety.

At first sight these decisions seem to be at variance with the illustrations in Section 39. According to the illustrations if a singer agrees to sing at a theatre for two nights in a week for a period of two months and then absents herself on one night, the other party is at liberty to put an end to the contract. Referring to the illustrations, GARTH CJ observed as follows:

That illustration is perhaps not a happy one, because it may lead to misapprehension. The singer by willfully absenting herself, though on one night only, did in fact refuse altogether to perform an integral and

41. (1928-29) 33 CWN 477. *P.C. Rajput v State of M.P.*, AIR 1993 MP 107: (1994) 1 MPLJ 387, delay on the part of the Government in handing over site to the contractor does not constitute such a fundamental breach or breach in entirety to entitle the contractor to sue the Government for breach after putting an end to the contract.

42. ILR (1878) 4 Cal 252.

essential part of her contract. By doing so she put it out of her power to perform her contract in its entirety. But here the plaintiffs have never refused to perform any part of their contract. They were willing to pay the sum due as soon as their cross-claims were adjusted.<sup>43</sup>

### *Partial failure going to the root*

Whether a partial failure goes to the root of the contract or not is a question of fact in each case. In a case before the Supreme Court:<sup>44</sup>

There was a contract for the sale of B Twill and Hessian deliverable in the months of April, May and June. April and May quota of B Twill and April quota of Hessian were delivered and they were accepted and paid for by the buyer. For the rest the sellers sent to the buyers delivery orders on certain mills asking them to take goods directly from the mills. The orders reached the buyers through the hands of several middlemen. They contained conditions different from the contract and required the buyer to take goods subject to the conditions imposed by the mills. The buyer refused to accept. The court held that the sellers were in breach of their contract.<sup>45</sup>

A contract was made for supply of human albumin. Deliveries were to be effected within the course of one year by monthly instalments. Time of delivery was to be important. No monthly quantity was fixed. Any shortfall in one month could be made up in subsequent months. The sellers failed. Nothing resulted from correspondence between the parties. The buyer ultimately repudiated the contract. He was allowed to recover damages for the breach of the whole of the contract. It was one contract and not a conglomeration of separate contracts.<sup>46</sup>

Where a party abandons a project before its completion, he is, of course, liable to pay the cost and expense of completion. But whether he would be entitled to recover anything for the actual work done depends upon a number of factors. One of them is that if the aggrieved party had an option to reject the work but nevertheless accepted it in its partial state, he would be bound to pay to the other an amount worked out on the basis of *quantum meruit*. Things may be different where there is no such option. In a case of this kind:<sup>47</sup>

43. *Schiller v Sooltan Chand*, ILR (1878) 4 Cal 252, 256.

44. *Juggilal Kamlapat v Pratapmal Rameshwar*, (1978) 1 SCC 69: AIR 1978 SC 389.

45. Once the repudiation has been accepted the contract becomes rescinded. An auction-bidder refused to accept the property because it measured less than what was represented. The Government accordingly cancelled the auction and realised much greater price at re-auction. The first purchaser got no relief. *Bhagat Ram Batra v Union of India*, (1976) 2 SCC 416: AIR 1976 SC 2128.

46. *Andard Mount (London) Ltd v Curewel (India) Ltd*, AIR 1985 Del 45; *Vysya Bank Ltd v A.P. State Agro Industries Devp Corpn Ltd*, AIR 2004 AP 10, no liability to pay interest by bank towards holder for delayed payment of cheques. Delay was due to the instruction of the party who had issued them.

47. *Sumpter v Hedges*, (1898) 1 QB 673 (CA).

A building contractor had done a little more than half the work for which he received part payment. He informed the owner that he had no money and could not go on with the work. The owner finished the building himself using the building materials which the contractor had left on the ground.

The judgment of the court was that the contractor was entitled to get the value of the materials so used but not to any amount for working. He had abandoned the contract. The owner completed and occupied whatever he found on the ground. That could not be regarded as accepting or enjoying the benefit of the work done by the contractor. The claim for *quantum meruit* was not justified.

Where the contract is for work and labour and the completion of the entire work is not a condition precedent, payment would have to be made for the work actually done. In a case of this kind:

The contract was to decorate a flat and to provide it with some furniture. The payment was to be net cash as the work proceeded and the balance on completion. The owner paid something more than half the contract money and moved into his flat and used the furniture. He refused to pay the balance money saying that there was bad workmanship and faulty design. The official referee reported that there had been a sufficient compliance with the contract and that the owner was bound to pay the whole amount less the cost remedying the defects which he worked out to be £56, roughly about 13 per cent of the total value of the contract.

The court did not interfere with the work of the referee. It was not a composite contract like a building or work project. It was more in the nature of a labour contract. The payment had to be measured by the amount of work done.<sup>48</sup>

A contract was awarded for four laning of a road on “build, operate, transfer” basis. The awarding authority terminated the contract on the contractor’s failure to provide financial guarantee as required under the contract within the stipulated time. It was an essential term relating to the eligibility of the contractor. The court said that the action in terminating the contract could not be faulted with.<sup>49</sup>

### Aggrieved party's liability to offer restitution

The aggrieved party may, after putting an end to the contract, bring an action for damages for breach, but he will be bound under Section 64 to

48. *Hoening v Isaacs*, (1952) 2 All ER 176 (CA). This should be contrasted with *Cutter v Powell*, (1775–1802) All ER Rep 159 (KB). The payment was promised for working as second mate for the whole of the voyage. The mate died en route and, therefore, could not complete the voyage. No recovery in terms of part payment on *quantum meruit* basis was allowed. See also *Bolton v Mahadeva*, (1972) 1 WLR 1009 (CA), where a contract for central heating of a house at a cost of £560 was completed in such a way that it required £174 to put it right. This was held to be not a substantial compliance.

49. *Sirmauli Infrastructure (P) Ltd v State of Maharashtra*, (2011) 5 Mah LJ 274.

restore to the other party the benefits he might have received under the contract. This has been so held by the Privy Council in *Muralidhar Chatterjee v International Film Co Ltd.*<sup>50</sup>

The defendants, a firm of film importers, agreed with the plaintiffs to supply them films at the rate of about one in a month. The plaintiffs were to pay them a fixed amount for rent and, of course, some other charges. One film was supplied and a sum of Rs 2000 was paid against it, but on account of exhibition difficulties, the film was returned to the defendants. Subsequently another sum of Rs 2000 was paid against which no film was supplied. The plaintiffs wrote to the defendants that on account of delay and breach of contract, all business dealings would be stopped. The defendants accepted this repudiation and plaintiffs sued them for the refund of their money.

It was held that the amount was refundable under Section 64, subject, of course, to the right of the defendant to claim damages for the breach. The case was referred back to the High Court for the determination of damages. Explaining the relationship between Sections 39 and 64, Sir GEORGE RANKIN said: "The contract which may be 'put an end to' under Section 39 is 'voidable'. The right to recover damages in cases where the contract has been rendered 'voidable' by the wrongful act of a party thereto and has been rescinded by the other party accordingly is a right expressly conferred by the statute. But the right to damages is no objection to the application of Section 64 to cases of rescission of contract under Section 39 and the liability to make restitution attaches to the party putting an end to the contract under Section 39."

Referring to the money paid under the contract his Lordship said: "The money was paid by the plaintiff in part discharge of the consideration or to become due to them from him under the contract. It was a benefit or advantage received under the contract which the defendants were bound to restore, though they may set off against the plaintiff's claim such damage as they had sustained. The fact that the money had been spent by the defendants for the purposes of the contract was wholly immaterial."<sup>51</sup>

A contract for providing CCTV at railway stations was terminated because vulgar and immoral clips were being telecast. The contractor gave no response to the termination. The TV operator admitted that such clips were being telecast. The termination was held to be proper. The authorities forfeited whole of his deposit for assuring proper performance. He contended that he had deposited all his life's earnings and that he would be ruined. The

50. (1943) 56 LW 283; AIR 1943 PC 34 at p. 37.

51. *Ibid* at p. 40. See also *Gurdial Singh v Pearey Lal Malhan*, AIR 1982 Del 120, where the vendor of property cancelled the contract, held, bound to refund benefits obtained. *De-Smet (India) (P) Ltd v B.P. Industrial Corpn (P) Ltd*, AIR 1980 All 253, where the repudiating party was allowed refund of the advance paid by him towards the purchase of a solvent extraction plant. Such an advance is not paid as a guarantee or earnest.

court said that forfeiture of the whole of the deposit was disproportionate to any loss that could have been caused by breach of the contract.<sup>52</sup>

### DAMAGES FOR BREACH [Ss. 73–74]

A contract is not a property. It is only a promise supported by some consideration upon which either the remedy of specific performance or that of damages is available.<sup>53</sup> The party who is injured by the breach of a contract may bring an action for damages.<sup>54</sup> “Damages” means compensation in terms of money for the loss suffered by the injured party. Burden lies on the injured party to prove his loss.<sup>55</sup> Every action for damages raises two problems. The first is the problem of “remoteness of damage” and the second that of “measure of damages”.

#### Remoteness of damage

Every breach of contract upsets many a settled expectation of the injured party. He may feel the consequences for a long time and in a variety of ways. A person contracts to supply to a shopkeeper pure mustard oil, but

52. *Sagar Vision Advertising v East Coast Rly*, AIR 2015 NOC 349 (Ori).

53. *Sunrise Associates v Govt of NCT of Delhi*, (2006) 5 SCC 603: AIR 2006 SC 1908.

54. This is the only remedy which the Contract Act affords. Some other remedies are afforded by the Specific Relief Act, 1963, e.g., an injunction to prevent breach or specific enforcement of the contract, i.e. an action for specific recovery of the thing promised to be sold. *P.R. & Co v Bhagwandas*, ILR (1909) 34 Bom 192; *Finlay Muir & Co v Radhakissen Gopikissen*, ILR (1909) 36 Cal 736. Specific recovery is not allowed when the thing in question is freely available in the market. The injured party should meet his requirement by purchasing elsewhere and then claim damages for the difference in prices. This approach was adopted by the Supreme Court in *State Bank of Saurashtra v P.N.B.*, (2001) 5 SCC 751: AIR 2001 SC 2412, the order for recovery of securities was not upheld. There was the alternative prayer for damages. The purchaser had already paid the price to the bank. The latter was directed to refund the money with a reasonable amount of compensation. *Gunvantilal Ratanchand v Rameshbhai P. Patel*, (2001) 2 GCD 1518 (Guj), the original claim was for specific performance. That being not available, an abrupt shift to claim for damages without any prior pleading and proof of loss was not allowed. *C. Panduranga Rao v Shyamala Rao*, 1999 AIHC 3715 (AP), specific recovery of property not ordered in favour of a person who did not pay nor showed his readiness and willingness to pay. *Data Access India Ltd v MTNL*, (2006) 126 DLT 617, writ remedy is generally not allowed because every breach of contract gives rise to a number of factual questions like meaning of breach, remoteness of damage, etc. This case involved multiparty arrangement involving a number of bank guarantees. *City Municipal Council v S.A. Lateef and Co*, AIR 2004 Kant HCR 3032, the claimant has to show breach on the part of the other party. The plaintiff here complained that sub-standard machinery was supplied to him, but even so he accepted delivery, no expert opinion taken, hence no evidence of any manufacturing defect. *Radheshyam v Lalchand*, (2005) 4 Mah LJ 441, sale of property, the buyer agreed that he would manage permission of competent Authority but nothing was done by him in that respect up to the time that the seller resold to another, the first buyer not allowed to sue for specific performance.

55. *Sudesh Prabhakar Volvoikar v Gopal Babu Savolkar*, (1996) 5 Bom CR 1, booking clerk of theatre misappropriated a sum of money meant for deposit in the film exhibitor's account, employer liable, but the plaintiff had to prove loss. The court said that if the *locus standi* and quantum of damages was not proved, the case could not stand. *ONGC Ltd v Saw Pipes Ltd*, (2003) 5 SCC 705: AIR 2003 SC 2629, breach of contract and loss must be proved. *Chief Secy, State of Gujarat v Kothari Associates*, (2003) 3 Guj LR 2177, principles as to damages stated and applied to building contracts. The court also surveyed authorities.

he sends impure stuff, which is a breach. The oil is seized by an inspector and destroyed. The shopkeeper is arrested, prosecuted and convicted. He suffers the loss of oil, the loss of profits to be gained on selling it, the loss of social prestige and of business reputation, not to speak of the time and money and energy wasted on defence and the mental agony and torture of the prosecution.<sup>56</sup>

Thus, theoretically the consequences of a breach may be endless, but there must be an end to liability. The defendant cannot be held liable for all that follows from his breach. There must be a limit to liability and beyond that limit the damage is said to be too remote and, therefore, irrecoverable.<sup>57</sup> The problem is where to draw the line.

### *The rule in “Hadley v Baxendale”*



CASE PILOT

A very noble attempt was made as early as (1854) in the well-known case of *Hadley v Baxendale*<sup>58</sup> to solve the problem by laying down certain rules.

The plaintiffs carried on an extensive business as miller. Their mill was stopped by a breakage of the crankshaft by which the mill was worked. The defendants, a firm of carriers, were engaged to carry the shaft to the manufacturers as a pattern for a new one. The plaintiffs' servant told the defendants that the mill was stopped, and that the shaft must be sent immediately. But the defendants delayed the delivery by some neglect, and the consequence was, that the plaintiffs did not receive the new shaft for several days after they would otherwise have done. The action was brought for the loss of profits which would have been made during the period of the delay.

ALDERSON B laid down the following rule:

Now we think the proper rule in such a case as the present is this:

Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonably be considered either arising naturally, i.e., according to the usual course of things, from such breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it.

56. See *Ram Kumar Agarwala v Lakshmi Narayan Agarwala*, AIR 1947 Cal 157. In another similar case, *Bostock & Co Ltd v Nicholson & Sons Ltd*, (1904) 1 KB 725, sulphuric acid sold under false warranty, seller not knowing what the buyer wanted it for, not liable for buyer's loss of goodwill and his liability to his customers, but only for defective goods and damage to other goods.

57. See Transworth, *Legal Remedies for Breach of Contract*, 70 Column LR 1145; Priest, *Breach and Remedy for the Tender of Non-confirming Goods under the Uniform Commercial Code: An Economist's Approach* (1978) 91 Harv LR 960. *Remoteness of Damages and Judicial Discretion*, (1978) Camb LJ 288; *Restitution as a Remedy for Breach of Contract: The case of a partially performing seller*, (1982) Yale LJ 16.

58. (1854) 9 Exch 341.

On the basis of this principle the defendants were held not liable for the loss of profits, because in the great multitude of cases of millers sending off broken shafts for repair, it does not follow in the ordinary circumstances that the mill is stopped. Even though it was pointed out that the mill was stopped there could have existed several reasons for the stopping of the mill. The fact that the mill was out of action for want of the shaft was a special circumstance affecting the plaintiff's mill and the same should have been pointed out to the defendants in clear terms. It should also have been communicated that the plaintiffs would have suffered unreasonable loss by way of delay.

This decision has always been taken as laying down two rules.

(i) *General damages*

General damages are those which arise naturally in the usual course of things from the breach itself. Another mode of putting this is that the defendant is liable for all that which naturally happens in the usual course of things after the breach.<sup>59</sup>

(ii) *Special damages*

Special damages are those which arise on account of the unusual circumstances affecting the plaintiff. They are not recoverable unless the special circumstances were brought to the knowledge of the defendant so that the possibility of the special loss was in the contemplation of the parties.

*No recovery of special damages when special circumstances  
not known*

Lack of knowledge of special circumstances once again prevented recovery of special damages in *Horne v Midland Railway Co.*<sup>60</sup>

The plaintiffs, a firm of shoe manufacturers, contracted to supply a quantity of shoes to a firm in London for the use of the French army at an unusually high price. The shoes were to be delivered by the 3rd of February. They consigned the shoes with the defendant railway company telling them that the consignment must reach by the 3rd, but not that there was anything exceptional in the contract. The consignment was delayed and the consignee refused to accept it. The plaintiffs had to sell them in the market at about half their contract price.

In the action against the defendants for the delay in delivering the shoes, they paid into the court a sufficient sum to cover any ordinary loss

59. See George T. Washington, *Damages in Contract and Common Law* (1932) 48 LQR 90; FE Smith, *The Rule in Hadley v Baxendale* (1900) 16 LQR 275; Shriram Pistons and Rings Ltd v Buckeye Machines (P) Ltd, AIR 2007 NOC 1844 (Del), damages can be claimed for breach of contract if not completed even within the extended period. Extension of time is not a waiver of all rights.

60. (1873) LR 8 CP 131.

occasioned thereby, but the plaintiffs further claimed the difference between the price at which they had contracted to sell the shoes and the price which they ultimately fetched. But it was held that this was a damage of an exceptional nature and it could not be supposed to have been in the contemplation of the railway company when it contracted to convey the goods by the 3rd.

For the same reason loss of profits was not allowed to be recovered in *British Columbia Saw Mill Co v Nettleship*.<sup>61</sup>

The parts of a saw mill machinery, packed in cases, were given to the defendant, a carrier, for carriage to Vancouver. One of the cases was lost and consequently a complete mill could not be erected and operated. The plaintiff claimed the cost of lost machinery and the profits which could have been earned if the mill had been installed in time.

The court allowed only the cost in Vancouver of the articles lost. The loss of profits to be made from the intended use of the mill was held to be too remote. WILLES J gave the following illustration in support of this conclusion:

Take the case of a barrister on his way to practice at the Calcutta Bar, where he may have a large number of briefs awaiting him; through the default of the Peninsular and Oriental Company he is detained in Egypt or in the Suez boat, and consequently sustains great loss; is the company to be responsible for that, because they happened to know the purpose for which the traveller was going?<sup>62</sup>

WILLES J further pointed out that special damages are recoverable only when the special purpose of the contract "is brought home to the party sought to be charged, under such circumstances that he must know that the person he contracts with reasonably believes that he accepts the contract with the special condition attached to it."<sup>63</sup>

#### *Special circumstances already within knowledge of contract breaker*

But in the subsequent case of *Simpson v London & North Western Railway Co*<sup>64</sup> the above suggestion was qualified to this extent that if the special circumstances are already within the knowledge of the party breaking the contract, the formality of communicating them to him may not be necessary.

61. (1868) LR 3 CP 499: 18 LT 604.

62. Corresponding to Illustration (r). This is not applicable when the contract is for sale of goods, *Kandappa Mudaliar v Muthuswami Ayyar*, ILR (1927) 50 Mad 94: AIR 1927 Mad 99.

63. Similarly, in *Dominion of India v All India Reporter Ltd*, AIR 1952 Nag 32, loss by railways of three volumes of a set of books without which the set became useless, recovery allowed only for the lost volumes, the goods were described only as a bundle of books without any indication of the importance of a volume. Compare this with *Hydraulic Engg Co v McHaffie Goslett & Co*, (1878) LR 4 QBD 670, the defendant failed to supply an essential part of a machine about which he knew that his buyer was under a contract to supply to a third party, he was held liable for the plaintiff's loss of profit.

64. (1876) LR 1 QBD 274.

The plaintiff was in the habit of exhibiting samples of his implements at cattle shows. He delivered his samples to the defendant company for consignment to the show grounds at New Castle. The consignment note said: "must be at New Castle on Monday certain". But no mention was made of the intention to place the goods in the exhibition. On account of negligence the goods reached only after the show was over.

But as the company was already aware of the object of carrying the goods there, the plaintiff was allowed to recover not only the loss of freight but also the profits he would have made by placing the goods at the show. COCKBURN CJ said:

The principle is now well-settled that, whenever either the object of the sender is specially brought to the notice of the carrier, or the circumstances are known to the carrier, from which the object ought in reason to be inferred, so that the object may be taken to have been in the contemplation of both parties, damages may be recovered for the natural consequences of the failure of that object.

In another case<sup>65</sup> a fragmentiser was purchased by the plaintiff under a hire-purchase agreement. Its rotor broke down before normal life. The plaintiff had no means to replace it at cash price. He had to arrange it again at a hire-purchase price and claimed the same as damages. The defendant contended that the plaintiff had to pay hire-purchase price because of his lack of means. This contention was rejected. The fact that in the present circumstances of economy business has to depend upon hire-purchase system, was held to be within the contemplation of parties.

### *Relationship between two rules re-examined*

The relationship between the rules was re-examined in *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd*<sup>66</sup> Lord ASQUITH worked out a number of propositions from a consideration of the leading authorities. The substance of the propositions is as follows: Only such loss is recoverable as was at the time of the contract reasonably foreseeable as liable to result from the breach. Foreseeability depends upon knowledge. Accordingly what was at that time reasonably foreseeable depends upon the knowledge then possessed by the parties or, at all events, by the party who later commits the breach. For this purpose, knowledge "possessed" is of two kinds: one imputed, and the other actual. Every one as a reasonable person, is taken to know the "ordinary course of things" and consequently to know what loss is liable to result from a breach of the contract in that ordinary course. This is the subject-matter of the "first rule" in *Hadley v Baxendale*. But to this knowledge which the defendant is assumed to possess must be added



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65. *B.P. Exploration Co (Libya) Ltd v Hunt (No. 2)*, (1981) 1 WLR 232 (CA). Where the lessor knew the purpose for which the lessee required the premises, he was held liable for the loss of that purpose during the delayed period. *Jacques v Miller*, (1877) LR 6 Ch D 153.

66. (1949) 2 KB 528 (CA).

his actual knowledge of the special circumstances of the case showing the possibility of more loss arising from the breach. Such a case attracts the operation of the “second rule” so as to make the additional loss recoverable.

The judgment emphasises that both the rules are based upon the principle of “foreseeability”. This gives a “new look for *Hadley v Baxendale*”. Now it has been clearly so stated by DIPLOCK LJ in *C. Czarnikow Ltd v Koufos*.<sup>67</sup>

That there are not two rules formulated in *Hadley v Baxendale* but only two different instances of the application of a single rule.

Similarly, SALMON LJ observed:<sup>68</sup>

Any damage actually caused by a breach of any kind of contract is recoverable provided that when the contract was made such damage was reasonably foreseeable as liable to result from the breach.

The facts of *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd*<sup>69</sup> were as follows:

A firm of launderers and dyers wanted to expand their business and, therefore, ordered with the defendants for the supply of a boiler of much greater capacity. The defendants agreed to deliver on June 5, 1946, but delayed delivery until November 8. The plaintiffs claimed as damages the loss of profits which would have been earned if their business was expanded in time as there were at the time unique business opportunities.

The court allowed £110 as general damages but disallowed loss of profits. On appeal the case was referred to an official referee to determine what damages, in addition to £110, should be allowed on the basis of the knowledge then possessed by the parties. ASQUITH J said “that no supplier who has promised delivery of a boiler of an unusually large size by a particular date, with knowledge that it was to be put into use immediately on delivery can reasonably contend that he could not foresee that loss of business would be likely to result from the delay”.

To the same effect is the decision of the House of Lords in *Monarch SS Co Ltd v Karlshamns Oljefabriker (A/B)*.<sup>70</sup>

A British vessel was chartered in April 1939, by a British company for carrying cargo of soyabeans from Manchuria to a port in Sweden. But owing to delay caused by the vessel’s unseaworthiness, she did not reach that port before the outbreak of war between Great Britain and Germany. Consequently, the ship was prohibited from going to its destination and ordered to discharge at Glasgow. The plaintiff, who needed soyabeans for their business as they were not locally available, incurred expenses in forwarding them in neutral ships.

67. (1966) 2 QB 695: (1966) 2 WLR 1397, 1497; on appeal, *Heron II, The Koufos v C. Czarnikow Ltd*, (1969) 1 AC 350: (1967) 3 WLR 1491 (HL).

68. *Ibid* at p. 1422.

69. (1949) 2 KB 528 (CA).

70. 1949 AC 196 (HL).

It was held that the loss was due to unseaworthiness of the ship and the defendants were liable for it, because, in view of the international situation, they should have foreseen that war might break out and cause loss or diversion of the vessel.

#### *House of Lords restore original vitality of two rules*

The interpretation put upon the *Hadley v Baxendale* principles by the Court of Appeal in the *Victoria Laundry* case had virtually replaced the expression “contemplation of the parties” with “reasonable man’s foresight” and this being the principle in the law of tort also, hardly any distinction remained between tort and contract principles relating to remoteness of damages. But the House of Lords in their decision in the *Heron II, The Koufos v C. Czarnikow Ltd*<sup>71</sup> have restored the distinction by again laying emphasis upon the “contemplation of the parties”.

A vessel was chartered to proceed to Constanza, there to load a cargo of three thousand tons of sugar; and to carry it to Basrah, or, at the charterers’ option, to Jeddah. The vessel left in time. A reasonably accurate prediction of the length of the voyage was twenty days. But the vessel in breach of contract made deviation which caused a delay of nine days. If the vessel had arrived in time, the charterer would have obtained roughly £1 more per ton than what he actually obtained. The shipowner knew that there was a market for sugar at Basrah, but did not know that the charterer wanted to sell the sugar promptly on arrival. The shipowner also knew that sugar prices were apt to fluctuate from day to day, but had no reason to suppose that fluctuation would be downwards rather than upwards. He was sued for the loss due to fall in market price. The umpire allowed this loss. But the trial judge allowed as damages only the interest on the value of the cargo during the period of delay. The Court of Appeal reversed this order and restored the award of the umpire and the House of Lords unanimously affirmed the decision of the Court of Appeal.

Lord REID emphasised that the rule (or rules) laid down in *Hadley v Baxendale* and which for over a century have been used for determining remoteness of damage should not be subjected to an interpretation which would result in a contrary decision of that case. His Lordship laid particular emphasis upon the fact that in that case the loss of profit was caused by the delay, but even so the defendant was held not liable not because the loss was not foreseeable but because as ALDERSON B put it “it is obvious that, in the great multitude of cases of millers sending off broken shafts to third persons by a carrier under ordinary circumstances, such consequences would not, in all probability, have occurred...”. ALDERSON B clearly did not and could not mean that it was not reasonably foreseeable that delay might stop the resumption of work in the mill. He merely said that in the

71. (1969) 1 AC 350: (1967) 3 WLR 1491 (HL).

great multitude—which can be taken to mean the great majority—of cases it would not happen. He was not distinguishing between results which were foreseeable or unforeseeable, but between results which were merely likely because they would happen in the great majority of cases, and results which were unlikely because they would only happen in a small minority of cases. He clearly meant that a result which will happen in the great majority of cases should fairly and reasonably be regarded as having been in the contemplation of the parties, but that a result which, though foreseeable as a substantial possibility would happen only in a small minority of cases should not be regarded as having been in their contemplation.

Applying this test to the facts his Lordship concluded that having regard to the knowledge available to the shipowner when he made the contract, any reasonable person in his position would have realised that such loss was sufficiently likely to result from the breach of contract thus making it proper to hold that the loss followed naturally from the breach or that the loss of that kind would have been within his contemplation.

Lord HODSON also presented the same view of *Hadley v Baxendale*.

I find guidance in the use of the expression in the great multitude of cases which is to be found in more than one place in the judgment in *Hadley v Baxendale*. It indicates that the damages recoverable for breach of contract are such as flow naturally in most cases from the breach, whether under ordinary circumstances or from special circumstances due to the knowledge either in the possession of or communicated to the defendants. This expression throws light on the whole field of damages for breach of contract, and points to a different approach from that taken in tort cases. The approach in tort will normally be different simply because the relationship of the parties is different. The claim against the tortfeaser who has inflicted tortious damage is not the same as the claim against an opposite party for breach of contract, for the latter claim depends on the contemplation of the parties to the contract and question of remoteness as such does not arise. Consequently, liability in tort may often be of a wider kind.

#### *Physical injury resulting from breach*

The wisdom of the distinction between tort and contract principles, at any rate in reference to physical injury caused by the breach, has again been questioned by Lord DENNING in *Parsons (H) (Livestock) Ltd v Uttley Ingham & Co Ltd*.<sup>72</sup>

72. 1978 QB 791: (1977) 3 WLR 990 (CA); *H. Parsons (Livestock) Ltd v Uttley Ingham & Co*, 1978 QB 791: (1977) 3 WLR 990, noted *Persons (H) (Livestock) Ltd v Uttley Ingham & Co Ltd*, 1978 QB 791: (1978) 94 LQR 171. An earlier authority to the same effect, *Smith v Green*, (1875) LR 1 CPD 92, cow sold warranted as free from diseases, but it was diseased, the buyer's other animals infected, seller liable for the loss of livestock and not only for the animal sold.

The plaintiffs were pig farmers and they purchased from the defendants a large hopper for storage of pig nuts. They had already purchased one from them earlier and it was serving them well. The hopper was ventilated at the top, but the ventilator had to be kept closed and was to be opened after the hopper was installed at the plaintiff's farm. The defendants negligently forgot to open it and the plaintiffs could not know, it being too high. The nuts stored in the hopper became mouldy and without any knowledge of the danger, they were served to the pigs. They suffered from a rare type of intestinal infection and 254 of them perished.

The defendants were held liable for the loss of the pigs but not for loss of profits from future sales of pigs. The loss of pigs was a physical injury and the court, feeling that for such injuries the principle should be the same as in tort, the defendants were liable for all damage which could reasonably have been foreseen at the date of the breach as a possible consequence of the breach. The loss of profits was an economic loss and the defendants were not liable for it because it could not have been within the party's contemplation at the time of the contract. Thus, the opinion of the Court of Appeal is that *Hadley v Baxendale* should be confined to economic loss and for physical injuries the principle of foreseeability which operates in tort should apply.<sup>73</sup>

#### *Damages for negligent survey report*

The applicable principles have been stated by the Court of Appeal in *Watts v Morrow*.<sup>74</sup> The plaintiffs purchased a country home for £177,500 in reliance on a survey prepared by the defendant surveyor in which he stated that overall dwelling house was sound, stable and in good condition although there were minor defects which could be dealt with as part of ordinary ongoing maintenance and repair. After taking possession the plaintiffs discovered substantial defects not mentioned in the defendant's report which required urgent repair, including the renewal of the roof, windows and floor boards. The plaintiffs carried out repairs to remedy the defects at a cost of £33,961 and sought to recover this amount. The surveyor admitted liability but pleaded that it should not be more than £15,000, being the difference between the price paid and the price that the home was worth if the defects were taken into account. The court held that the proper measure of damages was the diminution in value rather than the cost of repairs. Applying the principle of restitution to the terms of the contract, the amount required to put the plaintiff in the position in which he would have been if the surveyor had carried out the contract of survey properly was the amount by which he was caused to pay more than the value of the house in its true condition.

73. Distinction between tort and contract is breaking down at many points. See Fridman, (1977) LQR 482.

74. (1991) 1 WLR 1421 (CA).



## Section 73 of the Contract Act

The same principles are applicable in India. The Privy Council, for example, observed in *A.K.A.S. Jamal v Moolla Dawood Sons & Co*<sup>75</sup> that Section 73 is declaratory of the common law as to damages. Similarly, PATANJALI SASTRI J (afterwards CJ) of the Supreme Court observed in *Pannalal Jankidas v Mohanlal*<sup>76</sup> "that the party in breach must make compensation in respect of the direct consequences flowing from the breach and not in respect of loss or damage indirectly or remotely caused".<sup>77</sup> The section provides:

**S. 73. Compensation for loss or damage caused by breach of contract.**—When a contract has been broken, the party who suffers by such breach is entitled to receive, from the party who has broken the contract, compensation for any loss or damage caused to him thereby, which naturally arose in the usual course of things from such breach, or which the parties knew, when they made the contract, to be likely to result from the breach of it.

Such compensation is not to be given for any remote and indirect loss or damage sustained by reason of the breach.

**Compensation for failure to discharge obligation resembling those created by contract.**—When an obligation resembling those created by contract has been incurred and has not been discharged, any person injured by the failure to discharge it is entitled to receive the same compensation from the party in default, as if such person had contracted to discharge it and had broken his contract.

*Explanation.*—In estimating the loss or damage arising from a breach of contract, the means which existed of remedying the inconvenience caused by the non-performance of the contract must be taken into account.

### Illustrations

**[Market price criterion].**—(a) A contracts to sell and deliver 50 maunds of saltpetre to B, at a certain price to be paid on delivery. A breaks his promise. B is entitled to receive from A, by way of compensation, the sum, if any, by which the contract price falls short of the price for which B might have obtained 50 maunds of saltpetre of like quality at the time when the saltpetre ought to have been delivered.

**[Extra cost of hiring alternative ship].**—(b) A hires B's ship to go to Bombay, and there takes on board, on the first of January, a cargo, which, A is to provide and to bring it to Calcutta, the freight to be paid when earned. B's ship does not go to Bombay, but A has opportunities of procuring suitable conveyance for the cargo upon terms as advantageous as those on which

75. (1915–16) 43 IA 6: ILR (1916) 43 Cal 493: (1916) 1 AC 175.

76. AIR 1951 SC 144, 153: 1950 SCR 979: (1951) 21 Comp Cas 1.

77. Similarly, KANIA CJ of the Supreme Court observed in *Pannalal Jankidas v Mohanlal*, AIR 1951 SC 144: 1950 SCR 979: (1951) 21 Comp Cas 1 that the rule stated by ALDERSON B has consistently been accepted as correct; the only difficulty has been in applying it. The Supreme Court held in *Aslibing v L.S. John*, (1984) 1 SCC 205: AIR 1984 SC 988 that repudiation by one party puts an end to the contract although the right to sue for damages survives. Accordingly, the disqualification by virtue of a Government contract of holding an office of profit under the State would end as soon as the contractor gives up the contract.

he had chartered the ship. A avails himself of those opportunities, but is put to trouble and expense in doing so. A is entitled to receive compensation from B in respect of such trouble and expense.

*[Seller's loss on resale].*—(c) A contracts to buy of B, at a stated price, 50 maunds of rice, no time being fixed for delivery. A afterwards informs B that he will not accept the rice if tendered to him. B is entitled to receive from A, by way of compensation, the amount, if any, by which the contract price exceeds that which B can obtain for the rice at the time when A informs B that he will not accept it.

*[Ship seller's loss on resale of ship].*—(d) A contracts to buy B's ship for 60,000 rupees, but breaks his promise. A must pay to B, by way of compensation, the excess, if any, of the contract price over the price which B can obtain for the ship at the time of the breach of promise.

*[Loss of value caused by delay in transit].*—(e) A, the owner of a boat, contracts with B to take a cargo of jute to Mirzapur, for sale at that place, starting on a specified day. The boat, owing to some avoidable cause, does not start at the time appointed, whereby the arrival of the cargo at Mirzapur is delayed beyond the time when it would have arrived if the boat had sailed according to the contract. After that date, and before the arrival of the cargo, the price of jute falls. The measure of the compensation payable to B by A is the difference between the price which B could have obtained for the cargo at Mirzapur at the time when it would have arrived if forwarded in due course, and its market price at the time when it actually arrived.

*[Deficient house repairing service].*—(f) A contracts to repair B's house in a certain manner, and receive payment in advance. A repairs the house, but not according to contract. B is entitled to recover from A the cost of making the repairs that conform to the contract.

*[Difference in hiring charges of ship].*—(g) A contracts to let his ship to B for a year, from the first of January, for a certain price. Freights rise, and on the first of January, the hire obtainable for the ship is higher than the contract price. A breaks his promise. He must pay to B, by way of compensation, a sum equal to the difference between the contract price and the price for which B could hire a similar ship for a year on and from the first of January.

*[Buyer's breach, difference between market and contract prices].*—(h) A contracts to supply B with a certain quantity of iron at a fixed price, being a higher price than that for which A could procure and deliver the iron. B wrongfully refuses to receive the iron. B must pay to A, by way of compensation, the difference between the contract price of the iron and the sum for which A could have obtained and delivered it.

*[Delay caused by carrier, Hadley v Baxendale module].*—(i) A delivers to B, a common carrier, a machine, to be conveyed without delay, to A's mill, informing B that his mill is stopped for want of the machine. B unreasonably delays the delivery of the machine, and A in consequence, loses a profitable contract with the Government. A is entitled to receive from B, by way of compensation, the average amount of profit which would have been made by the working of the mill during the time that delivery of it was delayed, but not the loss sustained through the loss of the Government contract.

*[Knowledge of resale, loss of profit].*—(j) A, having contracted with B to supply B with 1000 tons of iron at 100 rupees a ton, to be delivered at a stated time, contracts with C for the purchase of 1000 tons of iron at 80 rupees a ton, telling C that he does so for the purpose of performing his contract with B. C fails to perform his contract with A, who cannot procure other iron, and B, in consequence, rescinds the contract. C must pay to A 20,000 rupees, being the profit which A would have made by the performance of his contract with B.

*[Where no knowledge of resale agreement, no more than market difference recoverable].*—(k) A contracts with B to make and deliver to B, by a fixed day, for a specified price a certain piece of machinery. A does not deliver the piece of machinery at the time specified, and, in consequence of this, B is obliged to procure another at a higher price than that which he was to have paid to A, and is prevented from performing a contract which B had made with a third person at the time of his contract with A (but which had not been then commu-

nicated to *A*), and is compelled to make compensation for breach of that contract. *A* must pay to *B*, by way of compensation, the difference between the contract price of the piece of machinery and the sum paid by *B* for another, but not the sum paid by *B* to the third person by way of compensation.

[*Building contract*].—(l) *A*, a builder, contracts to erect and finish a house by the first of January, in order that *B* may give possession of it at that time to *C*, to whom *B* has contracted to let it. *A* is informed of the contract between *B* and *C*. *A* builds the house so badly that, before the first of January, it falls down and has to be rebuilt by *B*, who, in consequence, loses the rent which he was to have received from *C*, and is obliged to make compensation to *C* for the breach of his contract. *A* must make compensation to *B* for the cost of rebuilding the house, for the rent lost, and for the compensation made to *C*.<sup>78</sup>

[*Breach of warranty as to quality of goods*].—(m) *A* sells certain merchandise to *B*, warranting it to be of a particular quality, and *B*, in reliance upon this warranty, sells it to *C* with a similar warranty. The goods prove to be not according to the warranty, and *B* becomes liable to pay *C* a sum of money by way of compensation. *B* is entitled to be reimbursed this sum by *A*.

[*Default in payment of money*].—(n) *A* contracts to pay a sum of money to *B* on a day specified. *A* does not pay the money on that day; *B*, in consequence of not receiving the money on that day, is unable to pay his debts, and is totally ruined. *A* is not liable to make good to *B* anything except the principal sum he contracted to pay, together with interest up to the day of payment.<sup>79</sup>

[*Market price and not loss of profit*].—(o) *A* contracts to deliver 50 maunds of saltpetre to *B* on the first of January, at a certain price. *B* afterwards, before the first of January, contracts to sell the saltpetre to *C* at a price higher than the market price of the first of January. *A* breaks his promise. In estimating the compensation payable by *A* to *B*, the market price of the 1 January, and not the profit which would have arisen to *B* from the sale to *C*, is to be taken into account.

[*Defaulting seller not liable for closure of mill*].—(p) *A* contracts to sell and deliver 500 bales of cotton to *B* on a fixed day. *A* knows nothing of *B*'s mode of conducting his business. *A* breaks his promise, and *B*, having no cotton, is obliged to close his mill. *A* is not responsible to *B* for the loss caused to *B* by the closing of the mill.

[*Defaulting seller not liable for loss of season*].—(q) *A* contracts to sell and deliver to *B*, on the first of January, certain cloth which *B* intends to manufacture into caps of a particular kind, for which there is no demand, except at that season. The cloth is not delivered till after the appointed time, and too late to be used that year in making caps, *B* is entitled to receive from *A*, by way of compensation, the difference between the contract price of the cloth and its market price at the time of delivery, but not the profits which he expected to obtain by making caps, nor the expenses which he has been put to in making preparation for the manufacture.

[*Carrier of passengers causing delay*].—(r) *A*, a ship-owner, contracts with *B* to convey him from Calcutta to Sydney in *A*'s ship, sailing on the first of January, and *B* pays to *A*, by way of deposit, one-half of his passage-money. The ship does not sail on the first of January, and *B*, after being in consequence, detained in Calcutta for some time, and thereby put to some expense, proceeds to Sydney in another vessel, and, in consequence, arriving too late in Sydney, loses a sum of money. *A* is liable to repay to *B* his deposit, with interest, and the expense

78. *First Consolidated v Padu Ehsan*, (1994) 1 Curr LJ 375 (Malaysia), in computing loss of profits in their claim for damages the plaintiff submitted the costing done by a witness who was not a qualified surveyor, nevertheless holding experience in this work. The defendant did not offer evidence of what would be the fair costing. In the circumstances, the submission of the plaintiff was accepted.

79. *Jay Container Services Shipping (P) Ltd v S.D.S. Shipping (P) Ltd*, (2003) 3 Bom CR 163, future rent not allowed to be recovered either as damages or as money due.

to which he is put by his detention in Calcutta, and the excess, if any, of the passage-money paid for the second ship over that agreed upon for the first, but not the sum of money which *B* lost by arriving in Sydney too late.

### Section 73 incorporates two rules of “Hadley v Baxendale”

The section declares that compensation is not to be given for any remote or indirect loss or damage sustained by reason of the breach.<sup>80</sup> The section also provides that the same principles will apply where there has been a breach of a quasi-contractual obligation.<sup>81</sup>

The section thus clearly lays down two rules. Compensation is recoverable for any loss or damage—

- (i) arising naturally in the usual course of things from the breach; or
- (ii) which the parties knew at the time of the contract as likely to result from the breach.

The first rule is “objective” as it makes the liability to depend upon a reasonable man’s foresight of the loss that will naturally result from the breach of the contract. The second rule is “subjective” as, according to it, the extent of liability depends upon the knowledge of the parties at the time of the contract about the probable result of the breach.<sup>82</sup>

80. *State of Rajasthan v Nathu Lal*, AIR 2006 Raj 19, recovery of amount for breach of contract without taking decision on the fact of breach not proper. *U.P. State Sugar Corpn v Mahalchand M. Kothari*, (2005) 1 SCC 348: AIR 2005 SC 61, receiver of sugar mill appointed for recovering dues of cane growers as arrears of land revenue, he contracted to supply sugar but failed to do so. The other party could not sue him. Suit could lie against the corporation into which the sick sugar mill was merged.

81. The right of action depends upon proof of breach. In *State of Karnataka v Shree Rameshwara Rice Mills*, (1987) 2 SCC 160: AIR 1987 SC 1359, the contract provided that damages would be assessed by the Government and it was held that the Government was not the proper party to determine whether a breach had taken place or not. To the same effect, *Vairappa Thevar v Tehsildar*, (1989) 1 MLJ 387; *P.C. Rajput v State of M.P.*, AIR 1993 MP 107: (1994) 1 MPLJ 387, road building contract, Government causing some delay but extending time, the contractor thereafter neglected the work, held, no breach on the part of the Government, writ remedy not allowed to enforce a contract between the State and citizen. *Amar Singh v UT of Chandigarh*, AIR 1993 P&H 100. But initial deposit amount was ordered to be refunded under writ jurisdiction when the Government stopped working and the dispute was not about damages for breach of contract. *Krishna & Co v Govt of A.P.*, AIR 1993 AP 1. The plaintiff has also to prove his loss. Where loss is not provable, reasonable compensation is awarded on the basis of the material before the court, *English Electric Co of India Ltd v Cement Corpn of India Ltd*, 1996 AIHC 1875 (Del).

82. See Murray Pickering, *The Remoteness of Damages in Contract*, (1968) 31 Mod LR 203, where the learned writer considers the decision of the House of Lords in the *Heron II*, *The Koufos v C. Czarnikow Ltd*, (1969) 1 AC 350: (1967) 3 WLR 1491 (HL) and traces the “objective” and “subjective” nature of the rules in *Hadley v Baxendale*, (1854) 9 Exch 341. For examples of breach see *M.P. Mines Ltd v Rai Bahadur Shriram Durga Prasad (P) Ltd*, (1972) 3 SCC 180: AIR 1971 SC 1983; *State of Kerala v Cochin Chemical Refineries Ltd*, AIR 1968 SC 1361: (1968) 3 SCR 556; *Ganpati Salt Works v State of Gujarat*, AIR 1995 Guj 61, no compensation on ground of equity where the claimant had duped the party to the lease and had grabbed the Government lease for himself. *Food Corporation of India v Babulal Agrawal*, (2004) 2 SCC 712, agreement to provide premises on lease for three years after construction, refused to do so, held breach actionable in damages. *Ex-Servicemen Security*

The burden of proof lies on the plaintiff to show that damage has been sustained and what shall be the measure of converting the loss into money. A claim for damages becomes liable to be rejected where this burden is not discharged.<sup>83</sup>

### Liability in ordinary cases

The extent of liability in ordinary cases is what may be foreseen by "the hypothetical reasonable man", as arising naturally in the usual course of things. One illustration is the decision of the Madras High Court in *Madras Railway Co v Govinda Rau*.<sup>84</sup>

The plaintiff, who was a tailor, delivered a sewing machine and some cloth to the defendant railway company to be sent to a place where he expected to carry on his business with special profit by reason of a forthcoming festival. Through the fault of the company's servants the goods were delayed in transmission and were not delivered until some days after the conclusion of the festival. The plaintiff had given no notice to the company of his special purpose.

He claimed as damages the expenses of travelling up to the place of festival and of staying there and the loss of profits which he would have earned. The court held that the damages claimed were too remote. All of these were due to the frustration of the special purpose and that was not known to the company. *Fazal Ilahi v East Indian Rly Co*<sup>85</sup> is another illustration of the same kind.

The plaintiff delivered to the defendant railway company's parcel office at Cawnpore four boxes of Chinese crackers for consignment to Allahabad where he needed them for a festival on 5th June, but he did not disclose the purpose. The company's servants considering it unsafe to send crackers by parcel train, actually sent them by goods train and they reached only after the conclusion of the festival. The company required him to take delivery on payment of additional freight, which he refused to pay and, therefore, the company sold the goods at a nominal price.

He sued the railway company. The court disallowed the claim for profits which would have been made, as the plaintiff's special purpose was not

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*Bureau v T.N. Electricity Board*, AIR 2003 NOC 13 (Mad), security personnel were provided by the plaintiffs (Bureau) to the defendants (SEB). One of the terms was that the plaintiffs would be liable for any loss due to the involvement of the personnel. Theft took place. No allegations of involvement of personnel. No FIR against them. The plaintiffs were entitled to their security charges.

83. *Draupadi Devi v Union of India*, (2004) 11 SCC 425.

84. ILR (1898) 21 Mad 172. Damages cannot be recovered by a person who does not do his duty under the contract, e.g. a person whose electricity supply is suspended for non-payment of bills. *Patel Dadubhai Narsibhai v Gujarat EB*, (1990) 1 Guj LR 673. But damages were allowed where there was a long delay in restoring supply after all requirements were fulfilled. *Gujarat Electricity Board v K.R. Patel*, (1988) 2 GLH 169.

85. ILR (1921) 43 All 623.

within the knowledge of the company.<sup>86</sup> But the plaintiff succeeded in recovering the cost price of his goods sold by the company in breach of the contract and Rs 100 as damages and other incidental expenses.

Even where the goods are altogether lost in transit, the carrier is not liable for the loss of profits which would have been made by selling the goods at their destination.<sup>87</sup>

### *Proof of loss is necessary*

In a claim for general damages the plaintiff has to assert that he has suffered some loss but for the purpose of claiming special damages he has specifically to plead and prove that he has sustained such special loss.<sup>88</sup> In a claim of compensation for damage to consignment, no details as to loss were mentioned in the plaint. It is necessary that some loss should be shown by evidence. The mere fact that the carrier admitted damage was held to be not sufficient to entitle the consignee to obtain a decree for compensation without proof of actual loss.<sup>89</sup>

### **Building contracts**

Since works and building contracts are undertaken only with a view to earning profits, the party committing the breach would be liable for the contractor's loss in terms of expected profits. The Supreme Court came to this conclusion in *A.T. Brij Paul Singh v State of Gujarat*.<sup>90</sup>

A Government building contract was allotted through tenders. It fell to the share of a Poona-based contractor who transported his mobile workshop from there to work site at Rajkot in Gujarat. He had done only a part of the work when the Government unjustifiably repudiated the contract. The contractor sued for loss of profits.

It was not disputed before the Supreme Court that where in a works contract the party entrusting the work commits breach, the contractor would be entitled to claim damages for loss of profit which he expected from the project. The court noted an observation in Hudson's BUILDING AND ENGINEERING CONTRACTS<sup>91</sup> that in major contracts subject to competitive

86. *Union of India v Hari Mohan Ghosh*, AIR 1990 Gau 14: (1990) 1 Gau LR (NOC) 31, railway administration held not liable for trader's expected profits for the loss of his consignment when the administration was not aware of the object of his dispatch.

87. *Ibid.* A consignee to whom a consignment had been delayed was not allowed to recover damages caused by the closure of his factory. *Union of India v Panipat Woollen Mills Co Ltd*, AIR 1967 Punj 497. *Shaw Wallace & Co Ltd v Union of India*, (2004) 5 CTC 308, a part of the goods were delivered in a damaged condition. Port Trust admitted the damaged condition, damage being in the course of consignment, the consignee was entitled to claim damages. *Union of India v Hari Shanker Gauri Shanker*, 2005 All LJ 2200, the cargo was damaged due to percolation of rain water into the wagon. It showed that the wagon was defective. Railway could not be absolved of its liability.

88. *Chief Secy, State of Gujarat v Kothari & Associates*, (2003) 1 GCD 372 (Guj).

89. *Shipping Corpn of India Ltd v Bharat Earth Movers Ltd*, (2010) 2 MWN (Civ) 1.

90. (1984) 4 SCC 59: AIR 1984 SC 1703.

91. (10th Edn, 1970).

tender on a national basis, the evidence given in litigation on many occasions suggests that the head office overheads and profit is between 3 to 7 per cent of the total price of cost which is added to the tender. The court accordingly allowed Rs 2 lakhs as compensation under the head "loss of profits" over and above other claims.<sup>92</sup>

In a contract for the construction of a swimming-pool, the depth of the pool happened to be only 6 feet 9 inches whereas the building contract required it to be 7 feet 6 inches and at the diving point it was not more than six feet. This resulted in a claim for damages for defective construction. The Trial Judge found that the pool was perfectly safe for diving and that the shortfall in depth made no difference to the value of the pool. He also found that it would cost about £21,000 to cure the defect by digging the pool deeper. It was quite likely that even after receiving the above amount, the owner might not spend on repair. He held that the appropriate measure of damages was the difference in value between the pool as it was and the pool as it should have been if the contract was properly performed and allowed £2500. The Court of Appeal reversed this and allowed the full cost of cure. But the House of Lords restored the decision of the trial judge.<sup>93</sup>

Some earlier cases on the subject were also decided either on the basis of cost of cure or difference in value depending on whether in the circumstances of the case, cure would be reasonable or whether recovery on the basis of difference in value would be reasonable. The latter would be more reasonable where the building, though defective, is nevertheless substantially useful. The costs of rectification even if recovered, may not be so used.<sup>94</sup>

An approach of this kind was also to be seen in a New York decision where two principles were stated: "first, the cost of reinstatement is not the appropriate measure of damages if the expenditure would be out of all proportion to the goods to be obtained, and, secondly, the appropriate measure

92. See further *State of Kerala v K. Bhaskaran*, AIR 1985 Ker 49. In a works contract the Government undertook the responsibility of supplying cement but failed to do so. The contractor was allowed to recover 10 per cent estimated profits as the Government did not controvert it. In *Basildon Distt Council v J.E. Lesser (Properties) Ltd*, 1985 QB 839: (1984) 3 WLR 812, in a building contract under which it was the responsibility of the contractor to design and construct dwellings, he was not allowed the defence of contributory negligence against his liability for defective design and execution. *Pishori Lal Maggo v DDA*, 1997 AIHC 1579 (Del), the arbitrator allowed recovery to the extent of 10 per cent profit on the estimated costs, the court affirmed the award. *Metro Electric Co v DDA*, AIR 1980 Del 266, clause providing for 10 per cent extra costs, upheld. *Govt of A.P. v V. Satyam Rao*, AIR 1996 AP 288, contractor prevented from completing contract because of breach on the part of the Government, award of damages on the basis of loss of profits which the contractor could have derived from the rest of the work. *C.T. Xavier v P.V. Joseph*, AIR 1995 Ker 140, 10 per cent of the total value of the contract allowed to the contractor by way of damages for breach of contract.

93. *Ruxley Electronics and Construction Ltd v Forsyth*, 1996 AC 344: (1995) 3 WLR 118.

94. See *East Ham Borough Council v Bernard Sunley & Sons Ltd*, 1966 AC 406 (HL) and *Jacob & Youngs Inc v George E. Kent*, (1921) 230 NY 239, New York Court of Appeal.

of damages is the difference in value, even though it would result in a nominal award.”<sup>95</sup>

### *Delay suffered by builder*

The builder was required to complete the work within 18 months but by reason of delays caused by the Department, it took 27 months to be completed. The builder suffered itemised damages which he proved by leading oral evidence. The amount claimed being reasonable was decreed.<sup>96</sup>

### **Scheme for allotment of plots**

Damages for mental pain and anguish cannot be awarded in a case in which there is a breach on the part of a development authority in delaying the completion of the scheme. It is not a head of damages in ordinary commercial contracts. The court, however, allowed interest at the rate of 12 per cent on the refundable amount though there was no provision in the contract to that effect. It was justifiable on equitable grounds. The brochure of the scheme clearly excluded the liability of the authority to pay interest in cases of refund of consideration. It was held that this clause would apply only to cases in which the claimant himself has brought about the circumstances of refund.<sup>97</sup>

A works contract was rescinded on the ground that the contractor had not completed within the stipulated time even 10 per cent of the works. But evidence showed that the contract was improperly rescinded and, therefore, it amounted to a breach of contract. The contractor claimed Rs 20,000 as compensation, being 10 per cent of the value of the contract. The court said that the contractor was entitled to claim damages for loss of profit which he expected from the project. His claim was held to be fully justified. The High Court erred in holding that the claim should have been based on actual loss suffered.<sup>98</sup>

95. *Jacob & Youngs Inc v George E. Kent*, (1921) 230 NY 239. Lord LLOYD extracted this statement from the judgment of CARDOZO J, in the above case. See *Ruxley Electronics and Construction Ltd v Forsyth*, 1996 AC 344: (1995) 3 WLR 118. See also Andrew Phang, *Subjectivity, Objectivity and Policy—Contractual Damages in the House of Lords*, (1996) JBL. *Gautam Constructions & Fisheries Ltd v National Bank for Agriculture and Rural Development*, (2000) 6 SCC 519: AIR 2000 SC 3018, basement area not allowed to be equated with office area for rate purposes. *Army Welfare Housing Organisation v Sumangal Services (P) Ltd*, (2004) 9 SCC 619: AIR 2004 SC 1344, statement of factors relevant for determining damages in a building contract. *Premier Explosives Ltd v Singareni Collieries Co Ltd*, AIR 2010 AP 107, contractor refused to go further with performance because of hardship, the court did not accept the defence of impossibility, the aggrieved party invoked bank guarantee and also risk purchase clause, the court regarded this as proper.

96. *Chief Secy, State of Gujarat v Kothari & Associates*, (2003) 1 GCD 372 (Guj), 1270 interest was allowed from the date of legal notice.

97. *GDA v Union of India*, (2000) 6 SCC 113: AIR 2000 SC 2003. The court noted its own decision in *Sovintorg (India) Ltd v State Bank of India*, (1999) 6 SCC 406: AIR 1999 SC 2963, where in similar circumstances the National Consumer Disputes Redressal Commission directed the amount deposited by the claimant to be returned with interest at 12 per cent and the Supreme Court enhanced it to 15 per cent.

98. *Dwaraka Das v State of M.P.*, (1999) 3 SCC 500: AIR 1999 SC 1031.

Where full payment was received for the house but the same was not provided, compensation could not be awarded because the allottee submitted no particulars of his loss. He was allowed 18 per cent interest on the amount paid.<sup>99</sup>

### *Auction sale of property*

The highest bidder was to make payment of a part of the consideration money. But he could not do so even after extension of time. Subsequently he himself surrendered his claim and asked for refund of his initial deposit. His prayer that he should not be compelled to hand over the assets given to him under the project to other tenderer was rejected, but forfeiture of his earnest money was held to be arbitrary and illegal.<sup>100</sup>

### Difference between market price and contract price (sale and supply transactions)

In a sale transaction, damages are generally awarded on the basis of the difference between the contract price and market price. If the seller defaults, the buyer may have to buy elsewhere at an extra cost. If the buyer defaults, the seller may have to make a forced sale which may bring him less money than what he would have obtained under the contract. Such difference is recoverable as damages. The fact that because of the seller's default, the buyer could not carry out production in his factory and suffered losses, such losses were held to be not recoverable being a remote consequence. The buyer was under a duty to keep his loss to the minimum by buying his material elsewhere so as to keep his business going.<sup>101</sup>

The Supreme Court has been generally following these principles in its various decisions. One such decision is *Murlidhar Chiranjilal v Harishchandra Dwarkadas*.<sup>102</sup>

There was a contract for supplying canvas to be consigned to Calcutta, free on rail (f.o.r.)<sup>103</sup> Kanpur. The transport and labour charges were to be borne by the buyer. The seller failed to supply at Kanpur and the question was whether damages were to be assessed according to Kanpur or Calcutta prices and whether the seller was entitled to profits which he could have made on resale at Calcutta.

WANCHOO J (afterwards CJ) held that the goods were deliverable at Kanpur and, therefore, damages should be assessed according to the difference between contract and market prices at Kanpur, for that was the only

99. *Krishna D. Singh v Pavan T. Punjabi*, (2004) 1 Bom CR 551.

100. *Ashok Kumar Sinha v Bihar State Financial Corpn*, AIR 2009 Jhar 42.

101. *Sarvaraya Textiles Ltd v N. Rajagopal & Co*, 2005 AIHC 3372 (AP).

102. AIR 1962 SC 366: (1962) 1 SCR 653.

103. That is, the goods were to be delivered at Kanpur where the seller was responsible for loading the goods onto the train for Calcutta. This was the point of division of responsibility between the seller and the buyer.

loss which would be said to have arisen naturally in the usual course of things from the breach. The learned judge referred to two principles which he considered to be well-settled. One is that as far as money can do it, the aggrieved party is to be put in as good a situation as if the contract had been performed. This is qualified by the second principle which imposes upon the buyer the duty to take reasonable steps to mitigate the consequences of the breach. These two principles also follow from the law as laid down in Section 73 read with the *Explanation* therefor. Here the contract was to be performed at Kanpur and, therefore, the buyer should have proved the difference in prices at Kanpur which he did not do and, accordingly the court said: "On this state of the evidence it could not be said that any damage naturally arose in the usual course of things."

The buyer contended that the seller knew that the goods were required at Calcutta and, therefore, it was in his contemplation that the loss would be suffered at Calcutta. He relied upon *R. & H. Hall Ltd v W.H. Pim Junior Co's Arbitration*<sup>104</sup> and *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd*<sup>105</sup>. Distinguishing the present case from these, the learned Judge observed:

They are cases of a special type; in one case the parties knew that goods purchased were likely to be resold before delivery and therefore any loss that by the breach of contract may eventually result may include loss that may have been suffered by the buyers because of the failure to honour the intermediate contract of resale made by them; in the other case, the goods were purchased by the party for his own business for a particular purpose which the sellers were expected to know and if any loss resulted from the delay in the supply, the sellers would be liable for that loss, if they had knowledge that such loss was likely to result.

In the present case, on the other hand, the only thing that the seller knew was that the goods were to be booked to Calcutta from which the court refused to infer that the goods were meant for resale or for resale in Calcutta alone. The buyer could have sold the railway receipt at Kanpur itself, or at any other place.<sup>106</sup>

104. 1928 All ER Rep 763.

105. (1949) 2 KB 528 (CA).

106. Where the goods contracted to be sold are not marketable in the sense that they cannot be sold elsewhere, the price fixed in the contract is the appropriate measure of damages. The State Electricity Board had refused to take goods after accepting tender, *Punjab SEB v Abnash Textile Trading Agencies*, AIR 1986 P&H 323; *Pravara Sahakari Sakhar Karkhana Ltd v Express Industrial Corpn*, AIR 2002 Bom 185, seller failed to deliver balance of the goods, the buyer was not able to show any loss in production, he was allowed Rs 25,000 (estimated amount) because of the breach of the contract. *Thyssen Stahlunion GmbH v SAIL*, AIR 2002 Del 255, the party to the arbitration proved no loss, the arbitrator could not have awarded damages. *International General Electric (India) Ltd v Haradhan Sasnal*, AIR 2005 Cal 308 buyer refusing to take goods which were made to his order. Bound to pay the price with interest for late payment. *V/O Tvaazhpromexport v Mukand Ltd*, (2005) 5 Bom CR 130, the seller failed to supply, the buyer bought the material at higher price, difference not allowed irrespective of the fact that the buyer resold at higher price and, therefore, might not

A bid was made at an auction for collection and removal of residue of tree growth and firewood. Before its confirmation, a fire destroyed the residue. The bidder asked for cancellation of the bid or for reduction of its amount. But his bid was accepted and he was called upon to deposit the bid amount. On his refusal to do so, the work was reauctioned for a lower amount. The bidder was sued for the difference. The Supreme Court rejected the claim. It said that whether there had been a contract or its breach required decision of a judicial authority and then only difference could be claimed. Before acceptance of his bid, the bidder had applied for cancellation or revision of his bid because of the intervention of an act of God. There was no contract and no question of realising the shortfall from the bidder.<sup>107</sup>

The defendant failed to supply goods and cancelled orders of the buyers in view of the firm's inability to comply with them. The firm promised to refund the advance money but failed to do so. Cheques issued for refund of the principal amount and interest bounced. The buyers had failed to invoke bank guarantees. Their claim was decreed to the full amount with interest at 18 per cent p.a.<sup>108</sup>

### Whether actual purchase or sale of goods necessary

The High Court of Delhi was of the view in *Union of India v Commercial Metal Corpn*<sup>109</sup> that it is not necessary that on default by the seller to deliver, the plaintiff should have actually bought the goods elsewhere and only then claim the difference. The court said that damages could be claimed on market basis. The same ruling was repeated in *Saraya Distillery v Union of India*,<sup>110</sup> the court saying that the injured party can recover compensation on the basis of the difference between the contract and market prices without actually purchasing the goods. All that has to be proved is the buying price at which the injured party can obtain substitute goods. In *Ismail Sait*

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have suffered any loss. *Devidayal Sales (P) Ltd v State of Maharashtra*, (2006) 4 Mah LJ 662, delay in delivery of goods not disputed, the other party held to be justified in taking off from the contractor's bill the amount of loss caused.

107. A. *Mohd Basheer v State of Kerala*, (2003) 6 SCC 159. T.N. *Civil Supplies Corpn Ltd v Oswal Solven Extraction (Madras) Unit*, AIR 2002 Mad 35, failure to lift rice bran according to terms of tender, liability for damages.
108. *Explore Computers (P) Ltd v Cals Ltd*, (2006) 131 DLT 477. The Delhi High Court in *Bhushan Industrial Co (P) Ltd v Cimmco International*, (1983) 54 Comp Cases 157, carved out the distinction between a performance guarantee and an advance payment guarantee to hold that under a performance guarantee, the bank is liable to make payment only after breach of contract and after the affected party has suffered loss or damage due to breach. However in an advance payment guarantee there is absolute obligation on the bank to make payment to the affected party in the event of non-performance of the contract and the bank is not concerned with the reason for non-performance of the contract.
109. AIR 1982 Del 267.
110. AIR 1984 Del 360. *State of Orissa v Pratibha Prakash Bhawan*, AIR 2005 Ori 58, in a contract for supply of material, person claiming damages has to specifically plead the manner in which he suffered loss. Without such statement, there is no automatic claim to damages. Blocking of money is not itself a claim for damages.

*& Sons v Wilson & Co*<sup>111</sup> the Madras High Court held that the provisions contained in Section 73 did not envisage that the injured buyer must resort to actual purchase and suffer loss before claiming damages.<sup>112</sup> The Bombay High Court has expressed the view that neither Section 73 nor these rulings would apply where the parties provide for a different rule. They can lay down their own remedial system. The difference which the court saw in this case was the provision in the contract that in the event of part delivery, "the purchaser shall purchase goods from the open market and then claim damages." It was on the basis of this clause that the court held that the plaintiff was not entitled to any compensation without actually acquiring the material elsewhere and then showing his loss.<sup>113</sup> Thus special circumstances may justify departure from the rule that actual purchase is not necessary. In a case before the Calcutta High Court,<sup>114</sup> the seller did not supply anything because he wanted increase in price to which the buyer did not agree. The buyer, however, purchased some quantity from the seller at the enhanced price as a special case outside the contract. The rest of the contract was cancelled. The buyer had not purchased anything from the market. His claim for damages was not allowed. At least the market price should be discovered and produced before the court. Quantification of damages without it was not proper.

#### *Getting work done through other sources*

The contractor failed to complete the work within 4 months from the date of contract. The delay was the result of his own doings and not that of the other party. The corporation had to get the work completed by inviting fresh tenders. Extra amount paid to the other contractor was allowed to be recovered. The consequences of delay were compensated by allowing interest at 6 per cent on the amount of extra payment.

#### *Premature termination of contract*

A clause in the contract provided for compensation for delay in completion. The contract was terminated before it could be completed and also before the completion period was over. The court said that no compensation could be claimed from the contractor. No evidence was also offered of additional cost, if any, for setting the work completed from other sources.<sup>115</sup>

#### *Incomplete execution*

A road building contract was to be executed in two phases. The second phase was never executed by the contractor. He was fully paid for completion

111. AIR 1919 Mad 1053.

112. The court agreed with similar view expressed in *Vishwanath v Amarlal*, AIR 1957 MB 190.

113. *Maharashtra SEB v Sterlite Industries (India) Ltd*, AIR 2000 Bom 204: (2000) 2 Mah LJ 181.

114. *Usha Deltron Ltd v Nand Kishore Parasramka*, AIR 2001 Cal 137.

115. *Engg Projects (India) Ltd v B.K. Constructions (BKC)*, AIR 2012 Kant 35.

of the first phase. The contractor was not allowed to claim compensation for not doing the work on the second phase just by showing technicalities.<sup>116</sup>

### Award of interest on difference

Where because of the purchaser's breach, the supplier had to resell the goods elsewhere and became entitled to recover the difference, the court allowed future interest at 20 per cent p.a. from the date of the suit till the date of judgment and 6 per cent p.a. from the date of judgment till realisation.<sup>117</sup>

### Interest by way of damages

Payments of running bills were delayed in breach of contract terms. The contractor had taken loan at 13.25 per cent interest. He was awarded interest for the period of delay at 12.5 per cent. This was held to be proper, the time period between raising of bill and payment being not very large.<sup>118</sup>

### Loss of profits is special loss

Thus, loss of profits which are to accrue upon resale cannot be recovered unless it is communicated to the other party that the goods are for resale upon a special contract. This is borne out by the decision of the Supreme Court in *Karsandas H. Thacker v Saran Engg Co Ltd.*<sup>119</sup>

There was a contract to supply 200 tons of scrap iron. The buyer undertook to supply the same quantity to the Export Corporation, Calcutta. The seller failed to supply and in consequence the buyer could not keep his date with the Corporation. The Corporation recovered from him the difference between the contract price and the market price. The seller contended that he should not be held liable for anything because control price of iron scrap was still the same and he had no knowledge of the contract of resale to the Corporation.

The court found the facts of the case to be similar to illustration (k) according to which the seller has not to pay any compensation that the buyer may have to pay to his sub-buyers by reason of the breach unless he was made aware of the buyer's purpose at the time of the contract. RAGHUBAR DAYAL J said: On account of non-delivery of scrap iron he [the buyer] could have purchased the scrap iron from the market at the same controlled price and similar incidental charges. This means that he did not stand to pay a higher

116. *MSK Projects (I) (JV) Ltd v State of Rajasthan*, (2011) 10 SCC 573; (2012) 3 SCC (Civ) 818. The loss of expected profits is recoverable as a special loss but in the present case it was not allowed because of the facts of the case. See, Lon L Fuller and W.R. Perdue, *The Reliance Interest in Contract Damages*, (1936) 46 Yale LJ 52–92, noted and cited in 2011 SCYD 419. *Pramod Buildings and Developers (P) Ltd v Shanta Chopra*, (2011) 4 SCC 741: AIR 2011 SC 1424.

117. *Cotton Corp of India Ltd v Alagappa Cotton Mills*, AIR 2001 Bom 429: (2001) 3 Mah LJ 415.

118. *Mecon Ltd v Pioneer Fabricators (P) Ltd*, AIR 2008 NOC 870 (Del).

119. AIR 1965 SC 1981.



price than what he was to pay to the respondent [the seller] and therefore he could not have suffered any loss on account of the breach.... The actual loss which he suffered on account of the breach was the result of his contracting to sell 200 tons of scrap iron for export to the Export Corporation. As the seller did not know this contract, he could not have known of the likelihood of the loss actually suffered.<sup>120</sup>

Where a person was dispossessed of his leased premises prematurely, he was allowed to recover retrenchment compensation which he had to pay to labour and loss of profits calculated on the basis of figures provided by the plaintiff for the period he actually did business. The court said that that was the best indicator. The period for loss of business would be the unexpired period of the lease.<sup>121</sup> The court said that there cannot be a direct and concrete evidence of loss of profits. Damages on account of loss of profit are in the nature of prospective damages and, therefore, necessarily contingent. It is now well established principle of law that the mere fact that damages cannot be assessed with certainty does not relieve the wrongdoer of the liability to pay damages.<sup>122</sup>

**Loss of expected profit.**—The Supreme Court reiterated that loss of expected profit attributable to breach of contract is recoverable. The court distinguished the contractual measure of damages from reimbursement or compensation. The contract in this case was “build-operate-and transfer” of an adjoining road. The contractor was to collect toll money from operation. This required government notification which was delayed. The claim for loss of expected profit was allowed.<sup>123</sup>

### Consequences of delay in transit

Consequences of delay in transit have been noted by the Supreme Court in some cases. A consignment of goods with the railways reached its destination after inordinate delay, caused by gross negligence, of seven months. The plaintiff's money remained blocked for the period. He was allowed to recover interest on the money by way of damages for the loss.<sup>124</sup> In another

120. See also *Modi Sugar Mills v Union of India*, 1984 Supp SCC 338: AIR 1984 SC 1248, where liability was imposed for not returning the containers in which the goods were sent. Some principles relating to measure of damages were restated by the Supreme Court in *Trojan & Co v Nagappa Chettiar*, AIR 1953 SC 235: 1953 SCR 789. Where no time for delivery of goods is specified, the measure would be prices on the date of refusal, *P.S.N.S. Ambalavanan Chettiar v Express Newspapers Ltd*, AIR 1968 SC 741: (1968) 2 SCR 239. The right to sue for damages does not give rise to a debt which is immediately due so as to entitle the plaintiff to a set-off against his own liability to pay back the loan. *Mirza Javed Murtaza v U.P. Financial Corp*n, AIR 1983 All 235. As for the effect of inflation on damages see Duncan Wallace, *Inflation and Assessment of Construction Cost Damages*, (1982) 98 LQR 406. Acceptance of earnest money under protest does not put an end to the right of the injured party to recover damages for breach. *Mohd Usman v Union of India*, AIR 1984 Raj 156.

121. *Kishan Lal Kalra v NDMC*, AIR 2001 Del 402: (2001) 92 DLT 67 at p. 409.

122. Citing *Chaplin v Hicks*, (1911) 2 KB 786 (CA).

123. *MSK Projects (I) (JV) Ltd v State of Rajasthan*, (2011) 10 SCC 573: (2012) 3 SCC (Civ) 818.

124. *Union of India v Steel Stock Holders' Syndicate*, (1976) 3 SCC 108: AIR 1976 SC 879.

case of delay and damage, the railways have been held liable to the extent to which the value of the goods had diminished.<sup>125</sup> Where the goods are damaged by the railways the measure of damages would be the market price at the time of damage and not the price at which the injured party purchased the goods.<sup>126</sup> Regard must also be had to the type of market and setback to price because of the taste and prejudices of a special customer class.<sup>127</sup> In a fire insurance contract, the damaged goods were sold by auction under due intimation to the insurer, who did not turn up, the court allowed the difference between the insured price and the amount realised.<sup>128</sup>

### Meaning of market price

In almost all sales transactions which fail to go through the normal yardstick for working out the sum of money to which the aggrieved party is entitled is the difference between the contract and market prices.<sup>129</sup> This rule presupposes the existence of a market and the possibility of ascertaining the price of the goods in that market. Both these concepts were the subject-matter of some explanation in a case where the buyer refused to accept the goods.<sup>130</sup> The court dealt with the question in the following way:

125. *Union of India v B. Prahlad & Co*, AIR 1976 Del 236 that is to say, the market value of the goods minus their value in their damaged state; the plaintiff must do all that he reasonably can to mitigate his loss; if the damaged goods are still saleable though at a lower price, the measure of damages will be the market price of the goods minus what they would have fetched in their damaged state if the plaintiff had sold them. *Savani Transport (P) Ltd v Gangadhar Ghosh*, AIR 1986 Cal 330, the court laid stress upon the fact that the salvage value of the goods cannot be ignored and that whatever be the difficulty the court cannot shrink from ascertaining the salvage value; *Dunn v Bucknall Bros*, (1902) 2 KB 614, 623 (CA).
126. *Union of India v West Punjab Factories Ltd*, AIR 1966 SC 395; (1966) 1 SCR 580; *Union of India v Jolly Steel Industries (P) Ltd*, 1980 Supp SCC 436; AIR 1980 SC 1346. See also *M. Lachia Setty & Sons Ltd v Coffee Board*, (1980) 4 SCC 636; AIR 1981 SC 162, where the auction purchaser refused to take the goods and the Coffee Board had to reauction them, the latter allowed to recover the shortfall from the defaulter. *Union of India v K.H. Rao*, (1977) 1 SCC 583; AIR 1976 SC 626, failure to supply onions; Government allowed to recover the difference at which they purchased onions elsewhere. *M.S. Desai & Co v Hindustan Petroleum Corp Ltd*, AIR 1987 Guj 19, where it was held that a premature termination of a privileged business, such as the privilege of distributing petroleum products, by the grantor, a Government Undertaking in this case, can be challenged by a writ petition as it involves non-contractual questions also and compensation can be awarded in the same petition.
127. *Madeshwara Cargo Movers v Hindustan Cocoa Products Ltd*, (1993) 2 Bom CR 154, sensitive goods like "five-star", "double decker" were under transport.
128. *Harsud Coop Mktg Society Ltd v United India Fire and General Insurance Co Ltd*, AIR 1992 Bom 341.
129. *Hajee Ismail & Sons v Williams & Co*, ILR (1918) 41 Mad 709; *Mackay v Kameshwar Singh*, (1931-32) 59 IA 398; AIR 1932 PC 196; *Vishwanath v Amarlal*, AIR 1957 MB 190. Where no market existed to enable the buyer to effect his purchase of the coal of the contract quality, the defaulting seller's rates with other buyers from him were taken into account for guidance. *Jugmohandas Vurjiwandas v Nusserwanji Jahangir Khambatta*, ILR (1901-02) 26 Bom 744.
130. *Shearson Lehman Hutton Inc v Maclaine Watson & Co Ltd*, (1990) 3 All ER 723 (QBD). (Commercial Court) See also *A. P. Paper Mills Ltd v Principal Secy*, (1997) 3 An LT 649 (DB), buyer refused supply of hardwood, sale by auction at his risk, loss recoverable.

In assessing damages for failure to perform a contract for the purchase of goods the measure of damages payable by the defaulting buyer is the difference between the contract price and the current or market price at the date of breach; based on a hypothetical sale of the particular amount of the goods in question in the available market, but disregarding any characteristics of the seller which might have led to a lower price being obtained. In determining whether there is an 'available market' for the goods in question, if the seller actually offered the goods for sale, there is no available market unless there is one actual buyer on that day at a fair price. If, on the other hand, there is only a notional or hypothetical sale there is no available market unless on the relevant day there were in the market sufficient traders, potentially in touch with each other, to evidence a market in which the seller could if he had wished have sold the goods. Furthermore, the market price on a hypothetical sale is the fair market price for the total quantity of the goods if they had to be sold on the relevant day, but taking into account the price which might be negotiated within a few days with other potential buyers who were not part of the market on that day only because of difficulties in communication. It followed that the plaintiffs were entitled to damages based on the fair market or current price on the date of the breach for 7755 tonnes of standard grade tin, but that price in turn would be based on both the price which would have been obtained by a sale of all the tin on 12 March, 1986, and the price which would have been obtained by sales negotiated over a short period before or after that date.<sup>131</sup>

### Escalation of costs

A works contract was in writing. Delay in completing the works was due to the contractor's fault. It seemed that he was delaying things in order to take advantage of escalation of prices. Full payment was already made to him according to the originally agreed rates. A *quantum meruit* suit for

131. The court followed: *Garnac Grain Co Inc v HMF Faure and Fairclough Ltd*, (1968) AC 1130: (1967) 3 WLR 143 (HL). See further *Rajasthan Rajya Sahkari Kraya Vikraya Sangh Ltd v Ram Mohan*, (1988) 2 Raj LR 962 where it was observed: It is not necessary to prove actual loss. Anticipated loss of profit can be determined by the court while awarding compensation. What is necessary is that the plaintiff should establish what was the contractual rate of purchase and what was the rate of article on the date on which it was to be supplied. The difference between the two is a loss to the purchaser, if it is not supplied by the seller to the purchaser. This is so because the buyer cannot be allowed to be put in a better position than he would have been if the contract had been performed. *Wertheim v Chicoutimi Pulp Co*, 1911 AC 301: (1908–10) All ER Rep 707 (PC). In this case goods were delivered by the seller late when they were worth Rs 50 per ton in the market as against the contract price of Rs 80, but the buyer got Rs 70 per ton on resale. He was allowed Rs 10 per ton by way of his loss. *Gauri Datt Basdeo v Nanik Ram Chauthmal*, (1916) 14 All LJ 597, where no time for delivery was fixed and the buyer having given notice fixing the time, the time so fixed was the day on which prices were to be compared. *Engell v Fitch*, (1869) LR 4 QB 659 (Exch). On deliberate refusal to sell land, the value of resale by the seller was taken as the evidence of market value.

recovering escalated costs was held to be not maintainable.<sup>132</sup> Where in a scheme for allotment of houses the limit of escalation cost was fixed in the scheme itself, the Authority was not allowed to charge anything in excess of the limit by way of escalation.<sup>133</sup>

### Agreement to provide finance

An arrangement to provide funds for an approved project is not a typical contract; it is only a facility. Where, after releasing some instalments, the lending institution refuses to go further, the borrower cannot compel it, nor hold it liable in damages for the loss of his expectations, nor claim a set-off against its demand for interest on the money already provided, his right, if any, to damages.<sup>134</sup>

Commercial parties are free to vary their contracting terms and to withdraw credit facilities without constituting duress. There is no economic duress where there are an arm's length commercial dealings between two companies having equality of bargaining power. This principle was laid down in a case in which facts were:

A company bought cigarettes in bulk from a person who happened by a mistake to deliver them to a wrong address. Before they could be collected from that place, they were stolen. The supplier invoiced the buyer for the price thinking that the property in the goods had passed to the buyer and threatened to cut off the buyer's credit facilities if he did not pay. The buyer paid to secure his credit facilities and brought an action for repayment saying that the payment was under pressure amounting to economic duress. This was not allowed.<sup>135</sup>

### Compensation for liability to third party before payment

Where, on account of the seller's default, the buyer was not able to keep his commitment under a sub-sale and became liable to compensate the third party, the court said that there is no rule of law that a liability without

132. *Gujarat Housing Board v Harilal Jethalal*, AIR 2001 Guj 259.

133. *Kanpur Development Authority v Sheela Devi*, (2003) 12 SCC 497: AIR 2004 SC 400. *Bareilly Development Authority v Vrinda Gujarati*, (2004) 4 SCC 606: AIR 2004 SC 1749, escalation of costs of flats in accordance with Rules duly intimated to and accepted by allottees. *Food Corporation of India v Ratnali N. Gwalani*, AIR 2004 MP 215: (2004) 2 CCC 393 (MP), delays in working because of obstructions caused by the Department, contract provided for escalation if delay was not due to contractor's fault, escalation allowed.

134. *Industrial Finance Corp of India v Sehgal Papers Ltd*, AIR 1986 P&H 21. This is so because the liability to pay damages is not a debt whether the claim is for liquidated or unliquidated damages. Debt is created by a decree. See *Textile Machinery Corp Ltd v Kichcha Sugar Co Ltd*, (1989) 2 Cal LT 101, the court relied on *Union of India v A.L. Rallia Ram*, AIR 1963 SC 1685: (1964) 3 SCR 164; *Kesoram Industries & Cotton Mills Ltd v CWT*, AIR 1966 SC 1370; *Union of India v Raman Iron Foundry*, (1974) 2 SCC 231: AIR 1974 SC 1265.

135. *CTN Cash and Carry Ltd v Gallaher Ltd*, (1994) 4 All ER 714 (CA). *Nagnath Kaulwar & Sons v Govindram Shyamsunder*, AIR 2004 Bom 271: (2004) 3 Mah LJ 457, action could lie at the place where the goods were to be received by paying for consignment documents and receiving delivery.

payment does not constitute a recoverable loss. Where a seller of goods breaches his contract with the buyer so as to result in the buyer being liable to a third party to whom he had agreed to resell the goods, the buyer has a claim for substantial damages against the seller prior to his discharging the liability to the third party by payment. In this case the first buyer had become impecunious and, therefore, unable to pay. His claim against the seller was assigned to the sub-buyer who had brought the claim in the right of the buyer. The court held that the liability to the third party was enforceable even before it was discharged.<sup>136</sup>

### Unfair or wrongful dismissal of employee

In an action for damages for breach of contract arising out of wrongful dismissal of an employee, the Employment Tribunal upheld the claim and awarded damages for unfair dismissal. The employee subsequently brought a civil suit for financial loss arising from psychological injury caused by the manner of dismissal. It was held that an employee had no right of action at common law to recover financial losses arising from the unfair manner of his dismissal. A conclusion to the contrary would be inconsistent with the statutory system for dealing with unfair dismissals established by the Parliament in 1971 to remedy the deficiencies in law as it then stood. ([English] Industrial Relations Act, 1971).<sup>137</sup>

### Agreement by employee to release all claims

An employee agreed to release all claims that he might have against the employer. The employee subsequently brought an action for a claim which was not known to exist when the release was signed. The House of Lords held that the claim was allowable. Their Lordships said that although a party could in a compromise agreement supported by valuable consideration agree to release claims or rights of which he was not and could not be aware, the court would be slow to infer that he had done so in the absence of a clear language to that effect. In this case, neither the bank nor the employee could have realistically supposed that a claim for stigma damages lay within the realm of practical possibility. On a fair construction of the documents, it was impossible to conclude that the parties had intended to provide for the release of rights and surrender of claims which they could never have had in contemplation at all. If the parties had sought to achieve so extravagant a result, they should have used language which left no room for doubt and which might at least have alerted the employee to the effect of what he was agreeing.<sup>138</sup>

136. *Total Liban Sa v Vitol Energy Sa*, 2001 QB 643 (QBD).

137. *Johnson v Unisys Ltd*, (2001) 2 WLR 1076 (HL).

138. *Bank of Credit and Commerce International S.A. v Ali*, (2002) 1 AC 251: (2001) 2 WLR 735 (HL).

### MEASURE OF DAMAGES

Once it is determined whether general or special damages have to be recovered they have to be evaluated in terms of money. This is the problem of measure of damages and is governed by some fundamental principles.

#### Claim for damages is not debt

A claim for damages arising out of breach of contract, whether for general or liquidated damages, remains only a claim till its adjudication by the court and becomes a debt only after the court awards it. Till then and on the basis of the claim alone, the claimant is not entitled to present a winding up petition of the defendant company on the ground of its inability to pay debts.<sup>139</sup>

#### Damages are compensatory, not penal

In the words of ASQUITH J: "It is well-settled that the governing purpose of damages is to put the party whose rights have been violated in the same position, so far as money can do so, as if his rights have been observed."<sup>140</sup> "The primary aim or principle of the law of damages for a breach of contract is to place the plaintiff in the same position he would be in if the contract had been fulfilled, or to place the plaintiff in the position he would have occupied had the breach of the contract not occurred. When this is accomplished, the primary aim or principle of the law of damages has been fulfilled."<sup>141</sup> In a case involving the construction of a swimming-pool where the depth of the pool happened to be less than what was specified, the pool being otherwise useful, the court allowed the difference in value of the pool as provided and its value as it should have been provided. The court did not allow the cost of setting right the pool because that would have given the recipient windfall profits which are impermissible because the award of damages is to compensate the claimant and not to punish the payer.<sup>142</sup>

*Robinson v Harman*<sup>143</sup> is an apt illustration. The defendant, having agreed to grant a lease of a certain property to the plaintiff, refused to do

139. *Greenhills Exports (P) Ltd v Coffee Board*, (2001) 4 Kant LJ 158 (DB).

140. In *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd*, (1949) 2 KB 528 (CA). *Chief Secy, State of Gujarat v Kothari & Associates*, (2003) 1 GCD 372 (Guj), damages must be commensurate with injury sustained; award of damages being compensatory and not retributive.

141. See *HAWTHORNE in Friedman Iron & Supply Co v J.B. Beaird & Co*, (1952) 63 SO 2d 144 (SC of Louisiana); Collected from Shepherd and Wellington, CONTRACT AND CONTRACT REMEDIES (1957) 912; *Murlidhar Chiranjilal v Harishchandra Dwarkadas*, AIR 1962 SC 366; (1962) 1 SCR 653.

142. *Ruxley Electronics and Construction Ltd v Forsyth*, 1996 AC 344; (1995) 3 WLR 118. The court was of the view that the owner would be unjustly enriched if he were allowed the cost of building a new pool and were nevertheless allowed to retain the existing one. *Thakorlal V. Patel v Lt. Col. Syed Badruddin*, (1993) 1 Guj LR 28, motive and manner of breach irrelevant, defendant is not to be punished.

143. (1848) 18 LJ Ex 202.

so. The court allowed the plaintiff by way of damages the expenses incurred by him on the preliminary legal work and also for the profits which he would have earned if the lease had been granted to him. PARKE B stated the principle thus:

What damages is the plaintiff entitled to recover? The rule of the common law is that where a party sustains a loss by reason of a breach of contract, he is, so far as money can do it, to be placed in the same situation, with respect to damages, as if the contract had been performed.

Thus, damages are given by way of compensation for the loss suffered by the plaintiff and not for the purpose of punishing the defendant for the breach.<sup>144</sup> Motive for and the manner of breach are not taken into account because generally “punitive damages are not recoverable for breach of contract”.<sup>145</sup>

### Inconvenience caused by breach

But the inconvenience caused by the breach may be taken into account. Thus, for example, in *Hobbs v London & South-Western Rly Co*,<sup>146</sup> where a train pulled its passengers to a wrong direction and consequently the plaintiff and his wife, finding no other conveyance, nor a place to stay, had to walk home at midnight, the jury allowed £ 8 as the damages for the inconvenience suffered by the plaintiffs in being obliged to walk and £ 20 in respect of the wife’s illness caused by catching a cold. On appeal, the court of Queen’s Bench held that the £ 8 was properly awarded but not £ 20.

The inconvenience of walking back must be taken to have been within the reasonable contemplation of the parties. But the wife’s cold was not the necessary or even the probable consequence of the breach.

But in the subsequent case of *McMahon v Fields*<sup>147</sup> the above decision was criticised and damages were allowed when the plaintiff’s horses were turned out of the defendant’s stable in breach of contract and they caught a cold before an alternative accommodation could be found for them.

144. For example, delay in payment of money will entail interest on remittances but other consequences are not taken into account. *Graham v Campbell*, (1878) LR 7 Ch D 490 (CA).

145. THE AMERICAN RESTATEMENT OF THE LAW OF CONTRACTS, S. 342 entitled *N. Sukumaran Nair v P. Narayanan*, 1996 SCC OnLine Mad 83: (1996) 2 LW 40, punitive damages may be allowed in special cases like breach of promise of marriage as in this case. Exemplary damages were allowed for loss of reputation and injured feelings. The future of the frustrated woman would be bleak, chances of marriage remote. *Suresh Babu Nath v Hargovind Batham*, AIR 1995 MP 82, compensation for breach of promise of marriage and for fraud for duping into sex on promise of marriage and resulting pregnancy.

146. (1875) LR 10 QB 111. *Hamlin v Great Northern Rly Co*, (1856) 1 H&N 408: 156 ER 1261.

147. (1881) LR 7 QBD 591 (CA). “The assessment of damages cannot be based on the economic policy of the country from where the goods are to be imported.” *Naihati Jute Mills Ltd v Khyaliram Jagannath*, AIR 1968 SC 522: (1968) 1 SCR 821. Quoted from I.C. Saxena, *Law of Contract*, ANNUAL SURVEY OF INDIAN LAW (1967–68). An arbitrator is also bound by the provisions of S. 73. *Bungo Steel Furniture (P) Ltd v Union of India*, AIR 1967 SC 378.

### Loss caused by misrepresentation

The price at which a thing is purchased and its difference with the real value, when misrepresentation about it is discovered, is the yardstick for compensation. A horse was purchased described as fit for races. But it turned out to be of different breed. That was discovered after a long process of trial and error and after discovery its market value was much less. It was held that where an article purchased as a result of misrepresentation could have been resold immediately after the sale for the price paid but by the time the misrepresentation was discovered its value had fallen by reason of a defect in it which had then become apparent, the appropriate measure of damages would be the difference between the purchase price and its value at the time when misrepresentation is discovered and not the difference between the purchase price and its actual value at the time of purchase.<sup>148</sup> The court referred to the decision in *Doyle v Olby (Ironmongers) Ltd*<sup>149</sup> which deals with cases in which a business or an article is not purchased for immediate resale. The court cited the following dictum of WINN LJ:

It appears to me that in a case where there has been a breach of warranty of authority, and still more clearly where there has been a tortious wrong consisting of a fraudulent inducement, the proper starting point for any court called on to consider what damages are recoverable by the defrauded person is to compare his position before the representation was made to him with his position after it, brought about by that representation, always bearing in mind that no element in the consequential position can be regarded as attributable loss and damage if it be too remote a consequence. It will be too remote not necessarily because it was not contemplated by the representor but in any case where the person deceived has not himself behaved with reasonable prudence, reasonable common sense or can in any true sense be said to have been the author of his own misfortune. The damage that he seeks to recover must have flowed directly from the fraud perpetrated on him.

WINN LJ then assessed the damages in that case by reference to precisely what the plaintiff had done after acquiring the business including selling the business at some later time and giving credit for that sale price. It is perhaps also useful to refer in this connection to *Johnson v Agnew*<sup>150</sup> in which Lord WILBERFORCE said:

“The general principle for the assessment of damages is compensatory, i.e. that the innocent party is to be placed, so far as money can do so, in the same position as if the contract had been performed. Where the contract is one of sale, this principle normally leads to assessment of damages as at the date of the breach, a principle recognised and embodied

148. *Naughton v O'Callaghan*, (1990) 3 All ER 191.

149. (1969) 2 QB 158.

150. 1980 AC 367; (1979) 2 WLR 487 (HL).

in Section 51 of the Sale of Goods Act, 1893. [S. 59 of the Indian Sale of Goods Act, 1930] But this is not an absolute rule; if to follow it would give rise to injustice, the court has power to fix such other date as may be appropriate in the circumstances. In cases where a breach of a contract for sale has occurred, and the innocent party reasonably continues to try to have the contract completed, it would to me appear more logical and just rather than tie him to the date of the original breach, to assess damages as at the date when (otherwise than by his default) the contract is lost. Support for this approach is to be found in the cases. In *Ogle v Earl Vane*<sup>151</sup> the date was fixed by reference to the time when the innocent party, acting reasonably, went into the market; in *Hickman v Haynes*<sup>152</sup> at a reasonable time after the last request of the defendants (the buyers) to withhold delivery. In *Radford v De Frobergville*<sup>153</sup> where the defendant had covenanted to build a wall, damages were held measurable as at the date of the hearing rather than at the date of the defendant's breach, unless the plaintiff ought reasonably to have mitigated the breach at an earlier date."

A person owned two neighbouring hairdressing salons. He sold one of them. He deliberately and falsely told the buyer before the sale that he would not work at the other salon except in cases of emergency. This statement was particularly important since it meant that the clientele would not follow him to the neighbouring business. After the sale was completed, the buyer discovered that the seller was working full-time at his other neighbouring business. An award of £10,000 was allowed to the buyer for the consequential loss of business. BELDAM LJ observed:<sup>154</sup>

"If in fact the plaintiffs lost the profits which they could reasonably have expected from running a business in the area of a kind similar to the business in this case, I can see no reason why they do not fall within the words of Lord ATKIN in *Clark v Urquhart*,<sup>155</sup> 'actual damage directly following from the fraudulent inducement'."

The court noted the development in this field to this effect as shown by a number of decisions which make it clear that the tortious measure of damages is the true one.<sup>156</sup>

### Incidence of taxation

Since the principle is that of compensation, and no more than compensation, the benefits, if any, that the plaintiff has received against the loss suffered are to be taken into account. For example, where a dismissed employee

151. 1868 LR 3 QB 272; *affd. Ogle v Earl Vane*, 1868 LR 3 QB 272.

152. (1875) LR 10 CP 598.

153. (1977) 1 WLR 1262.

154. *East v Maurer*, (1991) 1 WLR 461 (CA).

155. 1930 AC 28 (HL).

156. One such decision was *Chesneau v Interhome Ltd*, (1983) 114 NLJ 341.

receives unemployment benefit, his compensation is reduced by that amount. If he is given compensation for loss of prospective earnings, the amount of income tax which he would have to pay on the amount if received as earnings would go to reduce the compensation. This principle was laid down by the House of Lords in *British Transport Commission v Gourley*<sup>157</sup> and was followed by the Court of Appeal in *Parsons v BNM Laboratories Ltd*<sup>158</sup> where HARMAN LJ stated the effect of the House of Lords' decision in these words:

The case (*Gourley* case) decides that in an action whether in tort for injuries arising from negligence or in contract for wrongful dismissal where the loss of the plaintiff consists wholly or in part in a loss of earnings, and where the sum to be awarded in damages will not suffer deduction of tax in his hands, then in ascertaining the plaintiff's loss his tax liability, that is to say, the sum which he would have had to pay in income tax including sur tax in acquiring the lost earnings, must be deducted from his loss in assessing the damage... Unemployment insurance is a sum receivable by contract made by the employed man and his employer each of whom contributes to the State on the footing that if and when the servant is unemployed the State will make good part of his earnings to him. I do not think that such a payment is truly analogous to insurance money, as in the leading case of *Bradburn v Great Western Rail Co*<sup>159</sup> where there was a purely voluntary contract made by the plaintiff. This is a contribution which he is bound to make with the very object of mitigating the damage which inability to work will do him. It is just as if his employer continued to pay part of his wages. The loss he suffers is *pro tanto* diminished and therefore cannot be charged against the wrongdoer.<sup>160</sup>

### Nominal damages (no loss situation)

Where the plaintiff suffers no loss the court may still award him nominal damages in recognition of his right. But this is in the discretion of the court. The court may altogether refuse to award any damages or may award even substantial damages. "The court is competent to award reasonable compensation in case of breach, even if no actual damage is proved or shown to have been suffered in consequence of breach of contract."<sup>161</sup> It has been pointed out by the Delhi High Court, following some earlier High Court decisions,<sup>162</sup> that Section 73 does not give any cause of action unless and

157. 1956 AC 185: (1956) 2 WLR 41 (HL).

158. (1964) 1 QB 95: (1963) 2 WLR 1273 (CA).

159. (1874) LR 10 Ex 1.

160. Damages allowed in an arbitration award reflect business loss not speculation loss. *CIT v Shantilal (P) Ltd*, (1983) 3 SCC 561: AIR 1983 SC 952.

161. *T.A. Choudhary v State of A.P.*, (2004) 3 ALD 357 (DB).

162. *Sitaram Bindraban v Chiranjilal Brijlal*, AIR 1958 Bom 291.

until damage is actually suffered. The case before the court was *Union of India v Tribhuwan Das Lalji Patel*.<sup>163</sup>

A contract for the supply of sleepers to the railway administration contained a number of clauses including this that irrespective of whether the Government suffered any loss or not on account of the contractor's failure to supply, the Government was entitled to damages. The contractor failed to supply, but the railways did not suffer any loss. Even so an action for damages was instituted against the contractor.

It was argued on the strength of some High Court decisions<sup>164</sup> and illustration (a) to Section 73 that it is not necessary for the aggrieved party to prove that he purchased the goods from an alternative source and suffered a loss; he is entitled to the difference in the contract and market prices in any case. Reliance was also placed upon the Privy Council decision in *Mackay v Kameshwar Singh*<sup>165</sup> where it was observed that the difference, if the market price exceeds the contract price, is the sole damage in general recoverable and a contract of resale or repurchase is immaterial. PRAKASH NARAIN J did not agree with this contention. He took the Privy Council decision to be no authority for the proposition that irrespective of whether there was any loss, damages must still be paid and that the decision is only in the context of quantum of damages. Thus, he refused to countenance the view that compensation can be awarded when there has been no loss or damage. "If the contrary view was to be taken", he said, "the provision of Section 73 will become nugatory and a party would be penalised, though the other party has suffered no loss."

Even so the category of nominal damages cannot be ruled out. Thus, where a Government contract for building roads was terminated, before the expiry of the notice period as prescribed in the contract, in circumstances which did not entitle the contractor to recover loss of profit, he was allowed nominal damages.<sup>166</sup>

Where a seller of land suffered no loss from the buyer's refusal to perform, and, on the contrary, made a huge windfall profit by selling the land to another person, he was not permitted to forfeit the buyer's advance and this in spite of the fact that the land remained vacant till the new buyer was found.<sup>167</sup> A piece of land was sold. As a part of the sale agreement, the buyer

163. AIR 1971 Del 120. Citing *Vishwanath v Amaralal*, AIR 1957 MB 190. *Prem Lata v MCD*, AIR 2003 Del 211, alleged delay in supply, but no loss shown to have been caused. Claim for damages not allowed. *Maharashtra SEB v Sterlite Industries (India)*, (2001) 8 SCC 482: (2002) 1 Bom CR 415: (2002) 1 ICC 178, arbitrator's finding that damages could not be awarded under S. 73 not disturbed by the court.

164. Disagreeing with the above cited Madhya Bharat case and the decision of the Madras High Court in *Ismail Sait & Sons v Wilson & Co*, AIR 1919 Mad 1053.

165. (1931-32) 59 IA 398: AIR 1932 PC 196.

166. *State of M.P. v Recondo Ltd*, 1989 MPLJ 822. *Electronic Enterprises v Union of India*, AIR 2000 Del 55, the Government used the goods supplied, no damages claimed or proved for alleged late deliveries. The Government was not allowed to withhold payment.

167. *Mohanlal v Dayaldas & Co*, AIR 1976 Raj 68.

covenanted to build only 72 houses on the land. In breach of the agreement, the buyer built 77 houses. The seller sued him for breach of the covenant. The question was what should be the correct measure of damages where there is the following set of circumstances: (a) There has been a deliberate breach of contract, (b) the party in breach has made a profit from that breach, and (c) the innocent party is in financial terms in the same position as if the contract had been fully performed.<sup>168</sup> STYN LJ proceeded as follows stating and applying the first principles:

“An award of compensation for breach of contract serves to protect three separate interests. The starting principle is that the aggrieved party ought to be compensated for loss of his positive or expectation interests. In other words, the object is to put the aggrieved party in the same financial position as if the contract had been fully performed. But the law also protects the negative interest of the aggrieved party. If the aggrieved party is unable to establish the value of a loss of bargain he may seek compensation in respect of his reliance losses. The object of such an award is to compensate the aggrieved party for expenses incurred and losses suffered in reliance on the contract. These two complementary principles share one feature. Both are pure compensatory principles. If the aggrieved party has suffered no loss he is not entitled to be compensated by invoking these principles. The application of these principles to the present case would result in an award of nominal damages only.

There is, however, a third principle which protects the aggrieved party’s restitutive interest. The object of such an award is not to compensate the plaintiff for a loss, but to deprive the defendant of the benefit he gained by the breach of contract. The classic illustration is a claim for the return of goods sold and delivered where the buyer has repudiated his obligation to pay the price. It is not traditional to describe a claim for restitution following a breach of contract as damages. What matters is that a coherent law of obligations must inevitably extend its protection to cover certain restitutive interests. How far that protection should extend is the essence of the problem before us.”<sup>169</sup>

The object of the award in this case was not to compensate the plaintiff for financial injury but to deprive the defendant of an unjustly acquired gain. As to this his Lordship said:

“The introduction of restitutive remedies to deprive cynical contract breakers of the fruits of their breaches of contract will lead to greater uncertainty in the assessment of damages in commercial and consumer disputes. It is of paramount importance that the way in which disputes are likely to be resolved by the courts must be readily predictable. Given the premise that the aggrieved party has suffered no loss, is such a dramatic

168. *Surrey County Council v Bredero Homes Ltd*, (1993) 1 WLR 1361 (CA).

169. Citing MAC GREGOR ON DAMAGES and Professor PBH Birke, CIVIL WRONGS, A NEW WORLD (Butterworth Lectures, 1990–91).

extension of restitutionary remedies justified in order to confer a windfall in each case on the aggrieved party? I think not. In any event such a widespread availability of restitutionary remedies will have a tendency to discourage economic activity in relevant situations. In a range of cases, such liability would fall on the underwriters who have insured relevant liability risks. Inevitably the underwriters would have to be compensated for the new species of potential claims. Insurance premiums would have to go up. That, too, is a consequence which mitigates against the proposed extension. The recognition of the proposed extension will in my view not serve the public interest. It is sound policy to guard against extending the protection of the law of obligations too widely. The present case involves no breach of fiduciary obligations. It is a case of breach of contract. The principles governing expectation or reliance losses cannot be invoked. Given the fact of the breach of contract the only question is whether restitution is an appropriate remedy for this wrong. The case does not involve any invasion of the plaintiff's property interests even in the broadest sense of that word. I would therefore rule that no restitutionary remedy is available and there is certainly no other remedy available."

In such a case, however, the court may award nominal damages. The decision of the Court of Appeal in *Charter v Sullivan*<sup>170</sup> is an apt illustration.

The defendant, having contracted to buy a Hillman car from a car dealer, ultimately refused to buy. Within a week the car was sold to another customer. Indeed, the dealer was able to sell as many cars as he wanted and lost nothing on account of the defendant's breach. Even so he wanted to recover the loss of his profit.

The court held that he was entitled only to nominal damages and 40 shillings were allowed.

As against it, in another case<sup>171</sup> on account of the customer's breach in not lifting the car in terms of his agreement, the dealer had to return the car to the manufacturer. He was allowed to recover the profit which he would have made on sale of the car to the defaulting customer.

### *Compensation in no loss situations*

An action was brought for breach of contract arising out of overuse of musical recordings. The court generally orders in such cases an account of profits made in overuse but in this case the breach had caused no economic loss.<sup>172</sup> The court said:

Although the court could order an account of profits for breach of contract where the claimant could not prove that it had suffered any

170. (1957) 2 QB 117; (1957) 2 WLR 528 (CA).

171. *W.L. Thompson Ltd v Robinson (Gunmakers) Ltd*, 1955 Ch 177.

172. *Experience Hendrix LLC v PPX Enterprises Inc*, 2003 EWCA Civ 323: *The Times*, April 19, 2003 (CA).

financial loss, this would only be done in exceptional circumstances such as national security, exceptional profits and fiduciary breaches. Damages could be awarded for a breach of a restriction which had been imposed to protect the claimant's property, where an injunction was refused, because the court was only concerned with past profits.<sup>173</sup> This was not an exceptional case which justified an account of profits. Even so, the defendant should make a reasonable and substantial payment for the unauthorised use of the master records.

Where the highest bidder committed default in payment but the forest authorities suffered no serious prejudice due to the default, the court said that forfeiture of the whole of the deposit money was not justified. The court ordered refund of the actual amount without interest or costs.<sup>174</sup>

### Refund on partial cancellation of contract

The agreement was for sale of damaged food grains. The purchaser deposited a certain amount with the Food Corporation. An application was made for cancellation a certain part of the agreement which was not capable of being performed. This was conceded and some refund was made. The purchaser was not allowed to sue the corporation for breach of contract in the matter of refund. There was no proof of any such breach.<sup>175</sup>

### Pre-contract expenditure

Pre-contract expenditure may be recovered as damages if it was within the contemplation of the parties. The Court of Appeal laid down this principle in *Anglia Television Ltd v Reed*.<sup>176</sup> Here, a television artiste who having been engaged as a leading actor for a television film, repudiated the contract. The producer was unable to find a substitute and, therefore, had to abandon the project. The loss of profit was incapable of being estimated. The court allowed him as damages the money spent by him in engaging a director, a designer, etc., as this kind of expenditure was within the contemplation of the parties. Lord DENNING MR explained the principle thus:

The plaintiff in such a case as this has to make election: he can either claim for his loss of profits; or for his wasted expenditure. But he must elect between them. He cannot claim both. If he has not suffered any loss

173. *Modi Entertainment Network v WSG Cricket Pte Ltd*, (2002) 3 Bom CR 634, spillover of signals which was natural into the territory of other licensed broadcasters did not constitute breach of contract. Inspite of the efforts to prevent, overspill continued but, no loss of revenue was caused.

174. *State of A.P. v Singam Setty Yellamanda*, (2003) 2 An WR 154: AIR 2003 AP 182; *State of T.N. v T.R. Surrendranath*, AIR 2008 NOC 974 (Mad), road building contract, tenderer deposited earnest money and additional security, default by tenderer, the Highway Authority could prove no loss, liable to refund earnest and security amounts as otherwise there would be unjust enrichment.

175. *Food Corporation of India v Laxmi Cattle Feed Industries*, (2006) 2 SCC 699: AIR 2006 SC 1452.

176. (1972) 1 QB 60: (1971) 3 WLR 528: (1971) 3 All ER 690 (CA).

of profits—or if he cannot prove what his profits would have been—he can claim in the alternative the expenditure which has been thrown away, that is, wasted by reason of the breach. That is shown by *Cullinane v British Rema Mfg Co Ltd.*<sup>177</sup>

If the plaintiff claims the wasted expenditure, he is not limited to the expenditure incurred after the contract was concluded. He can claim also the expenditure incurred before the contract, provided that it was such as would reasonably be in the contemplation of the parties as likely to be wasted if the contract was broken.... He (the party, committing the breach) must pay damages for all the expenditure so wasted and thrown away. This view is supported by the recent decision of BRIGHTMAN LJ in *Lloyd v Stanbury*.<sup>178</sup> There was a contract for the sale of land. In anticipation of the contract—and before it was concluded—the purchaser went to such expense in moving a caravan to the site and in getting his furniture there. The seller afterwards entered into a contract to sell the land to the purchaser, but afterwards broke his contract. The land had not increased in value, so the purchaser could not claim for any loss of profits. But BRIGHTMAN J held that he could recover the cost of moving the caravan and furniture, because it was “within the contemplation of the parties when the contract was signed”. That decision is in accord with correct principle, namely, that wasted expenditure can be recovered when it was wasted by reason of the defendant’s breach of contract. It is true that, if the defendant had never entered into the contract, he would not be liable, and the expenditure would have been incurred by the plaintiff without redress; but, the defendant having made his contract and broken it, it does not lie in his mouth to say he is not liable, when it was because of his breach that the expenditure has been wasted.

Competitive tendering involves considerable expenditure of time and money. The tenderers do not get paid for it. Where a party tendered for a construction work, and before anything, was given to believe that the work would be allotted to them. They were encouraged to do further work in estimating and tendering, but ultimately the contract was awarded to someone else. For such further work the party was allowed to recover payment.<sup>179</sup> Where a quotation for a residential development was accepted “subject to contract” but no contract could follow because in the intervening period land prices crashed and the project had to be abandoned, it was held that the bidder’s expenditure in payment of fees to professional people for preparing plans of development was not recoverable. They had incurred it voluntarily and not on encouragement. The court said:<sup>180</sup>

177. (1954) 1 QB 292 (CA).

178. (1971) 1 WLR 535.

179. *William Lacey (Hounslow) Ltd v Davis*, (1957) 1 WLR 932. Expenditure was allowed to be recovered under the doctrine of restitution as explained in *Marston Construction Co Ltd v Kigass Ltd*, (1989) 15 Con LR 116.

180. *Regalian Properties plc v London Dockland Devp Corp*, (1995) 1 WLR 212.

"Each party to such negotiations must be taken to know that pending the conclusion of a binding contract any cost incurred by him in preparation for the intended contract will be incurred at his own risk in the sense that he will have no recompense for those costs if no contract results."

### Agreement to provide scientific process

The agreement was for setting up a project for converting menthons to menthol. The agreement showed that the requisite technical know-how was to be provided by the Indian Institute of Petroleum (IIP). A huge expenditure was incurred in setting up the plant. But the IIP failed in its experiment of converting the material even up to five years. It was something which had to be done under the contract within five months. The arbitrator awarded compensation of Rs 90 lakhs for the loss suffered in setting up the plant. The Court said that there was nothing against public policy in the award.<sup>181</sup>

### Mental pain and suffering and punitive damages (non-pecuniary loss)

In ordinary cases damages for mental pain and suffering caused by the breach are not allowed.<sup>182</sup> It is not appropriate to award damages for anguish and vexation caused by breach of contract when the contract is an ordinary commercial one.<sup>183</sup> But they may be allowed in special cases. According to the American RESTATEMENT such damages may be allowed where "the breach was wanton or reckless and caused bodily harm" and where the defendant had reason to know that the breach would cause mental suffering.<sup>184</sup> An illustration is found in a case before the Supreme Court of Colorado, U.S.<sup>185</sup>

The defendant, a banking corporation, agreed to loan the plaintiff money for a trip to California by crediting his account with such sums as he might need after reaching his destination. The plaintiff reached California, but the defendant refused to give him the promised credit.

The court allowed damages for humiliation and mental suffering. The banker could have foreseen that the plaintiff, having gone away from home and among strangers on the basis of the promise, would naturally suffer mental anguish if his cheque was not honoured.

181. *Council of Scientific and Industrial Research v Goodman Drug House (P) Ltd*, AIR 2007 Utt 58.

182. *Withers v General Theatre Corp*n Ltd, (1933) 2 KB 536 (CA); *Bangalore Development Authority v Syndicate Bank*, (2007) 6 SCC 711, compensation for mental agony and suffering, such a compensation cannot be awarded under the general law of contract, it can be awarded by applying the principle of administrative law, where the seller (houses) being a statutory authority acts negligently, arbitrarily or capriciously.

183. *Hayes v James & Charles Dodd (a firm)*, (1990) 2 All ER 815, 826 (CA); *Bliss v South East Thames Regional Health Authority*, 1987 CLY 1304; 1987 ICR 700; *Perry v Phillips*, 1982 CLY 2164.

184. S. 341 of the Restatement.

185. *Westosen v Olathe State Bank*, (1925) 78 Colo 217.

### *Three cases listed by the House of Lords*

The House of Lords in *Addis v Gramophone Co Ltd*<sup>186</sup> listed three situations in which mental pain and suffering can be taken into account:

There are three well-known exceptions to the general rule..., namely, actions against a banker for refusing to pay a customer's cheque when he has in his hands funds of the customer, to meet it; actions for breach of promise of marriage (now abolished in England), and actions like that in *Flurean v Thornhill*<sup>187</sup> where the vendor of real estate, fails to make title.

Lord ATKINSON then added that he knew of none other and that any tendency to create a fourth exception should be checked rather than stimulated. His Lordship warned that application of tort principles to contract would lead to confusion, uncertainty and anomalies and occasionally to injustice and make the law a still more 'lawless science' than it is said to be. Suppose, for example, that a debtor refused to pay his creditor, should the damages be reduced if the debtor is helpless and apologetic and increased if the refusal is from a malicious desire to injure the creditor? His Lordship expressed the opinion that these matters should not play any part in the law of contract where the principle is that the aggrieved party "is to be paid adequate compensation in money for the loss of that which he would have received had his contract been kept, and no more". The facts of the case were:

The plaintiff was employed by the defendant company at a certain salary and commission on trade done. He could be dismissed by six months' notice. He was given six months' notice and at the same time another person was appointed to his place, thus preventing him from acting as manager even for the notice period and earning his commission.

The House of Lords rejected the claim for damages for the humiliating manner of dismissal, but allowed damages for the commission and salary which he had lost. Lord ATKINSON explained the principles thus:

The damages the plaintiff sustained by his illegal dismissal were: (1) the wages for the period of six months...; (2) the profits on commission which would in all probability have been earned by him; and possibly (3) damages in respect of time which might reasonably elapse before he could obtain other employment.

His Lordship then referred to the sum of £600 which was awarded to him not in respect of these heads of damage, but in respect of the harsh and humiliating way in which he was dismissed, including the pain he experienced by reason of the imputation upon him conveyed by the manner of his dismissal. This kind of compensation was accordingly not allowed.

186. 1909 AC 488: 78 LJ KB 1122: 1010 LT 466. Followed in *Haron Bin Mundir v Singapore Amateur Athletec Assn*, (1992) 1 SLR 18 High Court Singapore so as to hold that in business matters damages for emotional loss are not allowed.

187. (1776) 2 WB 1078.

The reason for this conservative approach and reason why it would have to be diluted in the modern circumstances of life appears from the following statement.

"In an age where stress has, generally speaking, clearly increased and has become more of a reality in the perception of people generally, it is, perhaps, not surprising that there has been increasing dissatisfaction with this general approach. However, it is also clear that the courts have to be vigilant to guard against inflated and (more importantly) bogus claims, lest the release of the floodgates sweep away all semblance of reason, common sense and justice."<sup>188</sup>

This line of reasoning was approved by the House of Lords in *Johnson v Unisys Ltd.*<sup>189</sup> Here also their Lordships did not allow damages for unfair dismissal as a special count of liability under the head psychological injury caused by the manner of dismissal. The claim was for summary dismissal after an irregularity. Their Lordships observed by a majority that there is no right of action at common law to recover financial losses arising from unfair manner of dismissal. Any other conclusion would be contrary to the statutory system for dealing with unfair dismissals. Parliament in creating the new system under the Employment Rights Act, 1996 (English) had not left any scope for contractual damages where the power of dismissal was not exercised in good faith or fairly. The Parliament has established an entirely new system outside the ordinary courts with tribunals staffed by a majority of lay members applying new statutory concepts and offering statutory remedies. Many of the new rules such as the limit on the amount of the statutory award, are not based upon any general principles which the courts used to apply.

### Breach of promise of marriage

A sum of Rs 27,000 was awarded for breach of promise of marriage. The amount covered lowering esteem in society, mental torture and expenses on engagement ceremony.<sup>190</sup>

### Mental distress caused by negligent survey report or advice

The same principle was followed where mental distress was caused by a negligent survey report as a result of which a house was purchased at a price higher than it was worth and considerable time and money had to be spent on making it habitable. A sum of £ 8000 (being £ 4000 to each plaintiff) was awarded at the trial, but the Court of Appeal held that damages for breach

188. Andrew Phang, *Subjectivity, Objectivity and Policy—Contractual Damages in the House of Lords*, (1996) JBL 362.

189. (2001) 2 WLR 1076 (HL). For another case in which damages for humiliating manner of dismissal were not allowed see *Johnson v Unisys Ltd.*, (2001) 2 WLR 1076 (HL), compensation awarded by the industrial court was supposed to cover that aspect also.

190. *Tulshiram v Roopchand*, (2006)-2 Mah LJ 647: AIR 2006 Bom 183.

of a normal contract of survey are only recoverable for distress caused by physical consequences of the breach and not for mental distress not caused by physical discomfort or inconvenience resulting from the breach and that accordingly the plaintiffs were not entitled to damages for distress and inconvenience but instead they would each be awarded damages of £750 for physical discomfort.<sup>191</sup>

In *Hayes v James & Charles Dodd (a firm)*,<sup>192</sup> the court was of the view that the law on this point would seem to be in some doubt, but felt that, if the law needs clarification, it may be provided by the House of Lords or by the Law Commission. Damages awarded for negligence or want of skill, whether against professional men or anyone else, must provide fair compensation, but no more than that. The court believed that in one or more American States damages are awarded for wrongfully defending an action instead of admitting it, but felt that there was no such remedy in England. In *Perry v Sidney Phillips & Sons (a firm)*<sup>193</sup> damages were awarded for the distress, worry, inconvenience and trouble which the plaintiff had suffered while living in the house he bought, owing to the defects which his surveyor had overlooked. Lord DENNING MR considered that these consequences were reasonably foreseeable. KERR LJ stated a narrower test:<sup>194</sup>

So far as the question of damages for vexation and inconvenience is concerned, it should be noted that the deputy judge awarded these not for the tension or frustration of a person who is involved in a legal dispute in which the other party refuses to meet its liabilities. If he had done so, it would have been wrong, because such aggravation is experienced by almost all litigants. He awarded these damages because of the physical consequences of the breach, which were all foreseeable at the time. The fact that in such cases damages under this head may be recoverable, if they have been suffered but not otherwise, is supported by the decision of this court in *Hutchinson v Harris*.<sup>195</sup>

Applying these principles to the case of *Hayes v James & Charles Dodd (a firm)*<sup>196</sup> STAUGHTON LJ said:

191. *Watts v Morrow*, (1991) 1 WLR 1421 (CA). Following *Perry v Sidney Phillips & Sons (a firm)*, (1982) 1 WLR 1297 (CA) where the principle of modest compensation in such cases was adopted; *Hayes v James & Charles Dodd (a firm)*, (1990) 2 All ER 815, 826 (CA) agreeing with the remark in *Bliss v South East Thames Regional Health Authority*, 1987 CLY 1304: 1987 ICR 700, 718 that damages of this kind are only recoverable where the subject-matter of the contract or duty in tort is to provide peace of mind and freedom from distress. The other cases in which awards were modified and adjusted for inflation since the date of award: *Roberts v Hampson & Co*, (1990) 1 WLR 94; *Cross v Martin & Mortimer*, (1989) 1 EG LR 154; *Steward v Rapley*, (1989) 1 EGLR 159; *Bigg v Howard Son & Gooch*, (1990) 1 EGLR 173; *Hipkins v Jack Cotton Partnership*, (1989) 2 EGLR 157.

192. (1990) 2 All ER 815 (CA).

193. (1982) 1 WLR 1297 (CA).

194. *Ibid* at p. 712: 1307.

195. (1978) 10 Build LR 19 (CA).

196. (1990) 2 All ER 815, 825 (CA).

I am not convinced that it is enough to ask whether mental distress was reasonably foreseeable as a consequence, or even whether it should reasonably have been contemplated as not unlikely to result from a breach of contract. It seems to me that damages for mental distress in contract are, as a matter of policy, limited to certain classes of case. I would broadly follow the classification provided by DILLON LJ in *Bliss v South East Thames Regional Health Authority*:<sup>197</sup>

‘...where the contract which has been broken was itself a contract to provide peace of mind or freedom from distress ...’

It may be that the class is somewhat wider than that. But it should not, in my judgment, include any case where the object of the contract was not comfort or pleasure, or the relief of discomfort, but simply carrying on a commercial activity with a view to profit. So I would disallow the item of damages for anguish and vexation.

The facts were that the defendant solicitor told the plaintiffs who were shifting their motor repair garage that they would have the right of way from the backside of the site. But that was not to be. The supposed passage was very quickly blocked after completion of the purchase. The plaintiffs were unable to carry on business without access to the site. They claimed damages for wasted expenditure and for anguish and vexation. The court held as follows:

The judge had been entitled in the circumstances to award damages on the basis of comparing the plaintiffs' actual situation with the position in which they would have been if they had never entered into the transaction at all rather than with the position they would have been in had the transaction been successful. He had therefore been entitled to award damages on the basis of the capital expenditure thrown away in the purchase of the business and the expenses incurred. However, damages for anguish and vexation arising out of a breach of contract were not recoverable unless the object of the contract was to provide peace of mind or freedom from distress and accordingly, were not recoverable for anguish and vexation arising out of the breach of a purely commercial contract. It followed that the damages would be reduced by the amount awarded for anguish and vexation and to that extent the appeal would be allowed.<sup>198</sup>

The decision of the House of Lords in *Kuddus v Chief Constable of Leicestershire Constabulary*<sup>199</sup> shows that limits set by the decision in *Addis* may no longer keep arresting the progress of law. The decision of their

197. 1987 ICR 700, 718.

198. See also *Allied Maples Group v Simmons & Simmons*, (1995) 1 WLR 2117 (CA), which considered the question of the liability of a solicitor for negligent advice in the matter of takeover of business; *Brown v K.M.R. Services Ltd*, (1995) 4 All ER 598, in the circumstances of the case it was proper to assess damages on the basis of what, on the balance of probabilities, the plaintiffs would have probably done in the matter of investment if they had been properly advised. Evidence showed that they would have reduced the investment.

199. (2002) 2 AC 122; (2001) 2 WLR 1789 (HL).

Lordships in *Malik v Bank of Credit and Commerce International*<sup>200</sup> is an example of this forward movement. Stigma compensation was awarded in this case to an aggrieved employee for an unworthy removal. A learned commentator encompasses this development in the context of the law in Canada in the following words<sup>201</sup>: "By contrast the Supreme Court of Canada has now fully embraced it (the principle) in several recent cases and especially in *Whiten v Pilot Insurance Co*<sup>202</sup>... It is still far from certain that punitive damages will be awarded for 'pure' breach of contract between commercial parties of similar commercial experience and sophistication, rather even after *Whitten* it is still the case that such awards may be limited to situations where hurt feelings or damaged peace of mind are at stake, for example, in wrongful dismissal or insurance claim denial cases respectively."

### *Compensation for non-pecuniary loss*

The House of Lords in their decision in *Farley v Skinner*,<sup>203</sup> held that there is no reason why compensation for non-pecuniary damage should not be allowed. In this case, the claimant was considering the purchase of a tranquil country property. He instructed a surveyor to report on the volume of aircraft noise in the area. The surveyor negligently reported that the property was unlikely to be affected by the noise. The claimant bought the property and subsequently discovered that it was significantly affected by such noise. He stayed in the property and brought an action against the surveyor to recover compensation for non-pecuniary loss caused by inconvenience, etc. Their Lordships approved the award of £10,000 as damages for breach of a contractual duty of care in respect of the survey report. Their Lordships said that where a surveyor gives a contractual undertaking to investigate a matter important to the buyer's peace of mind, the buyer is in principle entitled to recover non-pecuniary damages for breach of that undertaking. There is no reason why the scope of recovery should depend upon the object of the contract as ascertained from all its constituent parts. It is sufficient that a major or important object of the contract is to give pleasure, relaxation, or peace of mind. Such a claim is also not barred by the fact that the surveyor undertook only to exercise reasonable care rather than to guarantee the achievement of a result. It would be a singularly unattractive result if a professional person who undertakes a specific obligation to exercise reasonable care to investigate a matter, which his client told him to be important, could please himself even by non-performance when his very payment was a part of the consideration for that performance. The fact that the claimant

200. 1998 AC 20: (1997) 3 WLR 95 (HL).

201. M.H. Ogilvie: *After Whitton: Punitive Damages for Breach of Contract in Canada*, 2004 JBL 549.

202. (2002) 1 SCR 595: (2002) 209 DLR (4th) 257 (Canada), citing G.H.L. Fridman: *Punitive Damages for Breach of Contract: A Canadian Innovation*, (2003) 119 LQR 20, heavy compensatory award was made against the insurer.

203. (2001) 4 UKHL 49 (HL).

nevertheless chose to stay there could not deprive him of his right because it was no justification for the surveyor's breach of duty. Lord STEYN advised a caution that awards of non-pecuniary damages should be restrained and modest. It is important that logical and beneficial developments in the law should not contribute to the creation of a society bent on litigation.

Their Lordships cited the principle of law as stated by BINGHAM LJ in *Watts v Morrow*<sup>204</sup> to the effect that a contract breaker is not in general liable for any distress, frustration, anxiety, displeasure, vexation, tension, or aggravation which his breach of contract may cause to the innocent party, but that this rule is not an absolute one. It is based on a consideration of policy. An exceptional category is where the very purpose of the contract is to provide pleasure, relaxation, peace of mind, or freedom from molestation. The learned Lord Justice, however added that a contract to survey the condition of a house for a prospective purchaser does not fall within the exceptional category and, therefore, in such cases damages would be recoverable only for physical inconvenience and discomfort caused by the breach.

It was observed in another case that sentences and phrases in a single speech of a judge cannot be treated as if they were provisions in an Act of Parliament. Judges are not supposed to frame definitions or to lay down hard and fast rules.

An important development for this branch of the law was *Ruxley Electronics and Construction Ltd v Forsyth*,<sup>205</sup> *Laddingford Enclosures Ltd v Forsyth*.<sup>206</sup> The plaintiff specified that the swimming pool should at the deep end be 7'6" deep. The contractor did not comply with this specification. The pool had the depth of only the standard 6'. The House of Lords found the usual "cost of cure" measure of damages to be wholly disproportionate to the loss suffered and economically wasteful. Their Lordships awarded the moderate sum of £2500 for the plaintiff's disappointment in not receiving the swimming pool he desired. In *Knott v Botton*<sup>207</sup> an architect was asked to design a wide staircase for a gallery and an impressive entrance hall. He failed to do so. The plaintiff spent money in improving the staircase to some extent and he recovered the cost of the changes. He also claimed damages for disappointment and distress in the lack of an impressive entrance hall. The Court of Appeal disallowed this part of the claim.

### *Housing service*

The complainant filed a petition before the Monopolies and Restrictive Trade Practices Commission against a Development Authority on the grounds of excessive delay and failure to hand over possession of the plot. Commission awarded, among other counts, Rs 50,000 as damages for mental agony suffered by the complainant. The Supreme Court held that this

204. (1991) 1 WLR 1421 at 1445 (CA).

205. 1996 AC 344; (1995) 3 WLR 118.

206. *Ibid.*

207. (1995) 45 Con LR 127.

was an error on the part of the Commission.<sup>208</sup> In such cases, the court said, the normal rule should apply which is that the vendor should pay damages for the purchaser's loss of bargain by paying the market value of the property at the time fixed for completion less the contract price. The purchaser may claim loss of profit which he intended to make from a particular use of the land if the vendor had actual or imputed knowledge of such use. For delay in performance the normal nature of damages is the value of the use of the land for the period of delay, viz., usually its rental value. Interest can be awarded on equitable grounds in appropriate cases. The rate of interest should neither be too high nor too low. Interest at the rate of 12 per cent p.a. should be just and proper and would meet the ends of justice in this case.

#### *Negligent surgical operation*

A 24-year-old female was surgically operated for sterilisation. The operation was performed in a crude and primitive manner without administering even local anaesthesia.

The doctor showed incompetence in cutting small intestine instead of fallopian tube which became the direct cause of death. Rs 1,60,000 with 12 per cent interest were awarded. The amount was directed to be paid to the husband and minor children of the deceased.<sup>209</sup>

#### *Negligence in maintenance of electricity lines*

Where the petitioner's sole son, who was blind, died of electrocution by coming in contact with a pole which was live due to inefficient maintenance, the Municipal Corporation was directed to pay Rs 50,000 with 12 per cent interest.<sup>210</sup>

#### *Contracts for providing peace of mind or preventing mental distress*

But now the principle is revolving round to this that in every proper case damages for mental distress can be recovered.

#### *Photographer's failure to appear at wedding*

In a Scottish case, a photographer who had agreed to take photographs at a wedding, failed in breach of his contract to appear there. As a result the bride had no photographs of her wedding. She was allowed damages for the resulting injury to her feelings.<sup>211</sup>

#### *Failure by band to attend wedding reception*

A businessman of some standing in his community engaged a top 12 men band for his daughter's wedding reception to which some 1200 guests came.

208. *GDA v Union of India*, (2000) 6 SCC 113: AIR 2000 SC 2003.

209. *Joseph v George Moonjely*, AIR 1994 Ker 289.

210. *Xavier v State of T.N.*, AIR 1994 Mad 306, interest running from the date of petition till payment. The court followed *Kumari v State of T.N.*, (1992) 2 SCC 223: AIR 1992 SC 2069.

211. *Diesen v Samson*, 1971 SLT 49; noted in CURRENT LAW, November 1971.

The band was to play for four hours during the reception, the meal and then for dancing. Such music was part of the expected hospitality. On the day, the band-master telephoned, half-an-hour after they should have arrived, to say that they had broken down 200 miles away and were not coming. Friends of the host assisted him by arranging two local musicians and by playing tapes but that was started later and was no proper substitute for the band. It was held that a daughter's wedding is a very special day for any father. It was a matter of personal prestige for the father to offer the special band as part of his hospitality to both sides' families and his many business and social friends and he suffered a considerable humiliation by the events. The court ordered refund of advance deposit and £800 as general damages for disappointment and humiliation.<sup>212</sup>

### *Cancellation of wedding reception*

A motel was booked for the plaintiff's daughter's wedding reception to which 105 guests had been invited. The motel contracted to provide a three-course meal, sherry reception and a room where a band would play for dancing. The motel cancelled this 48 hours before the wedding. The only alternative was a small function room at a public house where a cold buffet was laid on. The room was cramped and there was no space for dancing. It was held that an only daughter's wedding reception is of unique importance for a parent. General damages of £750 were awarded for inconvenience and disappointment plus £265 special damages for the cancellation fee of the band and telephone calls to notify guests of the changed venue.<sup>213</sup>

### *Holiday cases*

In *Jarvis v Swan Tours Ltd*<sup>214</sup> Lord DENNING MR described the principle that damages cannot be recovered for mental pain and suffering caused by the breach to be out of date.

The plaintiff wanted to spend his holidays. He was attracted by the representations held out by a tourist agency that certain kind of facilities, recreation, company, etc., would be provided by them on tours conducted by them. The promises turned out to be unreal and the plaintiff was much disappointed. He was allowed damages for disappointed expectations, the court saying that in a proper case damages for mental distress can be recovered and one such case is a contract for holiday.

212. *Dharni v Dharni*, 1988 CLY 409.

213. *Hotson & Hotson v Payne*, 1988 CLY 1047.

214. 1973 QB 233: (1972) 3 WLR 954 (CA). In another case, *Wilson v Pegasus Holidays (London)*, 1988 CLY 1059, a hotel was described in its brochure as offering a "superb standard of accommodation", but in fact it had inadequate toilet and bathing facilities, exposed electric wiring and was in a very poor decorative order. It was booked for skiing holiday, but the slopes were at some distance and the bus service was erratic. Following kinds of damages were awarded: £125 for loss of enjoyment and diminution in the value of the holiday; £400 for extra stress, worry and responsibility.

His Lordship laid down: "In a proper case damages for mental distress can be recovered in contract just as damages for shock can be recovered in tort. One such case is a contract for a holiday, or any other contract to provide entertainment. If the contracting party breaks his contract, damage can be given for disappointment, the distress, the upset and the frustration caused by the breach. (Such loss may be) difficult to assess in terms of money, but it is no more difficult than the assessment which the courts have to make everyday in personal injury cases for loss of amenities."

This was followed in *Jackson v Horizon Holidays*:<sup>215</sup>

The plaintiff entered into a contract for a holiday for himself, his wife and two children. In many material respects the defendant failed to provide the holiday in accordance with their description. The court allowed damages not merely for the distress to the plaintiff but also for the wife and children.

A Canadian court allowed damages for mental distress where a motor home was contracted to be borrowed to the defendant's knowledge for holiday purposes and he failed to provide it.<sup>216</sup> Where the buyer communicated to the seller that one of his reasons for buying the car was a forthcoming touring holiday but problems with the car spoilt the holiday. The disappointment of a spoilt holiday was a substantial element in the award sanctioned by the Court of Appeal.<sup>217</sup>

### Package tour

The tourist agency owes responsibility not only for its own services but also for services hired from others for further stages of the package. The plaintiff booked a package tour of mainland China for his daughter. The service was offered by a Hong Kong travel company. At the border with mainland China, the tour was joined by a guide of a Chinese travel company. One of the items was to visit and cross a lake. The party missed the ferry. An alternative arrangement was made by hiring a speedboat of a third agency. The boat was small. It could carry only eight at one time out of 24. The driver of the boat completed two trips and refused to go for the third. Another employee of the third agency was to drive the boat. This driver negligently operated too fast, caused a crash in which the plaintiff's daughter was thrown overboard and lost in drowning. The original Hong Kong agency tried to save its skin by saying that the tragedy was not due to any act on the part of their employees. Holding them liable the court said:<sup>218</sup>

215. (1975) 1 WLR 1468 (CA). Thirty-three hours dislocation caused to a tourist party being conducted under package holiday which obstruction was due to air traffic control problems, was held to be not a breach and, therefore, an action for inconvenience was dismissed. *Compton v I.L.G. Travel*, 1990 CLY 625.

216. *Elder v Koppe*, (1974) 53 DLR (3d) 705 (NSSC).

217. *Jackson v Chrysler Acceptances Ltd*, 1978 RTR 474.

218. *Wong Mee Wan v Kwan Kin Travel Services Ltd*, (1996) 1 WLR 38 (PC). For a study of Statutory and Case Law developments in this field see, David Grant, *Tour Operators*,

"Taking the contract as a whole their Lordships consider that the first defendant here undertook to provide and not merely to arrange all the services included in the programme, even if some activities were to be carried out by others. The first defendant's obligation under the contract that the services would be provided with reasonable skill and care remains even if some of the services were to be rendered by others, and even if tortious liability may exist on the part of those others."

### *Solicitor's failure*

The principle is now no more confined to holiday cases. The decision of the English Court of Appeal in *Heywood v Wellers (a firm)*<sup>219</sup> has rendered it to be a principle of general import.

The plaintiff engaged a firm of solicitors to obtain an injunction against a man who was harassing her. The solicitors obtained an injunction but failed to bring the man before the court when he molested her again with the result that the harassment remained unabated.

She was allowed to recover damages from the solicitors for the consequential mental anguish. The court expressed the opinion that this kind of loss is no different from any other loss, for any reasonable man could have foreseen that continued molestation would cause further mental distress.

JAMES J proceeded as follows:

It is also the law that where, at the time of making a contract, it is within the contemplation of the contracting parties that a foreseeable result of a breach of the contract will be to cause vexation, frustration or distress, then if a breach occurs which does bring about that result, damages are recoverable under that heading. Not in every case of breach of contract on the part of a solicitor towards his client will damage be recoverable under this head. It is only when the services contracted for are such that both solicitor and client contemplate that a failure by the solicitor to perform the contract will foreseeably occasion vexation, frustration or distress.

A solicitor was employed by the client to prevent removal by the father of the client's children from the United Kingdom. The solicitor accordingly notified the passport agency but failed to renew the notification. The father added children to his passport and took them away. The mother sued the solicitor. The court said that the solicitor's failure to renew the notification was a breach of contractual duty. There was a causal connection between the negligence and removal of the twins from UK. The fact that damages

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*Package Holiday Contracts and Strict Liability*, 2001 JBL 253.

219. 1976 QB 446: (1976) 2 WLR 101. *Bailey v Bullock*, (1950) 2 All ER 1167, in a case of solicitor's negligence it was held that damages for inconvenience and discomfort could be recovered for the solicitor's failure to get possession of premises for his client but not damages for annoyance and mental distress.

for loss of a child's company were not recoverable in tort, did not mean that there could be no recovery under contract too. A claim founded on a contract which had the object of providing pleasure, relaxation, peace of mind or freedom from molestation is an exception to the general rule that the contract breaker cannot be made liable for damages for injured feelings or distress. Accordingly, she was entitled to recover damages for mental distress.<sup>220</sup>

#### *Loss of pets due to carrier's negligence*

This principle was applied by a Canadian court to the distress caused by the loss of a pet due to a carrier's negligence.<sup>221</sup>

The plaintiffs wanted to carry their two pet dogs with them in the flight. The plaintiffs were willing to pay for the entire first class section of the aircraft for the purpose of keeping their pets with them. But the defendants did not agree to that. They told the plaintiffs that the pets would be carried in the cargo compartment and assured that they would arrive in the first class condition. But, as the luck would have it, the pets happened to be placed next to a container of dry ice which threw out fumes. One pet perished and the other was taken ill.

The plaintiff successfully claimed damages, apart from, for the loss of the dog, for "the anguish and sadness".

#### *Demotion of employee without reasonable cause*

Where an employee was relegated without appropriate cause to a position of lesser responsibility in breach of contract, it was held that since, it must have been in the contemplation of the parties that the breach, without reasonable cause, would expose the plaintiff to the vexation, frustration and distress which he had suffered, the plaintiff was entitled to damages of five hundred pounds. The plaintiff had become depressed, anxious, frustrated and ill.

#### *Delay in payment*

The person whose payment is delayed is entitled to loss of interest on the money. Where an insurer made payment of the life policy money one-and-a-half year after the policy became a claim and there was no justification for the delay, the claimant was allowed to recover the money with interest.<sup>222</sup>

#### *Dishonour of cheques*

An account holder in a building society described himself as a self-employed businessman in export and import dealings stating his

220. *Hamilton Jones v David & Snape*, (2004) 1 WLR 924; 2003 EWHC 3147( Ch).

221. *Newell v Canadian Pacific Airlines*, (1976) 74 DLR (3d) 574 (Ont Ct Ct).

222. *Adaramani Devi v LIC*, 1998 AIHC 3006 (Ori).

income to be below £5000. He issued a cheque for £4500. The building society happened wrongly to dishonour this cheque. He claimed substantial damages.

The Court of Appeal was of the view that it was too late in time (1996) to draw a distinction between traders and non-traders for the purposes of assessment of compensation for loss of honour in respect of general damages flowing from the dishonour of a cheque. The court said:<sup>223</sup>

The credit rating of individuals is as important for their personal transactions, including mortgages and hire-purchase as well as banking facilities, as it is for those who are engaged in trade, and it is notorious that central registers are now kept. I would have no hesitation in holding that what is in effect a presumption of some damage arises in every case, insofar as this is a presumption of fact.

### *Trade secrets*

Intellectual property rights include trade secrets, confidential information, know-how, patents, trade marks, copyrights, designs, etc. These rights do not have any physical corpus. They are intangible. They are the creations of brain and constitute a vital business property in the competitive market economy. A complete protection of such rights is necessary for encouragement of creative and innovative abilities. The protection afforded by law is exemplified in the following statement in Charlesworth:<sup>224</sup>

Intellectual property rights overlap, protecting different facets of a product, for example, the product itself may be patented, its method of manufacture may be protected as a trade secret; sales literature and software used to run the product, may be protected by copyright; its shape or configuration may be protected by new design right; and its name by a trade mark.

The usual remedies for breach of confidence are: action for an account of earnings from the use of the information; action for damages and an injunction for prevention of misuse. For an action to succeed it would be necessary to show that there was information of confidential nature which was shared under an obligation of confidence with the person proceeded against and that there was an actual or threatened use or disclosure of the information. If the information has already become a part of public knowledge, no action may lie. Every information or general knowledge of facts which comes to be picked up by an employee cannot be labelled as trade secret or confidential information. A TV personality who left employment of one company and joined another which proposed to establish a competitive business could not be restrained from doing so only for the fear that he

223. *Kpobraror v Woolwith Building Society*, (1996) 4 All ER 199 at p. 124 (CA).

224. CHARLESWORTH'S BUSINESS LAW (5th Edn, 1991).637.

might use his experience gained in the first employment in promoting the business of the next employer.<sup>225</sup>

There is an implied term in a contract of employment that an employee may not make use of his employer's trade secrets. An employee who comes in touch with such information can be restrained from using it to the prejudice of his employer's interest.<sup>226</sup> Secrets may also be shared with a collaborator on the condition that the company shall maintain secrecy of all the technical information and that it should obtain corresponding secret arrangements from its employees.<sup>227</sup>

An injunction can be issued against a third party also with whom the former employee gets new employment from using or further using any information of confidential nature provided to him by the employee in breach of his duty of confidence. If he still persists even after getting notice of the breach of confidence, he can be held liable in damages for the use of an intellectual property which did not belong to him.

### Damages for breach of confidence

Damages are also allowed for breach of confidence.

Three actresses formed a rock group. They conceived an idea of producing a television serial, based on their experience, to focus attention on their individual and group life so as to contrast their collective character with their individual character. The idea was conveyed in the course of oral negotiations to a television company. This resulted in a written agreement which provided some payment to the ladies but forbade the company from using the idea unless the ladies were given the opportunity to act and they declined it. Without giving the opportunity, the company produced the programme with great commercial success.

The company was held liable in damages to the ladies. The agreement contained an implied negative covenant. The circumstances in which it was communicated imported an obligation of confidence. The content of the idea was clearly identifiable, original, of potential commercial attractiveness and capable of reaching fruition.<sup>228</sup>

225. *Star India (P) Ltd v Laxmiraj Setharam Nayak*, (2003) 3 Mah LJ 726. For a study of the object showing the need for and techniques of protection see Ter Kah Leng and Susanna HS Leong, *Contractual Protection of Business Confidence*, (2002) JBL 513.

226. *Canadian Aero Service Ltd v O'Malley*, (1971) 23 DLR (3rd) 632, Ontario CA, Canada, here no use of secret knowledge was involved in obtaining a contract in competition with the former employer. *Attwood v Lamont*, (1920) 3 KB 571, the employee was not in touch with trade secrets.

227. *Niranjan Shankar Golikari v Century Spg & Mfg Co Ltd*, AIR 1967 SC 1098: (1967) 2 SCR 378.

228. *Fraser v Thames Television Ltd*, 1984 QB 44 (HL). Liability to damages is not excusable only because it is difficult to assess them with precision. In such cases the buyer is entitled to presumptions as to his loss. See *Andard Mount (London) Ltd v Curewel (India) Ltd*, AIR 1985 Del 45. It was a contract for sale of human albumin. *Prema Korgaokar v Mustak Ahmed*, AIR 1987 Guj 106. Breach of promise of marriage is actionable. The amount of

In a case before the House of Lords: a partnership firm imported goods and sold them to customers in the United Kingdom. Its principal customer was EB. The firm and EB were banking with the defendant bank. The same bank used to issue transferable letters of credit. Though EB was in touch with the details, it did not know the prices being paid by the firm to its suppliers. The bank had to send certain documents to the firm but by mistake sent them to EB from where EB came to know of the firm's profits margins and stopped taking the material from the firm. The firm sued the Bank for wrongful disclosure of confidential information. It was held that the loss of profits on repeat business was not too remote. The firm was entitled to recover the amount equal to the profits lost during the period for which the business was likely to have continued with EB. Their Lordships upheld the award which the judge had made, on a reducing basis extending over a four-year period.<sup>229</sup>

### Injunction to restrain breach of confidence

Where damages would not be an appropriate remedy, an injunction may be issued against improper use of confidence. An illustration is *Attorney General v Barker*.<sup>230</sup>

The first defendant was employed in the royal household between 1980 and 1983 on terms which included a contractual undertaking not to disclose, publish or reveal any incident, conversation or information concerning any member of the royal family or any visitor or guest which came to his knowledge during his employment or any information relating to his employment in the royal service unless duly authorised in writing to do so. The undertaking was perpetual and worldwide and the first defendant expressly acknowledged that it included an agreement on his part not to publish any such matter in any book. The second defendant, which was a Canadian company controlled by the first defendant, planned to publish in the United Kingdom a book written by the first defendant about his service in the royal household. The book was a flagrant breach of the first defendant's undertaking. The first defendant having refused to comply with the terms of his undertaking, the Attorney General issued a writ applying for worldwide injunctions against the defendants restraining publication of the book.

The court held as follows: The Attorney General's claim was not based on a breach of confidentiality but on a breach of contract, the consideration for the covenant by the first defendant not to publish matters concerning his experiences in the royal household being the agreement to take him on the staff of the royal household and to pay him wages or a salary. Accordingly,

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compensation depends upon circumstances among which mental pain and suffering is one factor.

229. *Jackson v Royal Bank of Scotland Plc*, (2005) 1 WLR 377 (HL).

230. (1990) 3 All ER 257 (CA).

the first defendant had for a consideration entered into a negative covenant which was limited neither territorially nor in time and such a covenant was enforceable provided it could not be attacked for obscurity, illegality or on public policy grounds such as being in restraint of trade. The covenant was not void on any ground of public policy or on the ground that it restricted the freedom of expression abroad contrary to Article 10 of the Convention for the Protection of Human Rights and Fundamental Freedoms and in the circumstances the balance of justice required that an interlocutory injunction having extra-territorial effect be granted against both defendants.

It was contended in a case before the Bombay High Court<sup>231</sup> that what was conveyed to the other party was an idea in the abstract without any concrete shape. The Division Bench did not agree with the contention and cited the following passage from Copinger and Skone James on COPYRIGHT:<sup>232</sup>

“There is a broad and developing equitable doctrine that he who has received information in confidence shall not take unfair advantage of it or profit from the wrongful use or publication of it. He must not make any use of it to the prejudice of him who gave it, without obtaining his consent or, at any rate, without paying him for it. It has for long been clear that the Courts can restrain a breach of confidence arising out of a contract or any right to property .... The ground of equitable intervention is that it is unconscionable for a person who has received information on the basis that it is confidential subsequently to reveal that information. Acceptance of information on the basis that it will be kept secret affects the conscience of the recipient of the information. In general it is in the public interest that confidences should be respected, even where the consider can point to specific financial detriment to himself. If a defendant is proved to have used confidential information, directly or indirectly obtained from a plaintiff without his consent, express or implies, he will be guilty of an infringement of the plaintiff’s rights.”

In another case before it, the Bombay High Court said that confidentiality was to cover only such information about which the parties had agreed in writing that it would be confidential and not every other piece of information.<sup>233</sup>

### Injunction for restraining breach of contract

A supply system to the Army which had been going on since 1960 was not allowed to be scrapped all of a sudden by blacklisting the supplier. A person dealing with the Government in matters of sale and purchase develops legitimate interest and expectations. The order of blacklisting amounted to denial of equality of opportunity. Before issuing such an order some explanation

231. *Zee Telefilms Ltd v Sundial Communications (P) Ltd*, (2003) 5 Bom CR 404.

232. 13th Edn.

233. *Villa Moda General Trading Co W.L.L. v Chordia Fashions (P) Ltd*, (2005) 3 CLT 331 (Bom).

should have been called for. The court would not interfere in the matter if it is decided again by giving opportunity to the supplier.<sup>234</sup>

### Injunction for restraining alienation of property

The petitioners succeed under Section 9 of the Arbitration and Conciliation Act, 1996 in making out a *prima facie* case of and balance of convenience in their favour and, therefore, an injunction was issued restraining the respondent from disposing of property which was comprised in the asset purchase agreement.<sup>235</sup>

### Writ remedy against termination of dealership

A dealership agreement was terminated by reason of breaches on the part of the dealer. He applied for a writ against the order expecting that contractual obligations should be decided on the basis of affidavit evidence. The court refused to entertain the petition. The matter related to contract, trade and business. It should be adjudicated through an appropriate civil action.<sup>236</sup>

### Termination of contract by Government and writ remedy

The foreign company to whom the contract for construction of a public road was awarded could not complete the project within the stipulated time inspite of the fact that sufficient time and opportunity was provided for the same. The Government terminated the contract in accordance with its stipulations. This was questioned in a writ. The court found that the termination had become necessary in public interest. There was no violation of Article 14 and, therefore, no scope for interference.<sup>237</sup>

An Authority which had granted a flyover contract to the writ petitioner arbitrarily rescinded it. The contractor's writ petition against it was held to be maintainable. A writ court is not always bound to relegate the aggrieved party to a civil suit and that merely because the other party has raised a factual dispute. The mere raising of a dispute about a fact does not make it a disputed fact. The writ court can go into such an attempt at disputing things, adjudicate it and grant appropriate relief.<sup>238</sup>

### Direction for payment in writ jurisdiction

The work was performed by the contractor in accordance with the applicable terms and conditions as prescribed by the State Government. The amount of payment which was due for the completed work was admitted by the State Authority. The court said that it was not appropriate for the State instrumentality to avoid payment of admitted amount and compel the

234. *Bombay Motor Stores v Union of India*, (2000) 1 BLJR 23 (Pat).

235. *Geep Batteries (P) India Ltd v Gillette India Ltd*, (2005) 120 DLT 387.

236. *Howrah Motor Co Ltd v Bharat Petroleum Corp*, (2000) 3 BLJR 1854 (Pat).

237. *OJSC Corpn Transstroy v Govt of Karnataka*, AIR 2005 Kant 351: 2005 AIR Kant 1492.

238. *U.P. State Bridge Construction Corpn Ltd v Bangalore Development Authority*, AIR 2005 NOC 421 (Kant): (2005) 5 Kant LJ 112.

contractor to pursue the conventional and cumbersome alternative remedy. Directions for payment could be issued in writ jurisdiction.<sup>239</sup> On the completion of a Government contract, the Government becomes liable for payment of the amount accrued to the contractor. He gets a legal right to invoke the jurisdiction of the writ court praying for mandamus for direction to the Government to make payment of the admitted outstandings.<sup>240</sup>

### Withdrawal of letter of intent and writ remedy

A letter of intent was issued in favour of the petitioner for granting him a retail outlet for sale of petroleum products. The letter was subsequently withdrawn without assigning any reasons. This was held to fall foul of Article 14 of the Constitution. The court said that in appropriate cases it could interfere in contract matters in the exercise of writ jurisdiction. The respondent was directed to restore the letter of intent and take further steps in accordance with the law and prescribed procedure.<sup>241</sup>

### Waiver and writ remedy

Waiver of credit guarantee commission charges, rebate and concessional rates of interest were held to be a part of the terms of loan. They were contractual matters between the parties. Any dispute as to such matters could be resolved through a civil suit and not under writ jurisdiction.<sup>242</sup>

### Non-performance of Government contract by contractor and writ

A foreign company contracting with the Government failed to complete the road building projects within the stipulated periods. Sufficient time and opportunities were afforded to the company to amend defaults. But it could not do so. Termination of the contract by the Government in accordance with contract stipulations was held to be justified in public interest. There was no violation of Article 14 and no occasion for issuing a writ.<sup>243</sup>

### Impact of inflation on damages

In *Doyle v Nichols*<sup>244</sup> the court took into account the likely impact of inflation while awarding damages to the widow of a doctor in respect of his death in a road accident. The House of Lords had expressed the opinion in an earlier case<sup>245</sup> that if there was a firm basis for the conclusion that the awardee would be affected by future inflation, the court should take it

239. *Satish Chandra v State of U.P.*, AIR 2006 NOC 529 (All): (2006) 2 All LJ 122 (DB).

240. *Damudhar Prasad Verma v State of Arunachal Pradesh*, (2003) 2 BC 351 (Gau).

241. *Alok Prasad Verma v Union of India*, (2000) 3 BLJR 1913 (Pat).

242. *Devi Prasad Steels (P) Ltd v A.P. State Financial Corpn*, (1999) 1 BC 497 (AP); *National Textile Corpn Ltd v Haribox Swalram*, (2004) 9 SCC 786: (2004) 3 BC 494: (2004) 4 SLT 487, contractual duty is not a statutory duty, no writ jurisdiction.

243. *OJSC Transstroy v Govt of Karnataka*, AIR 2005 Kant 351: 2005 AIR Kant 1492.

244. 1979 JBL 62. *The Times*, May 20, 1978.

245. *Taylor v O'Connor*, 1971 AC 115.

into account as best as it could. In this case the victim of the accident was a salaried employee. His salary would have naturally increased according to the rate of inflation. His dependents would suffer obvious injustice if their dependency figure was not increased accordingly.

In the case of the sale of a flat, long period of time running up to 20 years elapsed before relief could be obtained. Taking the calculation from the date of breach, the real estate valuation had increased manifold times. Damages were accordingly awarded with interest at the rate of 15 per cent per annum from the time of breach till date.<sup>246</sup>

#### Duty to mitigate [S. 73 (Explanation)]

The explanation attached to Section 73 provides for the duty to mitigate damages. It says:

In estimating the loss or damage arising from a breach of contract, the means which existed of remedying the inconvenience caused by the non-performance of the contract must be taken into account. The injured party has to make reasonable efforts to avoid the losses resulting from the breach so that his loss is kept to the minimum. The most frequent application of this rule takes place in contracts for sale or purchase of goods. On the buyer's refusal to take delivery, the seller should resell the goods at the prevailing market price and he may then recover from the defaulting buyer as damages the difference between the price he realised and the price he would have received under the contract.<sup>247</sup> If the seller does not resell the goods and his loss is aggravated by the falling market, he cannot recover the enhanced loss. The well-known authority for this proposition is the decision of the Privy Council in *A.K.A.S. Jamal v Moolla Dawood Sons & Co.*<sup>248</sup>

The plaintiff contracted to sell to the defendants 23,500 shares to be delivered and paid for on December 30, 1911. The shares were tendered on this date, but the defendants declined to take delivery or to pay for them. At the market price for sales upon that day, the shares would have realised Rs 1,09,218 less than their price under the contract. But the plaintiff sold the shares only after February when the market was again rising and he realised only Rs 79,862 less than the price under the contract. The defendants contended that they should be held liable to pay the loss of only Rs 79,862. But he was held liable for Rs 1,09,218. Lord WRENBURY explained the principles of law thus: It is undoubted law that a plaintiff who sues for damages owes the duty of taking all reasonable steps to mitigate the loss subsequent upon the breach and cannot claim as damages any sum which is due to his own neglect. But the loss to be ascertained

246. *Mohan Lal Abuja v Tarun Chandra*, (2009) 107 DRJ 342 (Del).

247. *P.S.N.S. Ambalavanan Chettiar v Express Newspapers Ltd*, AIR 1968 SC 741: (1968) 2 SCR 239.

248. (1915-16) 43 IA 6 at pp. 10-11: ILR (1916) 43 Cal 493.

is the loss *at the date of the breach*. If at that date the plaintiff could do something or did something which mitigated the damage, the defendant is entitled to the benefit of it.<sup>249</sup> If the seller retains the shares after the breach he cannot recover from the buyer any further loss if the market falls, nor is he liable to have the damages reduced if the market rises.

Where goods were sold 4½ months after breach in a crashing market, that was held to be not reasonable and F.C.I. was allowed to recover only nominal damages. Forfeiture of the earnest money of Rs 1000 was considered to be sufficient.<sup>250</sup>

Similarly, where a seller refuses to perform the contract, the buyer should buy the goods if they are available from any alternative source and cannot recover any further loss that may be due to his own neglect.<sup>251</sup>

#### *Auction sales and duty of mitigation*

In the application of the duty of mitigation to sales through auction, it has been held that if the highest bidder backs out, and as compared with the bids at reauction the bid of the next higher bidder at the original auction was much greater and if the right to sell the goods to him was still held in reserve (in this case his earnest money was still not refunded) the goods should be offered to him and the difference can be recovered from the defaulting bidder. The Municipality was allowed to recover nothing in this case because instead of accepting the next higher bid, the goods were reauctioned at a very low value.<sup>252</sup>

#### *Contract of employment and duty of mitigation*

The duty of mitigation also finds application in reference to premature termination of a contract of employment. Thus, where on account of the retirement of two out of four partners, a partnership firm was ended and with it the services of the manager but the remaining two partners reconstituted the firm and offered him employment on identical terms which he refused to accept and instead brought an action for damages, it was held that he should have accepted the employment in mitigation of his loss and that he was entitled to nominal damages only.<sup>253</sup>

249. "Stainforth v Lyall, (1830) 7 Bing 169, is an illustration of this".

250. *Bismi Abdullah & Sons v FCI*, AIR 1987 Ker 56; *Gujarat SRTC v Kay Orr Bros*, AIR 2000 Guj 313, the Government purchased the requisite machinery almost one year after the failure on the part of the tenderer. The Government was allowed the difference between the rates of the tenderer whose quotation was accepted and that of the next higher tenderer.

251. See *Rodocanachi v Milburn*, (1886) LR 18 QBD 67 (CA) and *Williams Bros v Aguis*, 1914 AC 510 (HL). Cited in *A.K.A.S. Jamal v Moolla Dawood Sons & Co*, (1915-16) 43 IA 6: ILR (1916) 43 Cal 493: (1916) 1 AC 175, 11. See also *Sotiros Shipping Inc v Sameiret Solholt*, 1981 Com LR 201, a contract for sale of ship, the seller defaulted, but offered alternative ship which the buyer refused to accept, held the buyer had reasonably failed to mitigate his loss. For a general study see P.J. Davis, *Economic Stringency and Recovery of Damages*, (1982) JBL 21, where the author considers the general aspects of the duty of mitigation.

252. *A.R. Krishnamurthy v Arni Municipality*, 1983 SCC OnLine Mad 126: (1985) 98 LW 187.

253. *Brace v Calder*, (1895) 2 QB 253: (1895-99) All ER Rep 1196.

But where no alternative employment of equal standing is available to him, the ex-employer cannot ask that he should have mitigated his loss by accepting a lesser job. The Bombay High Court in *K.G. Hiranandani v Bharat Barrel & Drum Mfg Co P Ltd*<sup>254</sup> explained the real nature of the duty of mitigation. VIMAD LAL J said:

Though what the Explanation enacts is popularly called the ‘rule’ in regard to mitigation of damages, and has been so referred to even in decided cases and standard works, and though it is loosely called a “duty” to mitigate, the position really is, as our legislature has rightly stated, merely this, that what the Explanation means is not in the nature of an independent rule or duty but is merely a factor to be taken into account in assessing the damages naturally arising from the breach, for the purpose of the main part of Section 73.

The learned Judge then adopted a passage from MAYNE ON DAMAGES<sup>255</sup> to the effect that the expression is somewhat loose one, since there is no duty which is actionable or which is owed to anyone by the plaintiff, and continued to say that the proper construction of the explanation is that the means, if any, of remedying the inconvenience caused by the breach of contract are factors that go to reduce the damages that might otherwise have arisen “naturally” from the breach.

Explaining the principle relating to damages arising from breach of a contract of employment, the learned Judge held that “there is abundant authority for the proposition that in cases in which the contract of employment was for a fixed period, the normal measure of damages would be the salary for the whole of the unexpired period of service. The principle of awarding damages for a reasonable period or reasonable period of notice comes into play only when the contract of employment is not for a fixed period.” The learned Judge found support in the decision of the Supreme Court in *S.S. Shetty v Bharat Nidhi Ltd*<sup>256</sup> where BHAGWATI J delivering the judgment of the Bench observed (*obiter*) that if the contract of employment is for a specific term, the servant would be entitled to damages the amount of which would be measured, *prima facie* and subject to the rule of mitigation, by the salary of which the master has deprived him.<sup>257</sup>

254. AIR 1969 Bom 373. To the same effect, *S.M. Murray v Fenner India Ltd*, AIR 1986 Del 427, employee was not compellable to take up a lesser job, the amount of compensation was the remuneration which he would have earned.

255. 12th Edn, para 149, point 2.

256. AIR 1958 SC 12; 1958 SCR 442.

257. Where a teacher was removed by the management without hearing and litigation persisted for 20 years, the court, taking note of the possibility that the employee must have picked up some employment, awarded salary of three years considering this as an adequate compensation, *Devi Kewalram Madrani v Premier High School*, (1995) 3 Bom CR 229. *Goetz (India) Ltd v H.R. Thimappa Gowda*, AIR 2016 NOC 179 (Kar), emphasis upon duty of mitigation. Termination was because of poor working which meant misconduct. But no enquiry conducted, nor employee heard, he thus became entitled to compensation and to retain the amount already paid.

On the facts of the case, the employer contended that the dismissed employee did not make any serious effort to find an alternative employment. Referring to this the learned Judge said that the defendant cannot impose new and extraordinary duties on the aggrieved party; nor can he ask him to take up just any and every employment that may be available to him, e.g., the employee is not expected to accept an employment in a lower status, nor will he be expected to go to a different part of the country or in a different type of work. In conclusion the learned Judge said that there was no evidence to show that a job similar to that of a general manager of a factory with somewhat similar status and pay scale as well as nature of work was available at or about the time when the breach occurred.

The burden is on the defendant to show the availability of an alternative job of equal status. It is not for the plaintiff to show the absence of such opportunities. The court can take notice of the fact that jobs are not a market commodity which can be bought at convenience. WADHWA J of the Delhi High Court permitted the plaintiff to prove for the purpose of calculating his compensation any remuneration which was being paid to him in addition to the amount mentioned in the contract.<sup>258</sup>

### *Stigma compensation*

An employee of a bank, which failed, was not allowed to maintain an action against the bank for damages for loss of reputation in the financial services industry by reason of belonging to a bank of that kind, though the damage to the reputation was such that he was not able to get employment in that industry.<sup>259</sup>

It became clear from this case that an action could lie at common law under the heading "stigma damages" representing the damage done to reputation. A claim of this kind was raised in *BCCI v Ali*.<sup>260</sup> The bank had rendered a number of employees redundant. They were required to sign a form of release under which they made the bank free of all their claims against it connected with the termination of their employment. They subsequently claimed "stigma damages" arguing that their image had been tarnished because of their association with the bank and its fraudulent activities. The trial court was of the view that it could not be said that the bank was under a duty of disclosure regarding the manner in which it had conducted its business. The Court of Appeal allowed the claim. The release deed could

258. *S.M. Murray v Fenner India Ltd*, AIR 1986 Del 427. The fact that an employee becomes entitled to contributory provident fund does not change the character of the employment to this extent that he became entitled to be there till retirement by superannuation. *M.D. Rajan v I.T.C. Ltd*, (1985) 2 MLJ 372; where the removal was on grounds different from those stated in the contract, the same was not upheld and new grounds were not permitted to be added to justify the action. *Purna Chandra Bora v Commr, Assam State Housing Board*, (1991) 1 Guj LR 192.

259. *Malik v Bank of Credit and Commerce International*, 1998 AC 20: (1997) 3 WLR 95 (HL).

260. (2000) 3 All ER 51 (CA).

not apply to a state of facts of which the releaser was unaware at the time. It would be unconscionable to hold him bound to such a state of things. A commentator on this decision has expressed the following lurking fear: "If the Court of Appeal's decision is correct, then very many of these settlements could be set aside with huge repercussions throughout the industry for the finality of these settlements. Finality in the face of potential litigation is of course a cornerstone of English law in this area."<sup>261</sup>

#### *Advantage out of one's own wrong not allowed*

The rule that a person cannot be permitted to take advantage of his own wrong is a rule of construction rather than a principle of law and therefore it can be excluded by express terms of the contract. Accordingly, damages for loss of share option cannot be claimed by an employee who is wrongfully dismissed shortly before becoming entitled to exercise the option if the option scheme expressly stated that the option was to lapse if the employee ceased to be employed by the employer. The option-holder is not entitled to any compensation for loss of the option if the option-holder ceased to be employed by the company for any reason whatsoever. Furthermore, the court said that the termination of a contract of employment destroys the status or relationship between the employer and employee, although certain aspects of the contract may continue to exist, and since the option to purchase the employer company's shares depended upon the status or relationship of the employer to the employee it no longer continued in existence when the employee was dismissed.<sup>262</sup>

#### *Aggrieved party increasing loss by unreasonable conduct*

Where the aggrieved party increases his loss by unreasonable conduct, he cannot hold the defendant liable for the same. For example, in *Derbshire v Warren*<sup>263</sup> the plaintiff's car was damaged due to defendant's negligence. The plaintiff got the car repaired at a cost which was double the value of a new equally good substitute car. The Court of Appeal did not allow him to recover the difference between the insurance money and the cost of repair, but allowed the difference between the insurance money and the market value of the car. HARMAN LJ distinguished the case from *O'Grady v Westminster Scaffolding Ltd*<sup>264</sup> where the plaintiff was held entitled to the cost of repairing his car at a cost considerably exceeding its market value, because the car was unique and could not be replaced.

The duty to mitigate damages in its essence means that the court can take into account the conduct of the injured party so as to see what he

261. Duncan Sheehan, *Unconscionability and Mistake in the Court of Appeal*, 2001 JBL 107.

262. *Micklefield v S.A.C. Technology Ltd*, (1990) 1 WLR 1002. The tort doctrine of contributory negligence is not applicable to the breach of a contractual duty which is of strict nature. *Barclays Bank Plc v Fairclough Building Ltd*, 1995 QB 214: (1994) 3 WLR 1057 (CA).

263. (1963) 1 WLR 1067 (CA).

264. (1962) 2 Lloyd's Rep 238.

ought in reason to have done, whereby his loss has been or would have been, diminished.<sup>265</sup> The substance of the rule was also indicated by the House of Lords in *British Westinghouse Electric & Mfg Co v Underground Electric Railway Co of London*,<sup>266</sup> where Lord HALDANE said:

The fundamental basis thus is compensation for pecuniary loss naturally flowing from the breach; but this first principle is qualified by a second, which imposes on a plaintiff the duty of taking all reasonable steps to mitigate the loss consequent on the breach, and debars him from claiming any part of the damage which is due to his neglect to take such steps.

Where a five star hotel accommodation was booked six months in advance to suit personal and family needs and though on account of heavy booking and rush the hotel was not able to provide the accommodation, they did arrange an alternative accommodation which the guest rejected, she was given refund of the whole money she had paid and was not allowed to recover anything more.<sup>267</sup>

Thus, what matters is the reasonableness of the conduct of the injured party.<sup>268</sup> A characteristic illustration is *Payzu Ltd v Saundars*.<sup>269</sup>

In a contract of sale of goods, delivery was to be in instalments over a period of nine months and payment was to be made within one month of delivery. The buyer failed to pay for the first instalment within the stated time. The seller refused to deliver any further instalments but offered to do so if cash was paid against each delivery.

The buyer sued him for breach of contract claiming as damages the difference between the contract and market prices. The seller contended that if the buyer had accepted their proposal of deliveries against cash, their loss would have been less. The question, therefore, was what a prudent person ought to have done in the circumstances. The court laid down that the buyer should have considered the proposal. "The plaintiffs were in fact in a position to pay cash for the goods, but, instead of accepting the defendant's offer, which

265. As stated by COCKBURN CJ in *Frost v Knight*, (1872) LR 7 Exch 111: 41 LJ Ex 78. The duty of mitigation does not cast any obligation on the plaintiff to prove that he had no means of remedying or mitigating the loss suffered. *Sagarmull Agarwalla v Union of India*, AIR 1980 Sikk 22, where an auction-purchaser refused to take the goods and they were reauctioned at a lesser price, the seller was entitled to recover the difference, the duty of mitigation does not stand in the way. *M. Lachia Setty & Sons Ltd v Coffee Board*, (1980) 4 SCC 636: AIR 1981 SC 162.

266. 1912 AC 673, 687.

267. *Toubi v Inatsun Holidays*, 1988 CLY 423, 1060. In another case the accommodation was provided but with lesser facilities than represented and £750 for diminution in value of holiday, £1000 for general inconvenience and disappointment and interest at 12 per cent allowed. *Jones and Jones v Villa Ramos*, 1988 CLY 1061.

268. *Le Blanche v L&N W Rly Co*, (1876) LR 1 CPD 286, 309, 313. *Santosh Kumar Chopda v State of M.P.*, (2003) 1 MPHT 343, auction of right to collect tendu leaves, the bidder could not pay after depositing earnest money, long delay in reauctioning, leaves allowed to whither away, the bidder held not liable for shortfall on reauction because of unreasonableness of conduct, forfeiture of earnest money held to be fully justified.

269. (1919) 2 KB 581.

was made perfectly *bona fide*, the plaintiffs permitted themselves to sustain a larger measure of loss which as prudent and reasonable people they ought to have avoided."

### *Transactions concerning property*

This result would not follow everywhere. Suppose that a buyer agrees to buy property having a certain quality and the seller delivers property without that quality. There is a difference between the market value of the property with that quality and without it. The buyer is clearly entitled to recover the difference between the two values. Suppose further that the seller in response to the buyer's notice proposes to buy back the property and refund the price, but the buyer refuses. Does he lose the right to recover the difference between the two values? The Court of Appeal answered in *Strutt v Whitnell*<sup>270</sup> where facts of this kind were involved, that the buyer would be entitled to retain the property and to recover the difference between the values. The seller cannot compel him to forgo his right to substantial damages as the price of retaining what has become his own property. The seller cannot say that the buyer had no good reason for refusing to accept his offer to buy back the property. "The buyer is entitled to retain his property without any investigation of his reasons for wishing to do so and that his right to recover the difference between the two values is not contingent on his having acted reasonably in the matter of the seller's offer to repurchase."

In such cases the option is with the buyer either to retain the goods and recover the difference or to return the goods against refund of price and then sue for damages for breach, if any. The seller cannot impose the choice of the option upon the buyer. The court distinguished this case from the decision in the *Payzu* case<sup>271</sup> where the goods had not been delivered in breach of the contract and were offered on different terms.

Section 73 is universally applicable to property transactions also. There is no other special provision about such transactions. In England, however, it was held by the House of Lords in the early case of *Bain v Fothergill*<sup>272</sup> that a purchaser of real estate cannot recover damages for the loss of his bargain. He is entitled to refund of his deposit and to the recovery of his expenses. The vendor, who was deceiving him may be sued for the tort of deceit for the consequences of deception in not providing good title or in making a promise without the intention of performing it. In India, on the other hand, it has

270. (1975) 1 WLR 870 (CA).

271. *Payzu Ltd v Saundars*, (1919) 2 KB 581.

272. (1874) LR 7 HL 158. The Karnataka High Court held in *Happy Home Builders (P) Ltd v Delite Enterprises*, (1995) 2 AIHC 1320 that in a transaction for sale of immovable property which fails to go through, unless there is evidence of loss to the prospective purchaser, he is not entitled to damages but only to refund of advance paid with interest. The doctrine of *status quo ante* becomes applicable. As against an advance of Rs 15,000 for purchase of property which the seller failed to perform, Rs 2000 per year were allowed as compensation for deprivation of money, *Sardar Mohar Singh v Mangilal*, (1997) 9 SCC 217: AIR 1995 SC 491.

been judicially observed that “the legislature has not prescribed a different measure of damages in the case of contracts dealing with land from that laid down in the case of contracts relating to commodities”.<sup>273</sup> So a frustrated purchaser of immovable property in India is entitled to damages equal to the amount of loss arising naturally in the usual course of things from the breach itself subject, of course, to the duty of mitigation.<sup>274</sup> The court said: “As Section 73 imposes no exception on the ordinary law as to damages, whatever be the subject-matter of the contract, it seems that in cases of breach of contract for sale of immovable property through inability on the vendor's part to make a good title the damages must be assessed in the usual way, unless it can be shown that the parties to the contract expressly or impliedly contracted that this should not render the vendor liable in damages.” Some other High Courts have expressed similar views.<sup>275</sup> Accordingly, where the vendor guaranteed a good title but even so the vendee was evicted, the latter was allowed to recover the value of the land at the date of eviction and not merely refund of price.<sup>276</sup>

The contract was for the provision of premises of certain nature which were prepared for a special purpose on lease for a minimum period of three years. The lessee returned the premises earlier. The court allowed lease money to be recovered for the full period of three years irrespective of the fact that no lease deed was executed.<sup>277</sup> Where the sale of property fell through because of the lack of title on the part of the seller, it was held in a suit for damages that the fact that the buyer had enjoyed the entire property for some period and also received rents, had to be taken into account while computing damages. The buyer had claimed refund of half the consideration paid by him. The same was allowed to him.<sup>278</sup>

#### *Negligent valuation*

The plaintiffs lost a huge sum of money because they happened to allow loans to purchasers of commercial property on the basis of valuation report given by the defendant. The valuation was negligently done. The loss became aggravated because of the collapse of the property market. The Court of

273. *Nagardas v Ahmedkhan*, ILR (1895) 21 Bom 175, FARRAN CJ at p. 185, contrary to the earlier observation of the same court in *Pitambar v Cassibai*, ILR (1886) 11 Bom 272.

274. This view was approved by the Bombay HC in *Ranchhod v Manmohandas*, ILR (1907) 32 Bom 165 where the court expressed the opinion that *Bain v Forthergill*, (1874) LR 7 HLC 158 was not applicable in India.

275. *Nabinchandra Saha Paramanick v Krishna Barana Dasi*, ILR (1911) 38 Cal 458; *Jai Kishen Das v Arya Priti Nidhi Sabha*, ILR (1920) 1 Lah 380; *Mangal Singh v Dial Chand*, AIR 1940 Lah 159; *Adikasavan Naidu v Gurunath Chetti*, ILR (1918) 40 Mad 338.

276. *Nagardas v Ahmedkhan*, ILR (1895) 21 Bom 175. *Kolimi Pedda Samas Hussain Saheb v Gowdara Rajasekhara Gowd*, AIR 2006 NOC 511 (AP), property sold to plaintiff with defective title, he was dispossessed, allowed damages assessed at market value on the date of dispossession and not on the date execution of sale deed. The vendor had categorically agreed to indemnify the vendee in case of any dispute as to title.

277. *Food Corporation of India v Babulal Agrawal*, (2004) 2 SCC 712: AIR 2004 SC 2926.

278. *Ram Autar v Ram Prasad*, (2004) 3 All LJ 3925.

Appeal allowed recovery of the whole amount lost. The court said that once it is established "that the valuer's negligence led the lender to make a loan, he would not otherwise have made it seems to us that the lender is entitled to be compensated for all the damage he has suffered. If the market moves upwards, the valuer reaps the benefit; if it moves downwards, he stands to lose."<sup>279</sup>

#### *Aggrieved party not to be inflicted with unusual burdens*

The duty of mitigation cannot impose upon the plaintiff burdens of unusual nature. There was a transfer of a part of a plot of land, the transferee undertaking to erect a boundary wall, which wall would have increased the value of the seller's remaining land. The buyer failed to erect the wall. In an action against him, the measure of damages would have been the cost of constructing the wall. He contended that if the wall had been constructed by the plaintiff as soon as there was the breach, the cost would have been much less; the plaintiff waited till the decision in the case and, in the meantime, inflation had escalated the cost. The defendant contended that he should not be held liable for the increased cost. The court felt that it was reasonable for the plaintiff to wait as long as his right to damages was disputed and there was no injustice to the defendant if the result of inflation was to increase the pecuniary amount of his ultimate liability.<sup>280</sup>

#### *Reluctance of courts to expand scope of duty of mitigation*

Thus courts have shown a great reluctance in expanding the dimensions of the duty of mitigation.

The distributor of a dress manufacturer agreed to purchase a given number of garments in two seasons. He had complete freedom to choose garments of any variety and to resell them in his area at any price. The distributor repudiated the contract. He was sued for breach. He argued that he should be called upon to pay damages for manufacturer's loss of profits on their cheapest garments, because he had the freedom to choose any garments.

The court said that since it could not have been in the contemplation of the parties that the distributor would stock only the minimum priced garments, which would have been destructive of their market, damages must be computed on the basis of a reasonable criterion which should also be the least unfavourable to the distributor.<sup>281</sup>

279. *Banque Bruxelles Lambert SA v Eagle Star Insurance Co Ltd*, 1995 QB 375: (1995) 2 WLR 607 (CA).

280. *Radford v De Froberville*, (1977) 1 WLR 1262.

281. *Paula Lee Ltd v Robert Zabil & Co Ltd*, (1983) 2 All ER 390 (QB). A contractor whose application for extension of time was disposed of after some time was not allowed to claim any compensation on the ground that if his application had been disposed of earlier, he would have earned something elsewhere, *Devender Singh v State of U.P.*, AIR 1987 All 306.

### *Contributory negligence*

In contract claims the duty to keep one's loss to the minimum is capable of taking care of the matter where the loss is either caused or increased by the claimant's contributory negligence. But where the defendant's liability in contract is the same as his liability in the tort of negligence, independent of the existence of any contract, the court has power to apportion blame and to reduce the damages recoverable by the plaintiff even though the claim is made in contract. This approach was adopted in a principal's action against his agent for breach of agent's duty in circumstances in which the principal failed to rectify the matters during the subsequent opportunities available to him.<sup>282</sup> The defence of contributory negligence is not available as against a claim for damages which is founded on a strictly contractual obligation. A contractor was engaged for cleaning of roofs made of corrugated asbestos sheets. He did not properly control the asbestos discharge. The refuse contaminated the premises necessitating extensive remedial works. As against the owners' action for damages, the contractor contended that the owners were also negligent because their architectural department did not provide proper supervision of the work. The court found that the owners' claim was only in contract being based on a breach of two contractual terms. The defence of contributory negligence would not apply to such a claim.<sup>283</sup>

### *Arbitrator's award*

The contract was for supply of batteries to a count of more than 15 lakhs. The suppliers guaranteed the performance and life of each battery. But the batteries did not work up to the guaranteed period. The arbitrator passed an award reducing the price proportionately on the basis of a representative sample pre-estimating the loss in the light of the formula stipulated in the contract clause. The court held the award to be proper.<sup>284</sup>

### *Recovery of damages as arrears of land revenue*

The Supreme Court has upheld the validity of a clause in a Government contract which authorised the State to recover damages as arrears of land revenue.<sup>285</sup> Where there was no such clause recovery of dues under a contract by way of arrears of land revenue was not allowed.<sup>286</sup>

282. *Forsikringsaktieselskapet Vesta v Butcher*, 1989 AC 852 (CA). The court adopted the ruling in *Rowe v Turner Hopkins & Partners*, (1980) 2 NZ LR 550, but did not follow *A.B. Marintrans v Comet Shipping Co Ltd*, (1985) 1 WLR 170.

283. *Barclays Bank Plc v Fairclough Building Ltd*, 1995 QB 214: (1994) 3 WLR 1057 (CA).

284. *Geep Industrial Syndicate Ltd v Union of India*, AIR 2002 NOC 180 (Del): 2002 AIHC 2201.

285. *State of Karnataka v Shree Rameshwara Rice Mills*, (1987) 2 SCC 160: AIR 1987 SC 1359.

286. *Mohd Umar v Nagar Palika, Khatima*, AIR 1998 All 227.

### Exclusion of Section 73: Arbitration clause

Whether in the context of terms and conditions of a contract it is permissible to provide that Section 73 would not apply and the special terms of the contract should be applied for making out recoverable loss, the court said that it depends upon the appreciation of the facts of the case and if the arbitrator had followed the special provision, no fault in his award could be found for that reason alone.<sup>287</sup>

### LIQUIDATED DAMAGES AND PENALTY [S. 74]

#### English Law

The parties to a contract may determine beforehand the amount of compensation payable in the event of breach. According to English law a sum so fixed may fall in any of the following two categories:

- (1) Liquidated damages, or
- (2) Penalty.

If the sum fixed represents a genuine pre-estimate of the probable damage that is likely to result from the breach, it is liquidated damages. A sum less than the amount of probable damage is also regarded as liquidated damages. The whole of such sum is recoverable.<sup>288</sup> A well-known illustration is *Dunlop Pneumatic Tyre Co Ltd v New Garage & Motor Co Ltd*.<sup>289</sup>

A manufacturer of tyres supplied a quantity of tyres to a dealer on the condition that they would not be sold below the list prices and that liquidated damages, not penalty, of £5 would be payable for every tyre sold in breach of the agreement. The dealer committed breach. The question was whether the above sum was intended as a genuine compensation for the loss suffered.

The House of Lords held it to be liquidated damages. Lord DUNEDIN stated the effect of cases in the following propositions:

- (1) The expression used by the parties is not conclusive. The court must find out whether the payment stipulated is in truth a penalty or liquidated damages.
- (2) The essence of a penalty is a payment of money stipulated as *in terrorem* of the offending party; the essence of liquidated damages is a genuine covenanted pre-estimate of damage.<sup>290</sup>
- (3) The question whether a sum stipulated is penalty or liquidated damages is a question of construction to be decided upon the terms and inherent circumstances of each particular contract.<sup>291</sup>

287. *Maharashtra SEB v Sterlite Industries (India)*, (2001) 8 SCC 482: (2002) 1 Bom CR 415.

288. See *Cellulose Acetate Silk Co Ltd v Widness Foundry (1925) Ltd*, 1933 AC 20 (HL).

289. *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd*, 1915 AC 79 (HL).

290. *Clydebank Engg & Shipbuilding Co Ltd v Don Jose Ramos Yzquierdo Castaneda*, 1905 AC 6.

291. *Public Works Commr v Hills*, 1906 AC 368; *Webster v Bosanquet*, 1912 AC 394 (PC).

- (4) To assist this task, various tests have been suggested:
- (a) It will be held to be penalty if the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach.<sup>292</sup>
  - (b) It will be a penalty if the breach consists only in not paying a sum of money and the sum stipulated is a sum greater than the sum which ought to have been paid.<sup>293</sup>
  - (c) There is a presumption (but no more) that it is penalty, when “a single lump sum is made payable by way of compensation, on the occurrence of one or more or all of several events, some of which may occasion a serious and others but trifling damage”.<sup>294</sup>

#### Court's power to reduce specified amount

If the sum fixed by the parties is found to be liquidated damages, the whole of it is recoverable. But if it is viewed as “penalty”, it is rejected. Damages will then be calculated according to the ordinary principles. In doing so the following “salutary warning” of DIPLOCK LJ should be kept in mind:<sup>295</sup>

The court should not be astute to descry a penalty clause in every provision of a contract which stipulates a sum to be payable by one party to the other in the event of a breach by the former.

To this Cheshire and Fifoot add:<sup>296</sup>

Such a stipulation reflects good business sense and is advantageous to both parties. It enables them to envisage the financial consequence of a breach; and if litigation proves inevitable, it avoids the difficulty and legal costs, often heavy, of proving what loss has in fact been suffered by the innocent party.

An illustration of “penalty” is *Ford Motor Co v Armstrong*.<sup>297</sup>

The defendant, a retailer, received from the plaintiffs, supplies of cars and parts and agreed not to sell any item below the listed price. A sum of £250 was payable for every breach as “agreed damages”.

292. Illustration given by Lord HALSBURY in *Clydebank case*, 1905 AC 6.

293. *Kemble v Farren*, (1829) 6 Bing 141 and JESSEL MR in *Wallis v Smith*, (1882) LR 21 Ch D 243 (CA).

294. Lord WATSON in *Elphinstone v Monkland Iron & Coal Co*, (1886) LR 11 AC 332 (HL). Following these propositions the Singapore CA held in *Golden Bay Realty Pte Ltd v Orchard Twelve Investments Pte Ltd*, (1989) 2 MLJ 70 (Malaysia), that liquidated damages rate specified in the agreement of 9 per cent per annum over 85 per cent of the purchase price of property could not be said to be an extravagant or unconscionable amount.

295. *Robophone Facilities Ltd v Blank*, (1966) 1 WLR 1428, 1447 (CA).

296. LAW OF CONTRACT (9th Edn by FURMSTON, 1976) 611.

297. (1915) 31 TLR 267 (CA).

A breach having taken place, a majority of the Court of Appeal held that the sum fixed was a penalty as it might happen that a part sold in breach was of lesser value than the damages payable.

### Application to hire-purchase contracts

Another illustration of penalty is *Lamdon Trust Ltd v Hurrel*.<sup>298</sup>

A car was purchased on hire-purchase terms, the total price payable by instalments being £ 558. The agreement provided that if the purchaser returned the car or if, on account of his default the seller retook it, the total sum, including the instalments already paid, of £425 must be paid. The purchaser paid up to £ 302 and then defaulted. The seller retook and resold it for £270, thus receiving a total sum of £ 572, which was more than the contract price. Even so he brought an action to recover £ 122, being the difference between £425 and the instalments paid.

But his claim failed. The court rejected the sum as being a penalty and not a genuine pre-estimate of the probable damage. In arriving at this conclusion DENNING LJ took into account these circumstances: "The £425 is three quarters of the total price. It is inserted by the hire-purchase companies by rule of thumb without regard to the make of car, its age, the market conditions or anything of the kind. It is the same for all." In addition to the liability to pay £425, the purchaser was to keep the car in good order, repair and condition and was to pay independent damages for any breach of this condition, supposing that the car was taken back within a month, could anyone think that the hire or depreciation would go up to £425. "In these circumstances", his Lordship concluded, "I cannot regard the figure of three-quarters as a genuine pre-estimate of damage. If the parties had genuinely tried to estimate the depreciation of this particular car, the figure would have been much less."

In India also hire-purchase agreements are not immune from the applicability of Section 74. They are also to be tested on the same anvil. In this case<sup>299</sup> interest at the rate of 18 per cent p.a. was added to the principal sum in advance. There was a further stipulation to pay compensation at the rate of 2½ per cent p.m. on the amount of hire-purchase in arrears. The total rate came up to 30 per cent p.a. on an amount which already included 18 per cent p.a. This was held to be excessive. Following the decision of the Supreme Court in *K.P. Subbarama Sastri v K.S. Raghavan*<sup>300</sup> the court said:

"A weak cannot be pushed to the wall because of the inequality of bargaining power. He cannot be held bound by terms in fine print which are unduly onerous, oppressive and unreasonable."

298. (1955) 1 WLR 391; *Sub nom. Lamdon Trust Ltd v Hurrel*, (1955) 1 WLR 391.

299. *Pushpendra Motilal Singh v Commercial Automobiles*, (1999) 2 MPLJ 319 at p. 324.

300. (1987) 2 SCC 424: AIR 1987 SC 1257.

### Heavy amount as evidence of penalty

The House of Lords in their decision in *Bridge v Cambell Discount Co Ltd*<sup>301</sup> carried this principle further still by holding that where two-third of the price is made payable in the event of a default, that should be viewed as a "penalty". The Court of Appeal pointed out in a subsequent case,<sup>302</sup> that where a hire-purchase agreement which, in the event of default, provides for the payment of the full amount or a fixed amount whether the default takes place in the beginning or towards the end of the period of agreement, is bound to be regarded as a penalty. Similarly, where the sum of money payable being very small and the agreement provides that in the event of default a large sum would become payable, that is obviously a penalty. In an old case:<sup>303</sup>

The defendant, an artiste, engaged himself to act as a principal comedian at a theatre for a fixed period on a charge of about three and a half pounds per night. The agreement provided that in the event of default by either party a sum of £1000 was payable. This was described in the agreement as liquidated and ascertained damages.

But even so the court held this to be a penalty. Its effect was that a failure to pay a small sum of £3½ or for any other minor default, a sum of £1000 would become payable. The amount thus bore no relation with the degree or extent of breach.

### Fixed figure constitutes ceiling

Where the figure of compensation assessed by the parties carries some sense, whether it is reasonable or not, it will constitute the ceiling, and nothing more than that would be recoverable. In a case before the House of Lords:<sup>304</sup>

A contract for the delivery and erection of a certain machinery provided that the contractor would have to pay £20 as penalty for each day of default. The contractor delayed the completion of the work by thirty weeks. According to the contract his liability was £600, but the purchasers claimed £5850 being the actual loss suffered by them by reason of the delay.

They were held entitled to claim only £600. Lord ATKIN, pointing out that the court was not bound by the terminology used by the parties, said:

301. 1962 AC 600: (1962) 2 WLR 439. *Sahdeo Mistry v Jharkhand State Housing Board*, (2003) 3 BC 506 (Jhar), a house allottee was not allowed to be subjected to exorbitant charges for his default in keeping up instalments, only interest for the period of default was allowed to be charged.

302. *Anglo-Auto Finance Co Ltd v James*, (1963) 1 WLR 1942 (CA).

303. *Kemble v Farren*, (1829) 6 Bing 141, the Court of Chancery.

304. *Cellulose Acetate Silk Co Ltd v Widness Foundry (1925) Ltd*, 1933 AC 20 (HL).

Except that it is called a penalty, which on the cases is far from conclusive, it appears to be an amount of compensation measured by the period of delay, I agree that it is not a pre-estimate of actual damage. I think it must have been obvious to both the parties that the actual damage would be much more than £20 a week; but it was intended to go towards the damage and it was all that the sellers were prepared to pay.<sup>305</sup>

### **Stipulation for payment on events extraneous to breach of contract**

A contract providing for payment of money by one party on the occurrence of a specified event, rather than on the breach of a contractual duty owed by that party, cannot be a penalty. A person who guaranteed the payment of promissory notes issued by a contractor against which loans were provided, could not avoid his liability by showing that the amount covered by the promissory notes would have amounted to a penalty.<sup>306</sup>

### **Applicable whether stipulation is for payment in cash or kind**

There is no difference between a penalty for non-payment of money due under a contract and a penalty for the non-performance of some other obligation and, furthermore, there is no distinction between a penalty which requires the payment of money and a penalty which requires the transfer of property. This observation occurs in a case<sup>307</sup> in which a clause in a sale agreement required the purchaser to transfer the shares back to the vendor for fixed sum if he defaulted in payment of instalments. The sum fixed for transfer back did not reflect the true value of the shares. The purchaser defaulted in payment of instalments and wanted to escape the rigour of the transaction by saying that it amounted to a penalty. The court said that the clause would not permit recovery of anything more than the plaintiffs actual loss.

### **Conditions of membership**

A rule of an association as a condition of membership and as a matter of policy provided that members should share equally in the benefits and burdens of the association and that someone who declined the burden should not participate in the benefit. The court said that a rule of this kind was not

305. See McGregor, *Compensation v Punishment in Damages Awards*, (1965) 27 All Mah LR 629; Hodgin and Veitch, (1965) 27 MLR 629; Hodgin and Veitch, *Punitive Damages, re-assessed*, (1972) 12 ICLQ 119; Benjamin, *Penalties, Liquidated Damages and Penal Clauses in Commercial Contracts*, (1960) 9 ICLQ 600. This is so under S. 74 also. The section contains the words not exceeding the amount named by the parties. *Nait Ram v Shih Dat*, ILR (1882) 5 All 238. Where the amount so named is more than reasonable, it would be reduced to a reasonable amount. *Abbakke Heggadthi v Kinbiamma Shetty*, ILR (1906) 29 Mad 491. Where the amount specified is in terms of "not less than" it would still be subject to the court's discretion to reduce it to a reasonable amount. *Chunilal V. Mehta and Sons Ltd v Century Spg & Mfg Co Ltd*, AIR 1962 SC 1314.

306. *Export Credit Guarantee Deptt v Universal Oil Products Co*, (1983) 1 WLR 399 (HL).

307. *Jobson v Johnson*, (1989) 1 WLR 1026 (CA).

in the nature of a penalty clause. The clause required the members under a resolution of the company to make additional subscription and provided that if a member failed to do so, he would be precluded from sharing the benefits of any recovery that the association might make. This was held to be not a penalty clause.<sup>308</sup>

### Section 74, Contract Act

Section 74 of the Indian Contract Act lays down a slightly different rule:

**S. 74. Compensation for breach of contract where penalty stipulated for.**—<sup>309</sup>[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.]

*Explanation.*—A stipulation for increased interest from the date of default may be a stipulation by way of penalty.]

*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 <sup>310</sup>[Central Government] or of any <sup>311</sup>[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.

*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.

#### *Illustrations*

- (a) A contracts with B to pay B Rs 1000, if he fails to pay B Rs 500 on a given day. A fails to pay B Rs 500 on that day. B is entitled to recover from A such compensation not exceeding Rs 1000 as the Court considers reasonable.
- (b) A contracts with B that, if A practises as a surgeon within Calcutta, he will pay B Rs 5000. A practises as a surgeon in Calcutta. B is entitled to such compensation, not exceeding Rs 5000, as the Court considers reasonable.
- (c) A gives a recognizance binding him in a penalty of Rs 500 to appear in Court on a certain day. He forfeits his recognizance. He is liable to pay the whole penalty.

<sup>312</sup>[(d) A gives B a bond for the repayment of Rs 1000 with interest at 12 per cent at the end of six months, with a stipulation that, in case of default, interest shall be payable at the rate of 75 per cent from the date of default. This is a stipulation by way of penalty,

308. *Nutting v Baldwin*, (1995) 1 WLR 201.

309. These paragraphs were substituted for the first paragraph of S. 74 by S. 4 of the Indian Contract (Amendment) Act, 1899 (VI of 1899).

310: These words were *substituted* for the "Government of India" by the Government of India (Adaptation of Indian Laws) Order, 1937.

311. *Subs.* by the A.O. 1950 for "Provincial Government".

312. Illustrations (d) to (g) *added* by S. 4 of the Indian Contract (Amendment) Act, 1899.

and *B* is only entitled to recover from *A* such compensation as the Court considers reasonable.

- (e) *A*, who owes money to *B*, a money-lender, undertakes to repay him by delivering to him 10 maunds of grain on a certain date, and stipulates that, in the event of his not delivering the stipulated amount by the stipulated date, he shall be liable to deliver 20 maunds. This is a stipulation by way of penalty and *B* is only entitled to reasonable compensation in case of breach.
- (f) *A* undertakes to repay *B* a loan of Rs 1000 by five equal monthly instalments, with a stipulation that, in default of any instalment, the whole shall become due. This stipulation is not by way of penalty, and the contract may be enforced according to its terms.
- (g) *A* borrows Rs 100 from *B* and gives him a bond for Rs 200 payable by five yearly instalments of Rs 40, with a stipulation that, in default of payment of any instalment, the whole shall become due. This is a stipulation by way of penalty.]<sup>313</sup>

### Rule stated in Section 74

The rule is that where a sum is named in a contract as the amount to be paid in case of breach, regardless whether it is a penalty or not, the party suffering from breach is entitled to receive reasonable compensation not exceeding the amount so named. The named sum constitutes the maximum limit of liability. The court cannot order damages beyond that. "The distinction [between liquidated damages and penalty] has been abolished in India. The courts award reasonable compensation not exceeding the stipulation. The courts knock down agreements which are unconscionable and extravagant."<sup>314</sup> The court has the latitude to reduce the amount to what appears to be reasonable in the circumstances.<sup>315</sup>

313. *Custodian v East West Travel and Trade Links Ltd*, (1995) 4 Bom CR 194 compound interest which amounted to penalty, but the court said that the conduct of the party in delaying payment and suppressing the liability to pay was such that no sympathy could be shown and the stipulated interest was recoverable. *H.P. Fruit Growers' Coop Mark Processing Society Ltd v H.P. Housing Board*, AIR 1996 HP 94, lease, lease instalments included interest rates, on default double rate payable over and above that already included, held penalty, it could at most be simple interest at normal rates.

314. *Pushpendra Motilal Singh v Commercial Automobiles*, (1999) 2 MPLJ 319 at p. 324. *Carl Estate (P) Ltd v Jagdish J.N. Counte*, (2005) 4 Bom CR 630, for failure to refund earnest money, the stipulation was that the defendant was to pay Rs 1000 as daily fine after expiry of 30 days' notice in addition to compound interest at 4 per cent. The stipulation was held to be penal in nature and so not enforceable. Only 10 per cent was allowed on the amount.

315. Hence, the right is the right to sue for the breach and not for the amount reserved because the court has to ascertain its reasonableness. *State of Gujarat v M.K. Patel & Co*, AIR 1985 Guj 179. Where under a term of the contract, the Government side was authorised to assess compensation for breach, it was held that the clause would apply only when there was an admitted breach. Such a clause would not enable the party so empowered to ignore the requirements of S. 74 one of which is that only a reasonable amount would be allowed. *Hameed v Jayabharat Credit and Investment Co Ltd*, AIR 1986 Ker 206. In a contract to supply hydrogen gas cylinders, the rate of Rs 1.25 per week for detention of the cylinders beyond the first three weeks' period was held to be a proper measure of damages. *Indian Drugs and Pharmaceuticals Ltd v Industrial Oxygen Co (P) Ltd*, 1984 Mah LJ 690. *A.P. SEB v V.B.C. Foods (P) Ltd*, AIR 1998 AP 177, a term in the energy supply agreement that 2 per cent per month interest would be charged on bill amounts in default was held to be reasonable within the meaning of S. 74. *Sabir Ram & Co v Rajasthan State Agricultural Marketing Board*, 1995 AIHC 358, award of full amount provided in contract for failure

Whether or not the party has proved to have suffered actual loss, is immaterial.<sup>316</sup>

This has certain advantages over the English system. The section dispenses with the necessity of laying down rules for distinguishing liquidated damages from penalty. Further, according to English law, the court must either accept the amount in whole or reject it in whole. In India, the court need not reject the amount. It may either accept the amount or reduce it to what appears reasonable. In the *Fateh Chand* case the Supreme Court observed as follows:<sup>317</sup> "Section 74 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. ... The Indian Legislature 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 the amount to be paid in case of breach and stipulations by way of penalty."

The amount stipulated in the contract is not decisive but it is a good attempt to avoid litigation. It is well known that assessment of compensation with precision is somewhat difficult task. The figure work provided by the parties gives a good start to overcome the difficulty of proof. In this case the court had to reduce the amount stipulated because neither that much loss was proved nor it was in the neighbourhood of probable loss.<sup>318</sup>

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of or delay in performance without assessment of loss suffered by the aggrieved party was held to be in the nature of levying a penalty. *John v Oriental Kuries Ltd.*, (1994) 2 KLT 353, provision for the whole number of instalments becoming immediately due on default, not a penalty. *M.M.T.C. Ltd v Sineximco (P) Ltd.*, (2006) 135 DLT 629, the buyer's failure in an international contract to accept delivery of goods because of a fall in prices was held to be not justified. The seller was not entitled to recover the whole amount specified in the liquidated damages clause. He is entitled only to be suitably compensated within the limits specified in the contract.

316. This section is not attracted by a penal provision in a consent decree. *Punjab Woollen Textiles Firm v Bank of India*, AIR 1992 P&H 158. For a contrary view, see *Parvati Bai v Ayodhya Prasad Jain*, 1985 MPLJ 703. But the provision is applicable to compromises, e.g. a truck driver's compromise agreement either to set right the damage done by negligent driving or to pay Rs 10,000. *C.K. Kesavam v Kudaythoor Panchayath*, (1990) 2 KLT 424. A stipulation for increased interest from the day of default may be a stipulation by way of penalty and whenever it is so, relief is to be granted under the section. The rate of interest will be allowed by way of compensation in the discretion of the court, *Pushpendra Motilal Singh v Commercial Automobiles*, (1999) 2 MPLJ 319. *Jagson International Ltd v Oil & Natural Gas Corp Ltd*, (2003) 4 Mah LJ 733; (2004) 2 Bom CR 272, the amount fixed in the contract as liquidated damages was allowed to be recovered, it seemed to have been fixed with due calculations and was also reasonable. The claimant had not to show any loss. Only the defendant to show that the claimant had suffered no loss. But that was not the case of the defendant here.

317. *Fateh Chand v Balkishan Dass*, AIR 1963 SC 1405; (1964) 1 SCR 515.

318. *Vijay Engineers & Developers v Suryadarshan Coop Housing Society Ltd*, (2011) 5 Mah LJ 610 (Bom). Similar statement are to be seen in *BSNL v Reliance Communication Ltd*, (2011) 1 SCC 394, the court emphasised the desirability of providing in commercial contracts, compensatory clauses particularly where commercial activities are subjected to regulatory regimes as in the case of telecom industry.

### One party not to be adjudicating authority

In a case before the Supreme Court<sup>319</sup> a clause in a contract was to the effect that for any breach of the conditions of the contract the first party shall be liable to pay damages to the second party as may be assessed by the second party. This clause was held to be void because it had the effect of making a party also a judge to decide breach and assess damages. The court said: "The power to assess damages is subsidiary and consequential power and not the primary power. Even assuming for argument's sake that the clause afforded scope for being construed as empowering the officer of the State to decide upon the question of breach as well as assess the quantum of damages, we do not think that adjudication by the officer regarding breach can be sustained under the law because a party to the agreement cannot be an arbiter in his own cause. Interests of justice and equity require that where a party to a contract disputes breach, adjudication should be by an independent person or body and not by the other party to the contract. The position will be different where there is no dispute or there is consensus between the parties regarding the breach of conditions. In such a case, the officer of the State even though a party to the contract will be within his rights in assessing the damages occasioned by the breach."<sup>320</sup> The cumulative effect of the decisions is that when breach is not admitted, one of the contracting parties cannot arrogate to itself the power to claim compensation for the breach from the other party without there being any adjudication by an outside agency as to whether there was any breach of contract. The State could not be a judge in its own cause or its own arbiter.<sup>321</sup>

### Breach and right to compensation must be established

The injured party has to prove that there has been a breach of contract on the part of the other party and, therefore, the remedial system provided in the contract has become exercisable. The claim in this case was for refund of amount retained by the other party as liquidated damages for breach. A decree for refund of the amount was passed without going into the question whether delay in completion of the work was caused due to lapses on the part of one party or the other or whether the guarantee had become

319. *State of Karnataka v Shree Rameshwara Rice Mills*, (1987) 2 SCC 160: AIR 1987 SC 1359.

320. *Anchor Lines (P) Ltd v Cement Corpn of India Ltd*, (2000) 4 Kant LJ 485, a party to the contract cannot be arbiter in his own cause; adjudication of disputed question of breach of contract should be by some independent person or body of persons. The party holding bank guarantee first encashed it and then gave notice to the other of the alleged breach of contract and adjustment of the guarantee amount against self-assessed damages. All this was held to be wrong.

321. *J.G. Engineers (P) Ltd v Union of India*, (2011) 5 SCC 758: AIR 2011 SC 2477, breach of contract and termination of contract based on exclusion clauses and excepted matters involving the question as to which party committed breach or delay and whether the contract was validly terminated, could be decided only by the adjudicatory forum, i.e. court or arbitral tribunal, and not by a party to the contract.

invokable. The case was sent back to the trial court for fact finding as to breach and its consequences.<sup>322</sup> The plaintiff, a Government undertaking, was dealing in export of marine products. It provided financial assistance to the defendant who was engaged in the business of sea food. A clause in the agreement provided that he would be liable to compensate the plaintiff if his goods were rejected by the foreign buyer. It was found that the goods were rejected not because of any inherent defect but because of the misfunctioning of the containers in which the goods were shipped. The plaintiff had filed a suit against the shipping agent but did not pursue it. An action against the defendant was not allowed. The plaintiff could not take shelter of the clause when there was no breach on the part of the defendant.<sup>323</sup>

The court has to make its own assessment of the amount of loss caused by the breach. It cannot blindly follow the contract clause in awarding damages without any adjudication.<sup>324</sup>

#### *Unilateral deduction from final bill not permissible*

It has been held that unilateral deductions towards liquidated damages from the contractor's final bill are not permissible. Even if there is a breach, the aggrieved party cannot offset its own work out liquidated damages and deduct the amount from the final bill. The party carrying out deduction is not free from the responsibility of showing evidence in justification of deductions. In this case, there were various facts which were denied by the contractor, that was clear from the pleadings and materials and documents on record. There was also the finding by the arbitrator that deductions were carried out on the basis of disputed facts and by attributing the delay to the contractor and this was contrary to the record.<sup>325</sup>

The contract carried a stipulation as to the amount of liquidated damages. There was delay in execution of work by the contractor. The aggrieved party became entitled to reasonable compensation but gave no evidence of the amount of loss caused. The contractor also did not show any precise amount of possible loss. The court awarded half of the amount claimed by way of reasonable compensation.<sup>326</sup>

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322. *FACT Engg Works v Kerala Industries*, AIR 2001 Ker 326.

323. *M.M.T.C. Ltd v S. Mohamed Gani*, AIR 2002 Mad 378. *SAIL v Gupta Brother Steel Tubes Ltd*, (2009) 10 SCC 63, agreement specified damages for certain types of breach of contract, the breaches alleged were of different nature, hence the clause as to liquidated damages was not to apply.

324. *Uma Minerals v Malabar Cements Ltd*, AIR 2003 Ker 146. *Chennai Metropolitan Water Supply & Sewerage Board v Aban Constructions (P) Ltd*, (2006) 3 CTC 794 (Mad), contract clauses clearly provided a formula for pre-estimation of damages in the event of breach, first extension was granted to the contractor, second extension was granted subject to the levy of liquidated damages as provided in the contract. Arbitrator did not proceed accordingly. Award set aside.

325. *Indian Oil Corp Ltd v Megi Control Systems (P) Ltd*, (2011) 5 Mah LJ 892.

326. *Construction and Design Services v DDA*, (2015) 14 SCC 263: (2016) 2 SCC (Civ) 800.

### Common features between English and Indian laws

Yet the distinction between liquidated damages and penalty is not altogether irrelevant to the section. Its relevance, in the first place, arises from the fact that the amount contemplated by the parties will be reduced only if it appears to be by way of penalty. Otherwise the whole of it is recoverable as liquidated damages. Secondly, the first explanation to the section uses the word "penalty". It provides that "a stipulation for increased interest from the date of default may be a stipulation by way of penalty". Where, for instance, money is borrowed at 12 per cent interest payable six-monthly, and the agreement provides that in case of default an interest of 75 per cent shall be payable. This is a stipulation by way of penalty.<sup>327</sup> Similarly, where a sum of Rs 100 is borrowed but a bond is given for Rs 200, which further provides that in default of payment of any instalment the whole shall become due. This is a penalty.<sup>328</sup> But where a sum of Rs 100 is borrowed and it is payable by five-monthly instalments and the bond provides that in default of payment of any instalment the whole shall become due, then it is not a penalty and the contract is enforceable. An illustration of penalty is the decision of the Madhya Pradesh High Court in *Gurubax Singh Gorowara v Begum Rafiya Khurshid*.<sup>329</sup> The contract involved the sale of standing trees for a sum of Rs 60,000. The contract provided that in the event of default by either party a compensation of Rs 50,000 would be payable. The court regarded this to be a penalty and required the plaintiff to prove his actual loss. It was not possible for the court to accept that a contract involving a consideration of Rs 60,000 would cause a damage of Rs 50,000 if not performed. Where the whole of the money is presently due and it is only for the benefit of the debtor and for his convenience that the creditor agrees to accept payment in instalments, a provision that a default in the payment of one instalment would make the whole amount to be due at once would not amount to penalty.<sup>330</sup>

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327. Charging of compound interest at the same rate after default is not penalty *per se*, *Mallavarapu Suryanarayana Murthy v Buddaraju Suryanarayana Raju*, AIR 1982 AP 313; following *Venkata Hanumantha Bhushana Rao v Gade Subbayya*, (1936) 44 LW 414; AIR 1936 PC 283.
283. Acceleration of interest is penalty, but not acceleration of capital. *Wadham Stringer Tin Ltd v Meaney*, (1981) 1 WLR 39. Where a sum of about Rs 16,000 was advanced and Rs 28,000 had to be paid back in instalments under Kuri Chit Fund Scheme, the whole becoming due on default in paying a single instalment, the Supreme Court held the stipulation to be by way of penalty. *K.P. Subbarama Sastri v K.S. Raghavan*, (1987) 2 SCC 424; AIR 1987 SC 1257.
328. *Hari Lahu Patil v Ramji Valad Panda*, ILR (1904) 28 Bom 371. "A compound interest is in itself perfectly legal, but compound interest at a rate exceeding the rate of interest on the principal moneys, being in excess of and outside the ordinary and usual stipulation, may well be regarded as in the nature of a penalty." *Rani Sundar Koer v Rai Sham Krishen*, ILR (1906-07) 34 IA 9; (1907) 34 Cal 150.
329. AIR 1979 MP 66.
330. *K.P. Subbarama Sastri v K.S. Raghavan*, (1987) 2 SCC 424; AIR 1987 SC 1257. There is a statutory power under the Usurious Loans Act, 1918 to relieve the borrower against exorbitant interest, *Najaf Ali Khan v Mohd Fazal Ali Khan*, AIR 1928 All 255, interest reduced from 37 per cent to 12 per cent. Exorbitant interest rates are reduced to reasonable amount.

It has been held that a term of a loan agreement which provides for immediate repayment of capital in the event of a default by the borrower and for payment of interest due up to the date of default, but not future interest, is not a penalty clause.<sup>331</sup> A clause in an agreement that the special benefit of a share in the property at a lower price offered to a party under the contract would not be available to a party defaulting in payment of an instalment within the stated time, has been held as not amounting to a penalty.<sup>332</sup>

Still another common feature between the English common law and Indian law is shown by the decision of the Supreme Court in *Chunilal V. Mehta and Sons Ltd v Century Spg & Mfg Co Ltd*,<sup>333</sup> where it has been held that “by providing for compensation in express terms the right to claim damages under the general law is necessarily excluded”.

An agreement for the appointment of managing agents provided that their remuneration would be Rs 6000 per month or 10 per cent of the gross profits of a year whichever was more and also that in the event of premature termination their compensation would be not less than Rs 6000 per month for the whole of the unexpired period. They were removed before the expiry of the term and claimed compensation at the rate of 10 per cent of the gross profits.

But the Supreme Court held that they must be content with the rate of Rs 6000 per month. They were bound by the clause. “It seems to us that the intention of the parties was that if the appellants were relieved of the duty to work as managing agents, they should not be entitled to get anything more than Rs 6000 per month by way of compensation.”<sup>334</sup>

### Forfeiture of earnest money or deposit

In the application of Section 74 to forfeiture clauses, the Supreme Court has drawn distinction between “earnest money” and “security deposit”. The distinction was set to work in *Fateh Chand v Balkishan Das*.<sup>335</sup>

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For example, 75 per cent reduced to 15 per cent and 60 per cent compound to 30 per cent simple.

331. *Angelic Star, The*, (1988) 1 FTLR 94 (CA).

332. *Sova Ray v Gostha Gopal Dey*, (1988) 2 SCC 134: AIR 1988 SC 981.

333. AIR 1962 SC 1314: 1962 Supp (3) SCR 549. Penalty cannot be imposed where delay is due to the conduct of the party trying to impose penalty. *ONGC v S.S. Agarwalla & Co*, AIR 1984 Gau 11.

334. There is nothing essentially wrong in awarding maximum fixed by the parties. *Shiva Jute Baling Ltd v Hindley & Co Ltd*, AIR 1959 SC 1357: (1960) 1 SCR 569. *Satyanarayana Construction Co v Union of India*, (2011) 15 SCC 101, once rate has been fixed in a contract for a particular work, the contractor is not entitled to claim any additional amount merely because he had to spend more in completing the work.

335. AIR 1963 SC 1405: (1964) 1 SCR 515. *Happy Home Builders (P) Ltd v Delite Enterprises*, (1995) 2 AIHC 1320. Forfeiture of licence fee does not take place automatically on violation of the conditions of the licence. The Commissioner may order forfeiture either in full or in part, but before that he must hear the licensee and pass a judgment in accordance with the loss to the Government. Automatic forfeiture would amount to penalty, *G. Shankar Reddy v Prohibition and Excise Supt*, (1997) 5 An LT 177.

An agreement for the sale of certain land and bungalow for Rs 1,12,500 provided that the buyer was to pay Rs 1000 as earnest money and Rs 24,000 on delivery of possession. The buyer made these payments and was put in possession. The agreement further provided that if the buyer failed to pay the balance price and get the sale deed registered by a certain date, the sum of Rs 25,000 would stand forfeited, the agreement cancelled and the buyer shall return possession to the seller. The buyer defaulted and the seller forfeited the above sum and brought an action to recover possession and compensation for occupation and use.

He was allowed to forfeit Rs 1000 being earnest money and to retain the sum of Rs 24,000 also not by virtue of his right to forfeit but as representing use value. SHAH J refuted the fallacy as shown by some High Court decisions that Section 74 applies only to cases where the aggrieved party is seeking to recover a fixed amount on breach of contract and not to cases where an amount received under the contract is sought to be forfeited.

In our judgment the expression “the contract contains any other stipulation by way of penalty” comprehensively applies to every covenant involving a penalty whether it is for payment on breach of contract of money or delivery of property in future or for forfeiture of right to money or other property already delivered. In all cases, therefore, where there is a stipulation in the nature of penalty for forfeiture of an amount deposited pursuant to the terms of contract, the court has jurisdiction to award such sum only as it considers reasonable, but not exceeding the amount specified in the contract as liable to forfeiture.<sup>336</sup>

Neither earnest money nor any other kind of deposit which is liable to be forfeited can be subjected to forfeiture if the underlying contract is void. The Supreme Court laid down this principle in a case in which in a transaction for sale of land the buyer was under the impression that he was getting the land at the agreed price per *bigha* whereas the seller believed he was selling

336. The provision is applicable to every kind of deposit by whatever name it may be called. The words “any other stipulation by way of penalty” are wide enough to cover all kinds of forfeiture provisions. *Union of India v Shaim Sunder Lal*, 1963 All LJ 251. *Bombay Scrap Traders v Port of Bombay*, (1994) 1 Bom CR 266, failure on the part of the tenderer to comply with the work order, forfeiture of earnest money, held justified. *State of Karnataka v Stellar Construction Co*, AIR 2002 Kant 6: (2002) 5 Kant LJ 474, the road building contractor was not paid extra charges because the claim in respect thereof was not found by the Department to be justified. He had received payment as per contractual terms. He stopped working and did not resume it inspite of clear notice. The court said that this amounted to breach. He was not entitled to claim refund of the forfeited security deposit. *New Media Broadcasting (P) Ltd v Union of India*, AIR 2008 NOC 967 (Del), contract envisaged specification of further details, by Govt, some changes on representation of bidders were within tender terms, bidder whose bid was accepted refused to sign, right to forfeit earnest money and claim damages arose. *Winmaxx Management Service (P) Ltd v UCO Bank*, AIR 2011 Gau 217, the auction buyer failed to pay the whole of the earnest money. Forfeiture of money actually paid by him held to be justified. *Haryana Financial Corpn v Rajesh Gupta*, (2010) 1 SCC 655: AIR 2010 SC 338, auction sale of unit, earnest money deposited on assurance that independent approach road to unit would be provided, but not actually done, the purchaser did not make further payment, forfeiture of his earnest held to be not proper.

per *kanal*. The parties being at cross-purposes and being not *ad idem*, the agreement was void. There was no question of forfeiting, the earnest money. It was refundable under Section 65, the contract having been discovered to be void.<sup>337</sup>

Similarly, there can be no forfeiture or encashment of bank guarantee where no contract arises. A tender which has been revoked before acceptance cannot be accepted and, therefore, the bank guarantee submitted along with the tender also becomes revoked and cannot be encashed.<sup>338</sup>

Whatever be the name or nature of the amount deposited by one party with the other which is liable to forfeiture in the event of breach, Section 74 would come into play and only that part of the amount would be open to forfeiture which is reasonable in the circumstances of the case. Anything more would tantamount to penalty.<sup>339</sup> Forfeiture of earnest money is permissible by way of liquidated damages.<sup>340</sup>

There is no absolute right to forfeit the entire amount without proof of the total extent of loss, when the material on record showed that the extent of loss was less than the amount held as earnest, forfeiture could not go beyond that. No one can be allowed to enrich himself at the cost of the other by taking advantage of the forfeiture clause.<sup>341</sup>



CASE PILOT

337. *Tarsem Singh v Sukhminder Singh*, (1998) 3 SCC 471; AIR 1998 SC 1400. But see *State of Gujarat v Dahyabhai Zaverbhai*, (1997) 9 SCC 34; AIR 1997 SC 2701, the contractor abandoned the project, forfeiture of security deposit held justified. *J.K. Enterprises v State of M.P.*, AIR 1997 MP 68, forfeiture of earnest money on failure of bidder to perform, justified.

338. *Omprakash & Co v City and Industrial Development Corp of Maharashtra Ltd*, (1994) 1 Bom CR 30; (1993) Mah LJ 1419. *V. Lakshmanan v B.R. Mandalagiri*, 1995 Supp (2) SCC 33, forfeiture of earnest money on default in sale of land. The same was the position in *Food Corporation of India v Sujit Roy*, AIR 2000 Gau 61. The earnest money of a tenderer was forfeited before acceptance of the tender and conclusion of the contract and the dispute between the parties was also not related with the contract, a *writ petition* challenging the forfeiture was held to be maintainable.

339. *Thakorlal V. Patel v Lt. Col. Syed Badruddin*, (1993) 1 Guj LR 28. See also *P. Nagrajan v Southern Structural Ltd*, ILR (1995) 1 Mad 337, agreement upon entering into service that the employee would serve for five years, Rs 15,000 payable for breach of the term, held reasonable compensation.

340. *Narendrakumar Nakhat v Nandi Hasbi Textile Mills Ltd*, AIR 1997 Kar 185. Where a contract for purchase of property worth Rs 30 lakhs carried earnest money of three lakh rupees and a damage clause of Rs 12 lakhs, the clause was held to be unreasonable, *Roshan Lal v Manohar Lal*, AIR 2000 Del 31. *H. Sowbhagya v NGEF Ltd*, AIR 2004 Kant 155, purchaser of property at auction defaulted, reauction brought higher price, earnest money not allowed to be forfeited though reasonable compensation was allowed. *Amarjeet Singh v Zonal Manager, FCI*, (2002) 4 ICC 47 (P&H), a public authority has to exercise its powers even under the contract fairly and reasonably. Even otherwise, namely where Government is not a party, the terms relating to forfeiture must be strictly followed and the courts should also strictly construe them.

341. *Gatta Rattaiah v Food Corporation of India*, AIR 2011 AP 65; *Jalal Nasar v Official Liquidator*, (2008) 5 CTC 385 (Mad), in a bidding process 10 per cent of the total value of the contract of Rs 236 crores, Rs 23.60 crores was required to be deposited as earnest money, the bidder could deposit only Rs 10 crores. The next highest bidder deposited whole of the earnest money but failed to deposit the rest of the amount required under the advertisement.

### *Forfeiture of earnest money on non-fulfilment of conditions of e-auction*

There was e-auction of “Film Solar Photovoltaic Module”. As per terms and conditions, e-waste certificate and e-waste disposal was to be obtained by the bidder. He did not do so. Forfeiture of earnest money as per forfeiture clause was held to be proper.<sup>342</sup>

A provision in a contract for recovery of double the amount of sale consideration as a penalty for breach of contract was held to be not legally permissible. It was vouched as a clear penalty for breach. Even otherwise it was clearly in the nature of penalty and therefore not permissible.<sup>343</sup>

### *Withholding of payment under bills*

There was e-tender for extraction of coal. The equipment capacity of the bidder was less than the required capacity. The bidder could not achieve the target. The result was huge shortage in extraction and transportation of coal. The tender requirement of deployment of requisite equipment was not fulfilled. It was held that withholding of his bills and imposition of shortfall penalty was proper.<sup>344</sup>

### *Whether actual loss necessary*

Another question which the court considered was whether actual proof of loss is necessary to recover anything under Section 74. In the earlier case of *Chunilal V. Mehta and Sons Ltd v Century Spg & Mfg Co Ltd*<sup>345</sup> MUDHOLKAR J suggested that where the right to recover liquidated damages under Section 74 is found to exist “no question of ascertaining damage really arises”. The section also says that the named sum is recoverable “whether or not actual damage or loss is proved to have been caused thereby”. But even so SHAH J felt that these words of the section only dispense with proof of “actual loss or damage”. The section does not justify the award of compensation, when in consequence of the breach no legal injury at all has resulted. This is so because compensation can only be awarded under Section 73 for loss which naturally arose or was in the contemplation of the parties. Thus

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Consequently forfeiture of earnest money of both of them. It did not appear in the judgment whether reasonableness of the amount forfeited was considered. Reasonableness is linked with the loss caused.

342. *M. Eswari v MSTC Ltd*, AIR 2014 Mad 182.

343. *Maya Devi v Lata Prasad*, (2015) 5 SCC 588.

344. *Sainik Mining & Allied Services Ltd v Mahanadi Coalfields Ltd*, AIR 2015 Ori 78.

345. AIR 1962 SC 1314: 1962 Supp (3) SCR 549. See also *Hind Construction Contractors v State of Maharashtra*, (1979) 2 SCC 70; AIR 1979 SC 720, where the State illegally rescinded the contract, it was not allowed to forfeit the contractor's deposit. *Sukhdev Kaur v Hoshiar Singh*, (2004) 2 ICC 55 (P&H), even where there is a liquidated damage clause the party claiming damages may have to show his loss this being necessary to ascertain the element of reasonableness, though actual proof of loss may not be necessary where the party committing breach knew that loss was a likely result of the breach.

proof of some loss is necessary,<sup>346</sup> though it will not be necessary to prove the extent of it.

This view was reaffirmed by SHAH J (acting CJ) in *Maula Bux v Union of India*.<sup>347</sup>

The plaintiff contracted to supply to Military Headquarters, U.P. Area, potatoes, poultry, eggs and fish for one year and deposited Rs 18,500 for due performance of the contract. The plaintiff having made persistent defaults in making regular and full supplies, the Government of India, in pursuance of the terms of the contract, rescinded the contract and forfeited the amount deposited by the plaintiff.

The High Court of Allahabad was of the view that the deposit in question was in the nature of earnest money and the Supreme Court decision in *Fatehchand v Balkishan Das*<sup>348</sup> did not purport to overrule the previous trend of authorities to the effect that earnest money deposited by way of security for the due performance of a contract does not amount to penalty as contemplated by Section 74. The Supreme Court did not countenance the view that every such deposit is necessarily an earnest. The court cited the meaning of earnest money as given in Earl Jowitt, THE DICTIONARY OF ENGLISH LAW.<sup>349</sup>

Giving an earnest or earnest money is a mode of signifying assent to a contract of sale or the like by giving to the vendor a nominal sum (e.g. a shilling) as a token that the parties are in earnest, have made up their minds.

The court also cited the observation of the Privy Council in *Chiranjit Singh v Har Swarup*<sup>350</sup> that "earnest money is part of the purchase price when the transaction goes forward: it is forfeited when the transaction falls through by reason of the fault or failure of the vendee". If this is the view of an earnest deposit, then quite obviously the deposit in the present case was not by way of earnest because it was not to be appropriated towards the payment of price, but was to be held as a security. SHAH, acting CJ (afterwards CJ), then referred to the cases to the effect that Section 74 has no application to forfeiture of deposits and ruled that this view is no longer good law. The learned Chief Justice continued:

346. The claimant has to prove his actual loss. *Karamchand Thapar & Bros Ltd v H.H. Jethandani*, 76 CWN 38. *Pure Pharma Ltd v Union of India*, ILR (2009) 1 Del 272, there must be proof of legal injury before compensation can be claimed.

347. (1969) 2 SCC 554: AIR 1970 SC 1955. Followed in *Food Corporation of India v Gauri Prasad Gopal*, 1987 All LJ 567 where the FCI had reserved the right to recover Rs 5000 on default by the supplier plus expenses and difference in prices in the alternative purchase and was ordered to refund the security deposit of Rs 5000 because the Corpn did not show any actual loss.

348. AIR 1963 SC 1405: (1964) 1 SCR 515.

349. At p. 689.

350. (1925-26) 53 IA 11: AIR 1926 PC 1.

Forfeiture of earnest money under a contract of sale, if the amount is reasonable does not fall within Section 74. This has been decided in several cases.<sup>351</sup> 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, the undertaking is in the nature of a penalty.

Referring to the argument that Rs 18,500 represent a genuine pre-estimate of the probable damage, the learned Chief Justice said that the Union has not proved to have suffered any loss. If no loss is proved to have been suffered, the provisions of the Act in Sections 73 and 74 relating to damages for breach are not attracted. The court confined the words of Section 74 that "whether or not actual damage or loss is proved to have been caused thereby" to cases in which it is not possible to prove the monetary value of the loss and, therefore, the value fixed by the parties may be taken as the reasonable measure of compensation. But where the loss in terms of money can be determined, the party claiming compensation must prove the loss suffered by him. Since no attempt was made by the Government to prove whether the prices paid to the alternative source of supply were less or more than the contract price, therefore, the Government was not entitled to any compensation for the breach.

Where the actual loss was not proved and the whole of the actually reserved amount of 5 per cent of the total project value was levied as liquidated damages, the court said that it amounted to a penalty. The award of the arbitrator to that extent was set aside.<sup>352</sup> Where the contractor delayed supplies of cables and the Government had to purchase from other sources and coincidentally happened to procure at cheaper rates, the award of the arbitrator awarding damages for breach of contract was set aside.<sup>353</sup>

In another similar case, the arbitrator awarded only half the amount that was specified in the contract because no actual loss was shown, the court refused to interfere. The award of 12 per cent interest was not interfered with.

Where there was breach of a rigging contract and the amount predetermined in the contract was recovered, justifying this recovery, it was held that it was not enough to defeat such a right to show that not enough material was placed on record for exact assessment of quantum of losses suffered.

351. Following cases were cited: *Chiranjit Singh v Har Swarup*, (1925–26) 53 IA 11: AIR 1926 PC 1; *Roshan Lal v Delhi Cloth & General Mills Co Ltd*, ILR (1911) 33 All 166; *Mohd Habibullah v Mohd Shafi*, ILR (1919) 41 All 324; *Bishan Chand v Radha Kishan Das*, ILR (1897–1900) 19 All 489.

352. *English Electric Co of India Ltd v Cement Corp of India Ltd*, 1996 AIHC 1875 (Del). *ONGC Ltd v Saw Pipes Ltd*, (2003) 5 SCC 705: AIR 2003 SC 2629 proof of loss not necessary when a genuine pre-estimate of the loss is stipulated in the contract.

353. *Haryana Telecom Ltd v Union of India*, AIR 2006 Del 339.

Burden of proving that no losses were actually caused to the other party was on the party committing breach. The court said that it was not necessary for the party to lead evidence to show the amount of loss suffered by it unless the breaching party came to the court and proved that no loss was in fact caused.<sup>354</sup>

#### *Where no loss caused*

An amount was paid by a purchaser in advance towards the purchase price of the goods. The contract provided that on default by the purchaser the amount would be forfeited. He defaulted. He was allowed refund. The seller proved no loss. The court said that retention of money for a long period was sufficient to compensate the plaintiff.<sup>355</sup> Where on default by the original bidder in paying the balance of the price, the material was reauctioned and the vendor State obtained a higher price, the court said that the provision for forfeiture of 25 per cent of the price paid in advance would have operated as a penalty. The court could award only a reasonable amount as damages, namely, interest on the amount in default from due date to receipt of price from alternative buyer.<sup>356</sup>

A clause in a contract permitted estimation and recovery of wrongful gain, if any, made by the contractor. The contract was terminated because of wrongful gain made by not fulfilling the conditions of the contract. The court did not permit the bank guarantee to be invoked because the Authority had already made good its losses by forfeiting performance security furnished by the contractor and had also recovered the penalty amount.<sup>357</sup>

Where the arbitrator recorded a finding that the supply of material beyond the stipulated period had not resulted in any loss to the Port Trust, the court said that compensation was payable only when the breach had resulted in a legal injury. Accordingly the Port Trust was not entitled to retain any amount towards compensation.<sup>358</sup>

#### *Exclusion of right to compensation*

It may be possible in some cases that no compensation is payable because the aggrieved party has suffered no loss, but it is not possible to say that no

354. *Jagson International Ltd v Oil & Natural Gas Corp Ltd*, (2003) 4 Mah LJ 733: (2004) 2 Bom CR 272. Another similar decision is in *ONGC Ltd v Saw Pipes Ltd*, (2003) 5 SCC 705: AIR 2003 SC 2629.

355. *Sabina D'Costa v Joseph Antony Noronha*, AIR 1984 Kant 122. Similarly, where the seller committed breach of the contract by sending defective goods which were rejected by the buyer, the seller was not allowed to forfeit the money held by him by way of advance payment. *P.M. Naina Mohammed Rowther v Kapporchan Jain*, 1987 SCC OnLine Mad 293: (1988) 1 LW 495. *Vishal Engineers & Builders v Indian Oil Corp Ltd*, AIR 2012 NOC 165 (Del), proof of loss is necessary. If there was absence of any loss and therefore without proving any semblance of loss, the party could not claim that even so it was entitled to liquidated damages.

356. *H. Sowbhagya v NGEF Ltd*, AIR 2004 Kant 155, the court also emphasised that the State was expected to act in a fair and non-arbitrary manner.

357. *A.S. Motors (P) Ltd v Union of India*, (2013) 10 SCC 114: (2013) 4 SCC (Civ) 660.

358. *Ennore Port Ltd v Hindustan Construction Co Ltd*, (2005) 4 LW 319.

compensation is payable because there is a provision to that effect in the contract. It has been held that contract clauses which disentitle an aggrieved party to the remedial benefits of Sections 55 and 73 would be void because of violation of the very intent and purport of the Contract Act. [S. 23] There is public policy and public interest element in these sections. Sections 73 and 55 are the very heart, foundation and basis of the contractual relation. A contract, which can be broken at will, will be destructive of the very edifice of the contract.<sup>359</sup>

### *Loss caused by mutual delay*

Both parties contributed to causing delay in completion of work. It was impossible to know what percentage of delay was attributable to one party or the other. Deduction of amounts from running bills of the contractor by way of liquidated damages was held to be illegal and improper.<sup>360</sup>

### *Where profit follows*

Where not only no loss was caused to the seller of land by the buyer's refusal to perform, but, on the contrary, he resold it at a profit, the seller was not permitted to forfeit the advance paid by the buyer.<sup>361</sup> The same result followed where 25 per cent of the auction purchase price was paid in advance and it was not allowed to be forfeited for the default in payment of the balance price. The reauction was at a higher price. The court, allowed interest on the balance from the date of default till due date of payment by the subsequent purchaser.<sup>362</sup>

**FORFEITURE OF EARNEST MONEY ONLY WHEN REASONABLE TO DO SO.**—In the subsequent case of *Shree Hanuman Cotton Mills v Tata Aircraft Ltd*:<sup>363</sup>

The plaintiffs contracted with the defendants to purchase from them aeroscrap for rupees ten lakhs and paid Rs 2,50,000, being 25 per cent of the purchase price. One of the conditions, among others being, that if he failed to pay the balance of the purchase price in accordance with the contract, the deposit would be forfeited and the contract cancelled. The buyer defaulted and the seller forfeited the deposit. The buyer sued to recover it.

359. *Simplex Concrete Piles (India) Ltd v Union of India*, ILR (2010) 2 Del 699.

360. *Mecon Ltd v Pioneer Fabricators (P) Ltd*, AIR 2008 NOC 870 (Del).

361. *Mohanlal v Dayaldas & Co*, AIR 1976 Raj 68. Compare this with *Lal Chand v Chandigarh Admn*, AIR 1992 P&H 194 where the earnest money of an allottee of a plot, who defaulted in further payments, was held to be properly forfeited irrespective of any consideration of the fact of loss, if any, caused, or profit obtained upon reallocation. Perhaps this is necessary to exclude opportunist allottees.

362. *H. Sowbhagya v NGEF Ltd*, AIR 2004 Kant 155.

363. (1969) 3 SCC 522: AIR 1970 SC 1986. *DDA v Gribshapana Coop Group Housing Society Ltd*, 1995 Supp (1) SCC 751: AIR 1995 SC 1312, additional amount demanded towards premium on the cost of the land allotted to the society, not paid, the Supreme Court justified forfeiture of earnest money.



The court held that the deposit in question was intended as earnest money. The agreement clearly provided that the deposit would carry no interest and would be adjusted in the final bills. It was a part of the price and the seller was entitled to forfeit it. VAIDALINGAM J found sufficient support in the following decision of the Privy Council:

In *Chiranjit Singh v Har Swarup*,<sup>364</sup> though the contract stipulated that a sum of Rs 20,000 should be paid as earnest, the buyer did not pay any amount by way of earnest, as such, but he paid Rs 1,65,000 against the purchase price. But, nevertheless, the High Court, as well as the Judicial Committee, treated a sum of Rs 20,000 out of the sum of Rs 1,65,000, as earnest money paid under the terms of the agreement, and a claim to recover that amount of earnest money was negatived. In the case before us, the contract clearly refers to the earnest money being paid and to the fact of Rs 2,50,000 having been paid as earnest. Therefore, there is no ambiguity regarding the nature of the above payment and the right of the respondent to forfeit the same.

The learned Judge refused to consider the obiter observation of the Supreme Court in *Maula Bux v Union of India*<sup>365</sup> that earnest money can be forfeited without attracting Section 74 if the amount thereof is reasonable as binding. He pointed out that the Supreme Court itself had no occasion in that case to consider the question of reasonableness or otherwise of the earnest deposit being forfeited.<sup>366</sup>

#### *Refund of earnest money where wrong specification provided*

The plaintiff contractor informed the State about difficulties that arose while he was excavating the river bank for construction of submersible bridge. The boring test showed that the sandy clay was 18 feet deep below the bed level whereas the information supplied was that it was only 12 to 16 feet deep. The State refused to revise rates. Delay in the work led the State to invite fresh tenders for the project. The plaintiff was allowed refund of his earnest money and also 1/3rd of the cost of construction.<sup>367</sup>

**DISTINCTION BETWEEN EARNEST AND DEPOSIT, HOW FAR REAL.**—Thus, it appears that the court has gone more by technical considerations than by the substance of the bargains in question. In either case the initial payment,

364. (1925–26) 53 IA 11: AIR 1926 PC 1.

365. (1969) 2 SCC 554: AIR 1970 SC 1955.

366. See also *Naresh Chandra Sanyal v Calcutta Stock Exchange Assn Ltd*, (1971) 1 SCC 50, 58: AIR 1971 SC 422; (1971) 2 SCR 483, 494, where upon the forfeiture of a share, the consequent price realised was more than the sum due and, therefore, the court ordered the surplus to be refunded to the holder whose share was forfeited for otherwise it would have been a penalty. *Mohd Sultan Rowther v Naina Mohammad*, AIR 1973 Mad 233, in the absence of a forfeiture clause, nothing can be forfeited, only reasonable compensation can be recovered. After deducting reasonable compensation, the remainder of the money has to be refunded to the depositor.

367. *State of Bihar v S. Gheyasuddin*, AIR 2009 NOC 387 (Pat).

whether named as earnest or security deposit, was intended as a cover or protection against inconvenience or possible loss likely to be caused by the breach. If the deposit was named as earnest the court allowed it to be forfeited, but not otherwise, thus defeating the purport of the bargain that the parties had voluntarily made. The fact that the payment of a sum of money in a purchase agreement is not expressed as a deposit does not for that reason alone render the payment not a true deposit or earnest money. The intention of the parties with regard to the payment as earnest money may be gathered by examining the agreement as a whole. Even if no time for completion of the sale by paying the balance of the price was specified, the seller's notice for completing the sale within seven days became a reasonable specification of time. Therefore, on the purchaser's failure to do so, the money paid by him was validly forfeited even if there was no provision in the original agreement for any such forfeiture.<sup>368</sup>

The facts of *Maula Bux v Union of India*<sup>369</sup> were virtually repeated before the Supreme Court in *Union of India v Rampur Distillery & Chemical Co Ltd*<sup>370</sup> with only this difference that instead of eggs etc., it was "rum" that the contractor had failed to supply and the Supreme Court refused to allow the deposit to be forfeited or reasonable compensation to be recovered as the court found that breach of contract caused no loss to the Government and the Government made no attempt to establish that it had suffered any loss or damage on account of the breach.<sup>371</sup> The Gujarat High Court in its decision in *Variety Body Builders v Union of India*<sup>372</sup> followed the Supreme Court decisions in reference to a failure to supply rubber and metal to the Western Railway. Commenting upon this trend of decisions, a learned writer says:

In the light of these decisions it is important for the Government departments to advise officers entering into contracts with contractors on behalf of the Government that they ought not to lull themselves into a false feeling of security by taking a security deposit and stipulating for its forfeiture upon default by the contractor. Under Section 74 all that the Government can claim is reasonable compensation and it is always necessary that the Government should establish the actual damage suffered by it by the contractor's default. If Government officers are not educated on these questions, the defaulting contractor will not only be able to recover his security deposit, but will be able to get away without paying

368. *Yab Kok Heng v International Auto Enterprise*, (1994) 1 CLJ 414 (Malaysia). The court said that expressions like earnest money, part payment or deposit are generally used interchangeably. So stated in *Sun Properties v Happy Shopping Plaza*, (1972) 1 Mal LJ 89 (Malaysia).

369. (1969) 2 SCC 554: AIR 1970 SC 1955.

370. (1973) 1 SCC 649: AIR 1973 SC 1098. *Pran Nath Suri v State of M.P.*, AIR 1991 MP 121, on the failure of the bidder to execute documents, the auctioneer not reselling during the whole of the period, not allowed to recover any loss but entitled to forfeit earnest money.

371. *SHELAT and CHANDRA JJ see at p. 1099.*

372. AIR 1973 Guj 256.

any damages for breach of contract, as did the contractor in *Maula Bux* and *Variety Body Builders*.<sup>373</sup>

Where the property of a company was auctioned but the auction purchaser made defaults and, therefore the property had to be auctioned again and then it realised over two lakhs more than the earlier bid money, it was held that the earnest money of the defaulting bidder running up to more than five and a half lakh rupees could not be forfeited. It would have been highly arbitrary and unreasonable to do so. A compensation of Rs 1,49,763 was awarded to the company.<sup>374</sup>

#### *No forfeiture where extra costs otherwise recovered*

Where, upon the failure of the contractor to complete the work, the State got the work executed at his risk and also recovered the extra expenses from him, the State was not allowed to forfeit his security deposit. This would have amounted to penalty and the State had suffered no loss.<sup>375</sup> The Andhra Pradesh High Court allowed the plaintiff to recover the stipulated amount of Rs 2000 from a vendor of land who failed to perfect his title within the prescribed time although no proof was given of any actual loss.<sup>376</sup>

#### *No forfeiture where contract still not formulated*

The requirement of tendering was satisfied by the highest bidder by depositing the requisite earnest money. The bid was not confirmed by the authority though a period of more than one year had passed. The bidder withdrew his tender. The authorities then confirmed his bid and forfeited his earnest money for not depositing the balance money within 30 days from the date of confirmation. The court said that the absence of any time prescribed for acceptance could not give the authority an unlimited and unreasonable period of time. The forfeiture was not proper and therefore the amount forfeited was refundable.<sup>377</sup>

After acceptance of tenders, the contractor was informed that any further sale of the plots by him would invite payment of premium equivalent to 20 per cent of the sale value of the plot. Such condition did not form part of public advertisement or terms of condition of auction sale. The contractors were held entitled to get refund of the earnest money deposited with interest at 7.5 per cent interest per annum from the date of withdrawal of offer till date of payment.<sup>378</sup>

373. For another learned study of the subject, see I.C. Saxena, *Deposit Forfeiture: A Comparative Legal Perspective*, (1970) 12 JIL 1 441 and the *Survey of the Law of Contract*, (1970) ASIL, 320, 353-57.

374. *H. Sowbhagya v NGEF Ltd*, AIR 2004 Kant 155.

375. *State of U.P. v Chandra Gupta & Co*, AIR 1977 All 28.

376. *Makkala Narasimlu v Gunnala Raghunandan Rao*, AIR 1977 AP 374.

377. *Commr of HR & CE Deptt v S. Muthukrishnan*, AIR 2012 Mad 43.

378. *Jayant Shanthal Sanghvi v Vadodara Municipal Corp*n, AIR 2011 Guj 122 (DB).



*Stipulation for refund of double amount of earnest and interest*

The stipulation in the contract was that if the party failed to perform from his side, he would refund the amount of earnest doubling it up and also with interest at 12 per cent p.a. It was held that the Civil Judge rightly decreed the suit of the plaintiff to receive the double amount by way of compensation. It must be presumed that the parties at the time of entering into the agreement knew very well the amount of loss which the plaintiff was likely to sustain in the event of breach. Where the parties were supposed to know that breach would cause loss in any case, it would not be necessary for the aggrieved party to show any actual loss. The court has the ample power to grant compensation for loss caused by breach of contract.<sup>379</sup>

**Security money under other contracts**

Security money paid in respect of other contracts cannot be forfeited in respect of the contract under dispute, but bill-money due to the contractor under other contracts may be so used.

A clause in a contract provided that all moneys or compensation payable to the Government under the terms of the contract may be realised out of the security deposit or money due under any other account.

The Supreme Court came to the conclusion that this clause enabled the Government to realise its claim from money due to the contractor in respect of other contracts and the security deposited under the present contract but not the security deposit belonging to other contracts.<sup>380</sup>

Where a contract for the supply of gas in cylinders was being performed in instalments and there was such a breach in respect of one instalment which entitled the purchaser to terminate the contract, he was allowed compensation at the rate fixed in the contract for the failure to supply the remainder. To attract Section 74 it is not necessary that a contract should be broken in its entirety.<sup>381</sup>

379. *Sukhdev Kaur v Hoshiar Singh*, (2004) 2 ICC 55 (P&H).

380. *Union of India v K.H. Rao*, (1977) 1 SCC 583: AIR 1976 SC 626. In the subsequent case of *H.M. Kamaluddin Ansari & Co v Union of India*, (1983) 4 SCC 417: AIR 1984 SC 29, where the court expressed the opinion that money due in respect of other contracts may be forfeited if there is a clear and express provision to that effect under the contract. Where a vendor has been given the right to repurchase on default and he does so, it cannot be called a penalty on default. The court cannot provide any relief against repurchase. *K. Simrathmull v Nanjalingiah Gowder*, 1962 Supp (3) SCR 476: AIR 1963 SC 1182. In the sale of a forest for Rs 60,000, damages for failure to perform were named as Rs 50,000, held, a penalty. The seller was not allowed even normal compensation because he proved no loss. *Gurubax Singh Gorowara v Begum Rafiya Khurshid*, AIR 1979 MP 66. Where the Government wants to debar and blacklist a contractor, that being also a penalty, the contractor should be given an opportunity to explain his position. *Joseph Vilangandan v Executive Engineer*, (1978) 3 SCC 36: AIR 1978 SC 930. *Pran Nath Gupta v Union of India*, AIR 2004 J&K 135, provision for recovery of money due under earlier bills from subsequent bills, its validity not allowed to be tested under writ jurisdiction.

381. *Indian Drugs and Pharmaceuticals Ltd v Industrial Oxygen Co (P) Ltd*, 1984 Mah LJ 690. *K.B. Machaish v Ajittira S. Mandanna*, AIR 1997 Kant 194, the party who caused

### *Show-cause notice before forfeiture*

Forfeiture of earnest money without insurance of a show-cause notice is violative of the principle of natural justice.<sup>382</sup>

### **Consent decrees**

The Madhya Pradesh High Court considered it to be well-settled that principles underlying Section 74 are applicable to consent decrees. A contract embodied in a decree is subject to all the incidents of any other contract. Accordingly, if it contains any clause which is of penal nature, it can be struck out. Applying these principles to a contract for sale of land for Rs 2000 half of which was deposited by way of earnest and which was compromised under which a consent decree was passed to the effect that the defendant would pay Rs 2000 plus costs in two instalments and that if he defaulted he would execute the sale deed in favour of the plaintiff, the default clause was held to be a penalty. The court said that the executing court shall always have power to apply equitable principles embodied in Section 74 and relieve a party to the contract against any term in the decree which operates as a penalty.<sup>383</sup> On the other hand, where the compromise about a decree was that if the tenant would pay all the money found due against him by a certain date, the landlord would not enforce the decree of dispossession, this was held to be as not amounting to a penalty.<sup>384</sup>

A compromise decree provided for payment of the principal sum with interest at the rate of 18 per cent p.a. from the date of suit till date of decree. Liberty was given to the decree holder to apply for its execution if the judgment-debtor failed to pay the decree by the date specified in it. This stipulation was held to be not in the nature of a penalty. The court said that the executing court had no jurisdiction to go into the question whether the rate of interest awarded was excessive or unreasonable.<sup>385</sup>

Where the plaintiff's suit was compromised on the basis that he would pay certain sum of money by instalments and that on default in payment, the plaintiff's suit would be dismissed, it was held that this would amount to penalty and, therefore, extension of time should be granted for covering up the delay in the payment of the first instalment.<sup>386</sup>

The burden to establish that a clause in the decree is in the nature of penalty and is unenforceable under Section 74 of the Contract Act is on the judgment-debtors. There cannot be any dispute that on account of the delay

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premature termination of a cinematographic agreement agreed that the aggrieved party would have suffered a loss of Rs 25,000. An award Rs 10,000 by way of damages was held to be justified.

382. *S.R.S. Infra Projects (P) Ltd v Gwalior Development Authority*, (2010) 2 MPLJ 142.

383. *Parvati Bai v Ayodhya Prasad Jain*, 1985 MPLJ 703. For a contrary view, see *Punjab Woollen Textiles Firm v Bank of India*, AIR 1992 P&H 158.

384. *Prithvichand Ramchand Sablok v S.Y. Shinde*, (1993) 3 SCC 271: AIR 1993 SC 1929, 1934–35.

385. *B.V. Basavaraj v N.R. Chandran*, (2000) 3 Kant LJ 195.

386. *Jolly Steel Industries (P) Ltd v Gupta Steel Industries*, (1997) 1 Bom CR 192.

in getting back the collateral securities on payment of the entire debt due to the bank the decree-holder would be put to serious loss as he might not be able to raise any further loan for his business or to discharge the existing loans by sale of the other properties as the title deeds were with the bank. Both the parties were aware of their rights and liabilities and with open eyes they entered into a compromise. When the parties submitted before the court and agreed to a decree in terms of the compromise specifying the liquidated damages, and a decree was passed in terms of the agreement, the judgment-debtor could not later turn round and contended that damages agreed to were penal in nature.<sup>387</sup>

A majority view of the Full Bench of the Allahabad High Court was that a compromise decree is a creature of the agreement on which it is based and it is subject to all the incidents of such agreement and that it is a contract with the command of a Judge super added to it and in construing its provisions the fundamental principles governing the construction of contracts are applicable. It was also held that one of the cardinal principles in the construction of contracts is that the entire contract must be taken as constituting an organic synthesis embodying provisions which balance in the sum of reciprocal rights and obligations.<sup>388</sup>

### Clear notice of clause requisite

To justify forfeiture of advance deposit, being a part of the price as "earnest" the terms of the contract should be sufficiently explicit and must be made known to the party making the deposit. In this case the aggrieved party has shown that the terms of auction were neither advertised nor were they supplied to the intending bidders at the time of the auction. The auctioning authority, therefore, could not contend that  $\frac{1}{4}$  payment was meant as earnest and a guarantee money for performance. Nor the authority had proved any loss upon the bidder's default.<sup>389</sup>

### Minimum charges

Minimum charges for supply of electricity have been held to be not by way of penalty. The maintenance of a supply line does cost something and if a consumer does not consume to a certain figure, the supplier may recover from him the specified minimum in order to meet his costs. This requires that the minimum should be reasonable in the circumstances and not arbitrary.<sup>390</sup>

387. *Sukumaran v Anthony*, (2005) 2 KLT 919.

388. *Habib Mian v Mukhtar Ahmad*, AIR 1969 All 296 (FB).

389. *Bhanwarlal v Babulal*, AIR 1992 MP 6.

390. *Mahavir Khandsari Sugar Mill v Maharashtra SEB*, AIR 1993 Bom 279. The court followed *Gujarat Electricity Board v Shri Rajratna Naranbhai Mills Co Ltd*, (1975) 16 Guj LR 90; *Watkins Mayor & Co v Jullundur Electricity Supply Co Ltd*, AIR 1955 Punj 133. Here the concept of minimum charge was thus explained: "A minimum charge is not really a charge which has for its basis the consumption of electrical energy. It is based on the principle that every consumer's installation involves the licensee in a certain amount of capital expenditure

### Interest by way of damages

Interest is generally not awarded by way of damages. There has to be an agreement to that effect or statutory provisions. When money due is wrongfully withheld, interest can be demanded even in the absence of agreement. But for that purpose, a written demand is mandatory. In the absence of any such thing as that, the plaintiff was allowed interest at the rate of six percent. The withheld payment was due under the contract.<sup>391</sup>

Where in the matter of a commercial transaction there was a term in the contract providing that the defendant would be liable to pay interest at 20 per cent p.a. in the event of breach and the facts showed that the defendant committed breach, the plaintiff was allowed interest at the specified rate from the date of suit till the date of judgment. He was also allowed interest at 6 per cent till payment as prayed.<sup>392</sup>

### Bank's service charges

As per the terms and conditions of the issue of credit card, the holder of the card had to pay a service charge if he did not pay to the bank within the stipulated time the amount used through the credit. This was held to be not a penalty. The fact that the bank was not complying with certain requirements of the Service Tax Charges Act would not alter the nature of the charge.<sup>393</sup>

### Compensation for giving wrong destination to ship

A charterparty was entered into for carriage of crude oil to destination at an Indian port. The charterer by mistake happened to mention a wrong port where the material could not be landed. The ship arrived there. Lay days for unloading began. The ship was then diverted to the right port. The arbitration award held the charterer liable for excess expenses and delay. The Supreme Court refused to interfere with the award.<sup>394</sup>

### Statutory compensation

Where compensation is payable in terms of a statutory provision, the Supreme Court has held that the provision applicable would be one that is in force at the time of cause of action and not one that was in force at the time of the contract. The plaintiff's husband was killed by a goods lorry which was insured with the defendant insurance company. At the time of the policy, the statutory compensation for loss of life under the Motor

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in plant and mains on which he has to have a reasonable return. He gets a return when energy is actually consumed... but the minimum charges are really a return on his capital outlay incurred for the particular consumer."

391. Y.P. Ganesan v T.N. Civil Supplies Corpn Ltd, (2006) 1 CTC 277 (Mad).

392. Cotton Corpn of India Ltd v Ramkumar Mills (P) Ltd, AIR 2009 NOC 384 (Bom).

393. Central Bank of India v Manipur Vasant Kini, (2000) 1 Mah LJ 744, the suit based on the money used through credit card was allowed as a summary suit.

394. Shipping Corpn of India Ltd v Mare Shipping Inc, (2011) 8 SCC 39: AIR 2011 SC 2608.

Vehicles Act, 1939, was Rs 20,000. By the time of the accident the Act had been amended by raising the compensation money to Rs 50,000. The court allowed the revised figure. This did not amount to retrospective operation, because the accident had taken place after the amendment. The result would have been different if the accident had happened before the amendment or if the parties had contracted only on the basis of law as it then stood.<sup>395</sup>

Where no ceiling was fixed on energy to be consumed by consumers and there was no breach of contract, nor any loss to the supplier, levy of penalty on energy consumed in excess of the contracted demand was held to be illegal.<sup>396</sup>

A *Statutory contract* means that it is a contract with some statutory content which generally contain provisions regarding determination of tariff as per, for example, Section 43-A(2) of the Electricity Supply Act, 1948 regarding determination of tariff. The court was dealing with a power purchase agreement.<sup>397</sup>

### Termination of contract for breach

The Authority was entitled to terminate the contract on any of the specified grounds including delay in execution of the project. The contractor could not complete the work in time. Termination of the contract for this reason was held to be valid. The mere fact that a wrong ground happened to be mentioned in the order of termination did not have the effect of invalidating the order of termination.<sup>398</sup>

### Jurisdiction

A substantial part of the contract remained unexecuted. The textile mills were situated in Bombay and the supply of the goods under the contract was to be made ex-factory at Bombay. Accordingly proceedings could be taken at Bombay.<sup>399</sup>

A ship was mortgaged in a foreign country the court said that under Section 11 of the Admiralty Act, the jurisdiction of the Indian High Courts in admiralty matters is equivalent to that of the High Court in England. Matters as to mortgaged ship can be dealt with by the courts in India provided the mortgage is registered in accordance with the provisions of the Merchant Shipping Act, 1894 or of 1958. This was so. The court therefore, had jurisdiction to try the suit.<sup>400</sup>

395. *Padma Srinivasan v Premier Insurance Co Ltd*, (1982) 1 SCC 613: AIR 1982 SC 836.

396. *Sri Vishnu Cements Ltd v A.P. SEB*, AIR 1999 AP 103.

397. *Indian Thermal Power Ltd v State of M.P.*, (2000) 3 SCC 379: AIR 2000 SC 1005.

398. *K. Pro Infra Works (P) Ltd v State of Manipur*, AIR 2015 NOC 505 (Mani). Information about delay was given to the contractor from time to time, the detailed notice of termination was served. Grounds mentioned by the contractor were considered and rejected.

399. *National Textile Corp Ltd v Haribox Swalram*, (2004) 9 SCC 786: (2004) 3 BC 494.

400. *Dallah Albaraka Investment Co Ltd v MT "Symphony" ex MT Arabian Lady*, (2005) 5 Bom CR 589.

Under the Indian Contract Act this type of relief is provided under Section 75.

**S. 75. Party rightfully rescinding contract entitled to compensation.**—A person who rightfully rescinds a contract is entitled to compensation for any damage which he has sustained through the non-fulfilment of the contract.

*Illustration*

A, a singer, contracts with B, the manager of a theatre, to sing at his theatre for two nights in every week during the next two months, and B engages to pay her 100 rupees for each night's performance. On the sixth night, A wilfully absents herself from the theatre, and B, in consequence, rescinds the contract. B is entitled to claim compensation for the damage which he has sustained through the non-fulfilment of the contract.

A work order for repairing the bank of a river was issued directing the work to be completed within 45 days. The alignment was given after 10 months that turned out to be wrong. Correct alignment was given subsequently when a substantial portion of the work had already been done. The work already done was not taken into account. The wrong alignment became the cause of washing away by devastating floods. The plaintiff's claim for compensation for the work already done was taken to be established.<sup>401</sup>

401. *Raharman Prodhan v State of W.B.*, (2009) 4 CHN 701.

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The following cases from this chapter are available through EBC Explorer™:

- *A.K.A.S. Jamal v Molla Dawood Sons & Co*, (1915–16) 43 IA 6: ILR (1916) 43 Cal 493: (1916) 1 AC 175
- *H. Sowbhagya v NGEF Ltd*, AIR 2004 Kant 155
- *Hadley v Baxendale*, (1854) 9 Exch 341
- *Karsandas H. Thacker v Saran Engg Co Ltd*, AIR 1965 SC 1981
- *Maula Bux v Union of India*, (1969) 2 SCC 554
- *ONGC Ltd v Saw Pipes Ltd*, (2003) 5 SCC 705
- *Shree Hanuman Cotton Mills v Tata Aircraft Ltd*, (1969) 3 SCC 522
- *Tarsem Singh v Sukhminder Singh*, (1998) 3 SCC 471
- *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd*, (1949) 2 KB 528 (CA)



CASE PILOT

## Certain Relations Resembling Those Created by Contract (*Quasi Contracts*)

There are many situations in which law as well as justice require that a certain person be required to conform to an obligation, although he has neither broken any contract nor committed any tort. For example, a person in whose home certain goods have been left by mistake is bound to restore them. Such obligations are generally described, for want of a better or more appropriate name, as *quasi-contractual obligations*.

### Rationale

#### *Theory of unjust enrichment*

The theory on which *quasi-contractual obligations* are based is not yet finally settled. Lord MANSFIELD who is considered to be the real founder of such obligations, explained them on the principle that law as well as justice should try to prevent "unjust enrichment", that is, enrichment of one person at the cost of another. His Lordship offered this explanation in *Moses v Macferlan*.<sup>1</sup>

Jacob issued four promissory notes to Moses and Moses indorsed them to Macferlan, excluding, by a written agreement, his personal liability on the endorsement. Even so Macferlan sued Moses on the endorsement and he was held liable despite the agreement. Moses was thus compelled to discharge a liability which he had excluded and, therefore, sued to recover back his money from Macferlan.

He was allowed to do so. After stating that such money cannot be recovered where the person to whom it is given can "retain it with a safe conscience", Lord MANSFIELD continued:

"But it lies for money paid by mistake; or upon a consideration which happens to fail; or for money got through imposition; or extortion; or oppression; or for an undue advantage taken of the plaintiff's situation, contrary to laws made for the protection of persons under those

1. (1760) 2 Burr 1005, 1012.

circumstances. In one word, the gist of this kind of action is, that the defendant, upon the circumstances of the case, is obliged by ties of natural justice and equity to refund the money."

A liability of this kind is hard to classify. Partly it resembles liability under the law of tort inasmuch as it arises independently of any contract. Partly it resembles contract inasmuch as it is owed only to one party and not "to persons generally". Thus it can be accounted for either under an implied contract or under natural justice and equity for the prevention of unjust enrichment. Lord MANSFIELD preferred the latter theory.

#### *Theory of "implied-in-fact" contract*

But beginning with the decision of the House of Lords in *Sinclair v Brougham*,<sup>2</sup> it became fashionable to discard Lord MANSFIELD'S formulation and to rely upon an implied-in-fact contract.

A building society undertook banking business which was outside its objects and, therefore, *ultra vires*. The society came to be wound up. After paying off all the outside creditors, a mixed sum of money was left which represented partly the shareholders' money and partly that of the *ultra vires* depositors, but was not sufficient to pay both of them. The depositors tried to get priority by resorting to the *quasi-contractual* action for recovery of money had and received for the depositors' benefit, for otherwise the shareholders would be unjustly enriched.

The House of Lords allowed rateable (*pari passu*) distribution of the mixed fund among the claimants, but did not allow any remedy under *quasi-contract*. Lord HALDANE maintained that common law knows personal actions of only two classes, namely, those founded on contract and those founded on tort. "When it speaks of action arising *quasi ex contractu* it refers only to a class of action in theory which is imputed to the defendant by a fiction of law."<sup>3</sup> Similarly, Lord SUMNER observed that an action for money had and received rests, not on a contractual bargain between the parties, but "upon a notional or imputed promise to repay".<sup>4</sup> Lord PARKER expressly pointed out that if a promise to pay back an *ultra vires* loan could be imputed to the company as *quasi-contractual* obligation, the result would be to validate a transaction which has been declared to be void on the ground of public policy and the law would be enforcing a notional contract where an express contract would have been void.<sup>5</sup>

This approach dominated decisions for a long time and the decision was taken to have settled that the juridical basis of *quasi-contract* was the

2. 1914 AC 392 (HL).

3. *Ibid* at p. 415.

4. *Ibid* at p. 452 (HL).

5. *Ibid* at p. 440. The Supreme Court applied the principle of unjust enrichment to cases of imported raw materials captively consumed in manufacture of final produce. *Union of India v Solar Pesticides (P) Ltd*, (2000) 2 SCC 705: AIR 2000 SC 862.

implied, notional or fictional contract. Where the circumstances of a case do not lead to an inference of this kind or where such an inference would be against the law, no liability will arise.

### *Restoration of theory of unjust enrichment*

The identification of *quasi-contracts* with implied contracts restricted the scope of relief which would have been possible without any such hindrance under the principle of “natural justice and equity”. The suffocation was felt by House of Lords itself in *Fibrosa Spolka Akeyjna v Fairbairn Lawson Combe Barbour Ltd*.<sup>6</sup> A sum of money was paid in advance under a contract for the supply of a machine or ‘for the supply of machinery’, and the performance was obstructed by the outbreak of war. Their Lordships allowed the advance to be recovered back as having been paid for a consideration which had wholly failed. Lord WRIGHT lent support to Lord MANSFIELD’s theory of unjust enrichment. He observed:<sup>7</sup>

“It is clear that any civilised system of law is bound to provide remedies for cases of what has been called unjust enrichment or unjust benefit, that is, to prevent a man from retaining the money of, or some benefit derived from, another which it is against conscience that he should keep. Such remedies in English law are generally different from remedies in contract or tort, and are now recognised to fall within a third category of the common law which has been called quasi-contract or restitution.”

Referring to the ratio decidendi of the decision of the House of Lords in *Sinclair v Brougham*<sup>8</sup> Lord WRIGHT pointed out that the case turned upon the principle that it was against public policy to allow the recovery of an *ultra vires* deposit, whether the claim be based upon contract or *quasi-contract*. The observations of their Lordships relating to the foundation of *quasi-contract* were merely *obiter dicta*. Indeed the House adopted the *pari passu* distribution of the available assets as a technique to prevent the unjust enrichment of the shareholders at the cost of the depositors.<sup>9</sup>

### Provisions of the Indian Contract Act

Chapter V of the Indian Contract Act deals with such situations under the heading “Of certain relations resembling those created by contract”. The chapter avoids the words “*quasi-contract*”, and in view of the clear statutory

6. 1943 AC 32 (HL).

7. *Fibrosa Spolka Akeyjna v Fairbairn Lawson Combe Barbour Ltd*, 1943 AC 32 (HL).

8. 1914 AC 392 (HL). *R. Baskar Bhat v Hindustan Petroleum Corp Ltd*, AIR 2002 Mad 330, a lessor not allowed to recover rent except from the date about which there was a proof of delivery of possession.

9. The matter was considered by Lord WRIGHT in his article on the case in 57 LQR 200 and included in his *LEGAL ESSAYS AND ADDRESSEES*, p. 1. Support for this approach is also to be found in Lord ATKIN’S speech in *United Australia Ltd v Barclays Bank Ltd*, 1941 AC 1, 27–29. Lord DENNING has also voiced himself against the implied contract theory. See (1949) LQR 37.

authorisation the courts in India are not hindered in allowing relief under the different sections of Act by the theoretical considerations concerning *quasi-contracts*. But English cases do provide valuable guidance not only as to scope of relief but also as to the way the provisions should be interpreted to keep them in tune with the changing notions of justice. Sections 68 to 72 provide for five kinds of *quasi-contractual* obligation.

### 1. Supply of necessities [S. 68]

Where necessities are supplied to a person who is incompetent to contract or to someone whom he is legally bound to support, the supplier is entitled to recover the price from the property of the incompetent person.<sup>10</sup>

**S. 68. Claim for necessities supplied to person incapable of contracting, or on his account.**—If a person, incapable of entering into a contract or anyone whom he is legally bound to support, is supplied by another person with necessities suited to his condition in life, the person who has furnished such supplies is entitled to be reimbursed from the property of such incapable person.

#### *Illustrations*

- (a) A supplies B, a lunatic, with necessities suitable to his condition in life. A is entitled to be reimbursed from B's property.
- (b) A supplies the wife and children of B, a lunatic, with necessities suitable to their condition in life. A is entitled to be reimbursed from B's property.

### 2. Payment by interested person [S. 69]

**S. 69. Reimbursement of person paying money due by another, in payment of which he is interested.**—A person who is interested in the payment of money which another is bound by law to pay, and who therefore pays it is entitled to be reimbursed by the other.

#### *Illustration*

B holds land in Bengal, on a lease granted by A, the Zamindar. The revenue payable by A to the Government being in arrear, his land is advertised for sale by the Government. Under the revenue law, the consequence of such sale will be the annulment of B's lease. B, to prevent the sale and consequent annulment of his own lease, pays to the Government the sum due from A. A is bound to make good to B the amount so paid.

### Conditions of liability

The conditions of liability under this section may now be stated.

#### *Payer must be interested in making payment*

Firstly, the plaintiff should be interested in making the payment. The interest which the plaintiff seeks to protect must, of course, be legally recognisable. His honest belief that he has an interest to protect is enough.<sup>11</sup>

10. This provision has already been considered in Chapter 4, "Capacity to Contract".

11. So held by the Allahabad High Court in *Munni Bibi v Triloki Nath*, ILR (1932) 54 All 140. The interest in performing one's contract is something different. Accordingly in *Transworld*

Where a party had agreed to purchase certain mills, he was allowed to recover from the seller the amount of already overdue municipal taxes paid by him in order to save the property from being sold in execution. By agreeing to purchase the property he had acquired sufficient interest in it to safeguard.<sup>12</sup> Lord RADCLIFFE refused to agree that the payment in question was voluntary: "The company had contracted to buy these mills, and they were imminently threatened with a forced sale which would, of course, defeat its purchase. Money had to be found for the taxes if the mills were to be saved. The Maharaja (seller) showed no sign of paying the municipality. So the appellant company paid. But to describe it in those circumstances as having made a voluntary payment appears to their Lordships to involve some misuse of language."

Explaining that the purchaser was sufficiently "interested" so as to attract Section 69, his Lordship continued: "In any ordinary use of language the company was interested in the taxes being paid at the time...since only through a payment could it realise the fruit of the contract that it had entered into. The words (of S. 69) themselves do not require that a person to be interested in a payment should at the time have a legal proprietary interest in the property in respect of which the payment is made. It is no doubt true that there have been decisions which have tested whether a person was interested in a payment by ascertaining whether he had such a proprietary interest. It may be a good test in appropriate circumstances. But it would be a bad fallacy to deduce from the circumstance that a person may be interested in payment because he has an interest in the property to which it relates the conclusion that no one who has not any interest in a property can be interested in a payment made in respect of that property. In truth, Section 69 invites no such judicial limitation. The section is part of a Chapter of the Contract Act devoted to 'Quasi-contract'. The phrase itself is no doubt taken from a familiar branch of the English common law, although there is no reason to suppose that the Indian Contract Act was intended to do no more than to reproduce in compendious phrases the precise doctrines of the English law of contract. But the general purport of the section is reasonably clear to afford to a person who pays money in furtherance of some existing interest an indemnity in respect of the payment, against any other person who, rather than he, could have been made liable at law to make the payment."

#### *But should not be bound to pay*

Secondly, it is necessary that the plaintiff himself should not be bound to pay. He should only be interested in making the payment in order to protect his own interest. Where a person is jointly liable with others to pay, a

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*Shipping Services (I) (P) Ltd v Owners*, 1984 SCC OnLine Mad 285: (1986) 99 LW 517 no recovery from the owners of ship was allowed to a person who repaired it under his contract with the charterers.

12. *Govindram Gordhandas Seksaria v State of Gondal*, (1949–50) 77 IA 156: AIR 1950 PC 99.

payment by him of the others' share would not give him a right of recovery under this section.<sup>13</sup> Where a port authority was under a statutory liability to pay an injured workman and paid him, it could not recover from the defendant, a contractor, whose negligence had caused injury, because the port authority was not only "interested" but was also bound in its own independent obligation to pay.<sup>14</sup>

#### *Defendant should be under legal compulsion to pay*

Thirdly, the defendant should have been "bound by law" to pay the money. The words "bound by law" have been held, after some hesitation, to mean bound by law or by contract. It is not necessary that the liability should be only statutory. It is enough that "the defendant at the suit of any person might be compelled to pay".<sup>15</sup> Explaining the purport of the phrase in *Govindram Gordhandas Seksaria v State of Gondal*,<sup>16</sup> where a Maharaja, having sold certain mills without paying overdue municipal taxes, was sued by the buyer who had to pay to save the property from being sold, Lord RADCLIFFE said: "The Maharaja was bound to pay this money in the sense that he made a legally enforceable contract with Seksaria to pay it. Unless the words 'bound by law to pay' where they occur in the section, exclude those obligations of law which arise *inter partes*, whether by contract or by tort, and embrace no more than those public duties which are imposed by statute or general law, the Maharaja was a person from whom reimbursement could be claimed under the section. But their Lordships think that the words extend to any obligation which is an effective bond in law. Certainly the common law of England afforded a right of indemnity to one who had paid 'under compulsion of law' against the true obligor without limiting the circumstances in which the latter's liability had arisen. Certainly, too, there is authority in the courts of India for the proposition that 'bound by law' covers obligations of contract or tort."

Where a person is only morally bound and is not legally compellable to pay, he will not be bound to pay the party discharging his moral obligation. In a case before the Madras High Court, a person had, before his death, gifted certain claims to the defendant. The taxing authorities, however, added the claims to the estate of the deceased and recovered the tax from his

13. *Venkata Simbadri Jagpatiraju v Sri Lakshmi Nrusimha Roopa Sadruannama Arad Dugarazu Dakshina Kavata Dugarazu*, AIR 1916 Mad 980; *Gopinath v Raghuvansh Kumar Singh*, AIR 1949 Pat 522.

14. *Port of the Trust, Madras v Bombay Co (P) Ltd*, AIR 1967 Mad 318. *Urban Improvement Co (P) Ltd v Ujagar Singh*, AIR 1996 P&H 167, increased development charges paid by developer, entitled to recover from purchaser. *Krishna Pillai Rajasekharan Nair v Padmanabha Pillai*, (2004) 12 SCC 754: (2004) 2 ICC 89, subrogation to the position of mortgagee by operation of law. The subrogatee does not become a mortgagee. He only gets certain rights on redeeming the mortgage which include the remedies of redemption, foreclosure and sale. He exercises these rights not as a mortgagee, but by way of rights akin to those of a mortgagee.

15. *Rasappa Pillai v Mitta Zemindar Doraisami Reddiar*, AIR 1925 Mad 1041.

16. (1949-50) 77 IA 156: AIR 1950 PC 99; see also *Raghavan v Alamelu Ammal*, ILR (1907) 31 Mad 35.

widow despite her protests. The widow then sought to recover the amount from the defendant, but he was held not liable. If the taxing authorities had ordered him to pay, only then it could be said that he was bound by law to pay.<sup>17</sup>

### *Payment should be by one to another*

Lastly, the plaintiff should have made the payment to another person and not to himself. "Thus, where a certain Government was the tenant of a land and paid to itself out of the rent due to the landlord the arrears of land revenue due to itself, the Government could not recover from the landlord. It was a transfer of money from one head to another within the Government and not 'payment to another' and though it was done to save the land from being sold in execution, it did not come within the principle of the section."<sup>18</sup>

Goods sent by consigner through a carrier were looted enroute. The entire amount of damage was paid by the insurer to the consignee. It was held that the insurer became entitled to recover reimbursement from the carrier on the basis of the letter of subrogation issued by the consignee to the insurer. The insurer stepped into the shoes of the insured for recovery of the amount."<sup>19</sup>

### 3. Liability to pay for non-gratuitous acts [S. 70]

Section 70 creates liability to pay for the benefits of an act which the doer did not intend to do gratuitously.

**S. 70. Obligation of person enjoying benefit of non-gratuitous act.**—Where a person lawfully does anything for another person, or delivers anything to him, not intending to do so gratuitously, and such other person enjoys the benefit thereof, the latter is bound to make compensation to the former in respect of, or to restore, the thing so done or delivered.

#### *Illustrations*

- A, a tradesman, leaves goods at B's house by mistake. B treats the goods as his own. He is bound to pay A for them.
- A saves B's property from fire. A is not entitled to compensation from B, if, the circumstances show that he intended to act gratuitously.

#### Conditions of liability under the section

GAJENDRAGADKAR J (afterwards CJ) stated in *State of W.B. v B.K. Mondal & Sons*<sup>20</sup> the conditions on which the liability under the section arises:

"It is plain that three conditions must be satisfied before this section can be invoked: (1) a person should lawfully do something for another person or deliver something to him; (2) in doing the said thing or delivering the

17. *Raghavan v Alamelu Ammal*, ILR (1907) 31 Mad 35.

18. *Secy of State for India v Fernandes*, ILR (1906–08) 30 Mad 375.

19. *East India Transport Agency v Oriental Insurance Co Ltd*, AIR 2014 NOC 456 (Chh).

20. AIR 1962 SC 779: 1962 Supp (1) SCR 876.

said thing he must not intend to act gratuitously; and (3) the other person for whom something is done or to whom something is delivered must enjoy the benefit thereof.”

“*Not intending to do so gratuitously*”

Thus, one of the purposes of the section is to assure payment to a person who has done something for another voluntarily and yet with the thought of being paid. He should have contemplated being paid from the very beginning. A Municipal Council which constructed and maintained a bus-stand was allowed to recover some charges from bus operators who used the stand though there was no agreement to that effect.<sup>21</sup> An employer is bound to pay for services rendered by his employees.<sup>22</sup> A university could not escape its liability to reimburse a lecturer who worked under an appointment given to him by the vice-chancellor though the post on which he was appointed was not sanctioned by the State.<sup>23</sup> The words “does anything” would include payment of money. Making payment for another tantamounts to doing something for him. Accordingly, a bank discounting an order of payment and giving credit to the customer was allowed reimbursement from the customer for something done for him.<sup>24</sup> Where a tenant bank overstayed and also did not pay the increased rent which it had acknowledged, the court said:<sup>25</sup> Having regard to the law laid down in various decisions of the Supreme Court and High Courts on the principle of “tenant-holding over” and its consequential effect making the tenant liable to pay damages or mesne profits to the landlord for continuing in possession without any authority of law and similarly in view of the legal position as regards the principle of unjust enrichment under the provisions of Section 70 of the Act, the court came to the inevitable conclusion that the defendant bank was liable to pay the plaintiff the entire amount of the suit claim.

21. *Municipal Council, Rajgarh v M.P. SRTC*, 1991 MPLJ 910. Rs 3 per bus was considered to be quite reasonable. *A. Abu Mohammed v K. M. Mohammed Kunju Labba*, (1994) 2 KLJ 664, amount paid during negotiations for a proposed marriage, proposal fell through, the amount allowed to be recovered back. *Food Corporation of India v Alleppey Municipality*, AIR 1996 Ker 241, services rendered by Municipal Corporation in respect of buildings owned by Central Government, payment is in the nature of compensation under S. 70.
22. *Bihar Nurses Registration Council v Harendra Prasad Sinha*, (1991) 1 PLJR 114: (1991) 2 BLJR 1222.
23. *Shyam Behari Prasad Singh v State of Bihar*, (1991) 2 BLJR 1024.
24. *Federal Bank v Joseph*, (1990) 1 KLT 889.
25. *Bank of India v V. Swaroop Reddy*, AIR 2001 AP 260: (2001) 2 An LT 388; *Syndicate Bank v Seenu Traders*, 1999 AIHC 1876 (Kant), borrower liable to pay interest irrespective of anything else because otherwise he would be enriching himself at the cost of the lender; *B.N. Venkataswamy v P.S. Rukminiamma*, 1999 AIHC 1979 (Kant), interest is recoverable even if there is no provision to that effect in the loan agreement. *Nannapaneni Venkata Rao Coop Sugars Ltd v SBI*, (2003) 6 An LT 199: (2003) 6 ALD 307, amount of loan was required to be kept in SB A/c till utilisation, SB interest allowed on the amount, nothing against it in RBI directions. *Niranjan Das v Orissa SEB*, (2003) 96 Cut LT 528, liability to pay for electricity used after expiry of licence.

The plaintiff was singing for the firm of defendants. Her songs were recorded by them. During the process of recording she did not seem to have acted gratuitously. The defendants enjoyed the benefit of her recordings they commercially marketed the cassettes and CDs of her song recordings. There was no formal contract. Defendants had no right to make any business by use of her performance. The court said that because they did make business use of her work, a *quasi-contract* arose under Section 70 making the defendants liable to pay for her services.<sup>26</sup>

*Section would not encourage officious interference  
in affairs of others*

Secondly, the person for whom the act is done is not bound to pay unless he had the choice to reject the services. "If a person delivers something to another, it would be open to the latter to refuse to accept the thing and to return it; in that case Section 70 would not come into operation. Similarly, if a person does something for another, it would be open to the latter not to accept what has been done by the former; in that case again Section 70 would not apply. In other words, the person said to be liable under Section 70 always has the option not to accept the thing. It is only where he voluntarily accepts the thing or enjoys the work done that the liability under Section 70 arises."<sup>27</sup> In the application of this principle, the courts have had to strike a balance between two factors. One of them being that the rule cannot be used by anybody to make officious interference in the affairs of another.<sup>28</sup> And the other that the court will not compel a person to pay for services which have been thrust upon him against his will. JENKINS CJ, dealing with the scope of Section 70 in *Suchand Ghosal v Balram Mardana*,<sup>29</sup> said:

"The terms of Section 70 are unquestionably wide, but applied with discretion; they enable the courts to do substantial justice in cases where it would be difficult to impute to the persons concerned relations actually created by contract. It is, however, especially incumbent on final courts of fact to be guarded and circumspect in their conclusions and not to countenance acts or payments that are really officious."

*Request for services creates implied promise to pay*

Yet, thirdly, it is necessary that services should have been rendered without any request. Reasonable compensation may, however, be recovered for

26. *Neha Bhasin v Anand Raaj Anand*, (2006) 132 DLT 196; *Charu Bhatnagar v H.P.M.C.*, AIR 2006 HP 119, supplier of fruits allowed to recover price. It was immaterial that he was not mutated owner of the orchard at the time.

27. *Ibid. Haji Adam Sait Dharmastapanam v Hameed*, 1985 KLT 169.

28. *Muthu Raman v Chhima Vellayan*, ILR (1916) 39 Mad 965.

29. ILR (1911) 38 Cal 1.

services rendered at request.<sup>30</sup> This has been so held by the Supreme Court in *State of W.B. v B.K. Mondal & Sons*.<sup>31</sup>

The plaintiff, on the request of an officer of the State of West Bengal, constructed a kutch road, guard-room, office, kitchen, room for clerks and storage sheds for the use of the Civil Supplies Department of the Government. The State accepted the works but tried to escape liability under the pretence that no contract had been concluded in accordance with the requirements of Section 175(3) of the Government of India Act, 1935 (now Article 299 of the Constitution of India). The contractor was thus forced to try his luck with the State under Section 70, and it proved to be better than that of the State but at the cost of fighting up to the Supreme Court for a sum of Rs 19,325.

GAJENDRAGADKAR J (afterwards CJ), examined the conditions of liability under the section and found that they were all satisfied by the facts and, therefore, held the State liable. There was no doubt that the State even after having requested for the works had the right to reject. "It could have called upon the contractor to demolish the storage sheds and take away the material used; but if the State accepted the storage sheds and used them and enjoyed their benefit, then different considerations come into play and Section 70 can be invoked."

Where an item of work in a running contract was changed and the builder worked out that item also but reluctantly and under pressure of the Department, his claim for such additional working was allowed.<sup>32</sup>

30. *Sib Kishore Ghose v Manik Chandra*, (1915) 29 IC 453, lawyers entitled to reasonable fee where none was agreed to. See, however, *Abu Mahommad v Mohd Kunju Lebba*, (1994) 2 KLT 713 where THOMAS J has been of the view that S. 70 indicates that there is no distinction between the grant of a benefit to another on request or a grant without request. In both cases, the person who enjoys the benefit is liable to recompense the grantor. In this case payment was made on demand under a marriage proposal which fizzled out.

31. AIR 1962 SC 779: 1962 Supp (1) SCR 876. Where the goods delivered have been accepted, the remedy is a suit for price and not under this section. *Union of India v Sita Ram Jaiswal*, (1976) 4 SCC 505: AIR 1977 SC 329; *Mir Abdul Jalil v State of W.B.*, AIR 1984 Cal 200, contract without compliance with Article 299. *Civil Engineers (India) v DDA*, (1995) 60 DLT 26, work done by contractor on oral instructions, nothing in writing, work accepted, order of payment by arbitrator valid. *Dinshaw and Dinshaw v Indoswe Engineers (P) Ltd*, AIR 1995 Bom 180: (1995) 3 Bom CR 548, in a building contract, some additional work was done which was not covered by the contract, the other party held liable to pay for such work. Inferior pipes were installed whereas the contract required quality. Payment on the basis of inferior quality ordered. *Union of India v Col. L.S.N. Murthy*, (2006) 4 ALD 368 a person whose contract was void was held entitled to compensation, if he established that the person had enjoyed benefit of things delivered and the delivery was not intended to be gratuitous on appeal, *Union of India v Col. L.S.N. Murthy*, (2012) 1 SCC 718: (2012) 1 SCC (Civ) 368. *National Fertilizers Ltd v Somvir Singh*, (2006) 5 SCC 493: AIR 2006 SC 2319, remuneration already paid to persons whose appointment was not lawful was not allowed to be recovered.

32. *Chief Secy, State of Gujarat v Kothari & Associates*, (2003) 1 GCD 372 (Guj). *Municipal Committee, Pundri v Bajrang Rao Nagrath*, AIR 2006 P&H 142, work carried out by the contractor on oral request of the Councillor, Municipality benefited by it, liability to pay arose. *Gopal Chandra Bhui v Bankura Zilla Parishad*, 2015 SCC OnLine Cal 261: AIR 2015 Cal 124, a tender for construction of pucca sech nala involved additional excavation of a

*Non-compliance of constitutional requirements  
of contracting with State*

The learned judge had still to face the mighty argument that the statutory formalities of contracting with the State had not been observed and that the enforcement of any such contract would defeat the relevant statute. This difficulty was got over by holding that what was sought to be enforced was not a contract, but a relation resembling those created by a contract. Thus, in cases falling under Section 70 the person doing something for another cannot sue for specific performance, nor ask for damages for breach and this for the simple reason that there is no contract between the parties. All that Section 70 provides for is that if the services or goods are accepted a liability to pay arises. The mandatory provisions of Section 175(3) of the Government of India Act, 1935, could be said to be circumvented only if a contract not fulfilling the requirements were to be enforced, and not when a claim was enforced under Section 70 which arises not by virtue of any contract but rather by reason of the fact that the work has been done by one party and enjoyed by the other without any contract at all. The mere act of construction and its acceptance by the State cannot be said to contravene the provisions of Section 175(3). "Once it is realised that a cause of action for a claim for compensation under Section 70 is based not upon the delivery of the goods or the doing of any work as such but upon the acceptance and enjoyment of the said goods or said work, it would not be difficult to hold that Section 70 does not treat as valid the contravention of Section 175(3) of the Act. That being so, the argument that the respondent's construction of Section 70 nullifies the effect of Section 175(3) of the Act cannot be accepted." "Any other approach would not only cause injustice to a private party, but would also hamper Government business." "It is well known that in functioning of the vast organisation represented by a modern State, Government officers have invariably to enter into a variety of contracts which are often of a petty nature. Sometimes they have to act in emergency, and on many occasions, in pursuit of the welfare policy of the State, the Government officers may have to contract orally or through correspondence, without complying with the provisions of Section 175(3). If, in all these cases, what is done in pursuance of the contract is on behalf of the Government and for their use and enjoyment and is otherwise legitimate and proper, Section 70 would step in and support a claim for compensation made by the contracting parties notwithstanding the fact that the contracts had not been made as required by Section 175(3). ... We are referring to this aspect of the matter not with a view to detract from the binding character of

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large heap of earth. This was done by the contractor on verbal instructions of the Authority. For this extra work of gratuitous nature the contractor became entitled to compensation. He claimed an amount which appeared to be exorbitant. The case was remanded back to the trial court for determination of amount payable.

the provisions of Section 175(3), but to point out that like ordinary citizens even the State Government is subject to the provisions of Section 70.”

The court also laid down that the position of the State cannot be compared with that of a minor. “The minor is excluded from the operation of Section 70 for the reason that his case has been specifically provided for by Section 68. What Section 70 prevents is unjust enrichment and it applies as much to corporations and Government as to individuals .... Besides, in the case of a minor, even the voluntary acceptance of the benefit of the work done or thing delivered, which is the foundation of the claim under Section 70, would not be present and so, on principle, Section 70 cannot be invoked against a minor.”<sup>33</sup>

The principle of this case has been reaffirmed by the Supreme Court in *Piloo Dhunjishaw Sidhuwa v Municipal Corp of City of Poona*.<sup>34</sup> Here too the Corporation tried to escape liability for spare motor parts supplied to it on the ground that the contract was not made in accordance with the Bombay Municipal Corporation Act (59 of 1949). But the Corporation was held liable to pay under Section 70. The only question was what should be the measure of compensation. SHAH J (afterwards CJ) cited with approval the decision of the Lahore High Court in *Secy of State v G.T. Sarin & Co*<sup>35</sup> where it was held that “a person without an enforceable contract in his favour supplying goods to a Government Department is entitled to a money equivalent of the goods delivered, assessed at the market rate prevailing on the date on which the supplies were made”. In the present case the rates quoted by the supplier in his invoice were considered to be the fair measure of compensation giving the State the right to show that the market price was less than that, but the Corporation did nothing in this respect.<sup>36</sup> Thus, though the claim under Section 70 is not based upon any contract, yet the contract between the parties is relevant at least for indicating the fair measure of compensation.

#### *Recovery under Oral or non-provable contracts*

A highway work was allotted on emergency basis. The cost of work was sanctioned by the superintending engineer. But no allocation of funds was made. The work was completed. It was held that the state could not leave the

33. Followed in *New Marine Coal Co v Union of India*, AIR 1964 SC 152: (1964) 2 SCR 859; *Mulamchand v State of M.P.*, AIR 1968 SC 1218: (1968) 3 SCR 214, where no restitution was allowed because the plaintiff could not prove what work he had done for the Government; *Mangi Lal v Mewar Textile Mills Staff Consumers Coop Society Ltd*, 1985 Raj LR 274, the cost of construction of canteen was allowed to be recovered when because of the violation of the canteen allotment rules, the canteen was taken over by the State.

34. (1970) 1 SCC 213: AIR 1970 SC 1201.

35. ILR (1930) 11 Lah 375.

36. Again followed in *Pannalal v Commr*, (1973) 1 SCC 639, where the State was held liable to pay for the construction of a hospital. See at p. 643. An executory contract not complying with the statutory requirements cannot be enforced. *Karamshi Jethabhai Somayya v State of Bombay*, AIR 1964 SC 1714: (1964) 6 SCR 984.

contractor high and dry. The statement compensate him. The work was not supposed to have been done on gratuitous basis. The amount as sanctioned and recommended must be paid. Such a claimant should not be compelled to go into litigation. Technicalities should not come in the way of substantive work.<sup>37</sup>

The Supreme Court has further held that where a contractor whose work has been accepted by the other party claims compensation under an oral agreement, which he is not able to prove, he would still be entitled to compensation under Section 70.<sup>38</sup> In another case,<sup>39</sup> the Supreme Court held the Government liable to a person who, on the instructions of the Government, transferred the steel allotted to him in excess to a third person who failed to pay.

#### *Work done after termination of contract*

Anything done after the termination of a contract would come within the scope of Section 70.<sup>40</sup>

#### *Contracts void under Article 299*

Recovery under the section is possible even if there was no contract or the contract was void under Article 299 of the Constitution.<sup>41</sup> Thus the Government was allowed to recover the cost of training from a candidate who refused to join the Government service. The Government could have waived but there was no evidence of waiver. He was sent on training on his agreeing to serve the Government. He could not say that no advantage came to him from the training.<sup>42</sup> It has been held that salary or pension which happens to be wrongfully paid is recoverable. This is so irrespective of the fact whether the payment was made either by reason of misrepresentation or fraud or otherwise.<sup>43</sup>

It is not necessary that services should have been rendered under circumstances of pressing emergency.<sup>44</sup>

37. *Ram Pravesh Prasad v State of Bihar*, AIR 2007 Pat 26; *Pampara Philip v Koorithottiyil Kinhimohammed*, AIR 2007 Ker 69, the buyer of a motor can misinformed about the year of the model, he was allowed to recover back the advance money paid by him, he had used the vehicle for more than a month for which he was required to pay Rs 100 per day to the seller.

38. *V.R. Subramanyam v B. Thayappa*, AIR 1966 SC 1034: (1961) 3 SCR 663. The position, therefore, is that S. 70 does not require a contract. A person who purchased the equity of redemption and saved the property from being sold out was allowed to recover proportionate reimbursement from his co-owner. *Asaar Ali Khan v Baijnath Prasad*, AIR 1983 All 197. No relief can be allowed under this section where there is neither contract nor any other service. *Devi Sahai Palliwal v Union of India*, (1976) 4 SCC 763.

39. *Union of India v J.K. Gas Plant*, (1980) 3 SCC 469; AIR 1980 SC 1330.

40. *Food Corporation of India v Gopal Chandra Mukherjee*, (2003) 2 ICC 797 (Cal).

41. *Anil Harish v Govt of Maharashtra*, (2004) 6 Bom CR 322, the Government secretary was not authorised to enter into lease deed on behalf of the Government. Lease was also not in writing. Art. 299 not complied with.

42. *P.C. Wadhwa v State of Punjab*, AIR 1987 P&H 117.

43. *State of Punjab v Rafiq Masih*, (2014) 8 SCC 883.

44. *Damodara Mudaliar v Secy of State for India*, ILR (1895) 18 Mad 88.

### *"Lawfully does"*

Fourthly, services should have been rendered lawfully. Commenting upon this in *State of W.B. v B.K. Mondal & Sons*,<sup>45</sup> the Supreme Court has said that the word "lawfully" is not a surplusage and must be treated as an integral part of Section 70 and even if it is taken to refer to an object of consideration which is forbidden by Section 23 of the Contract Act, it cannot be taken to mean as requiring the State to pay under Section 70 for the services which it has enjoyed was something forbidden by Section 175(3) of the Government of India Act, 1935. Payment for extra work done in connection with a contract without any agreement has been allowed to be recovered under this section.<sup>46</sup>

It has been a point of emphasis that between the person claiming compensation and the person against whom it is claimed, some lawful relationship must exist, and it should arise by reason of the fact that what has been done for the former has been accepted and enjoyed by the latter. Acting on this, the Orissa High Court allowed a person to recover what he had paid to another for purchasing his paddy not knowing at the time that his purchase was in violation of a State Control Order.<sup>47</sup> Where a lady Advocate accepted the request of the District Magistrate and rendered services as an Assistant District Counsel for a certain period, she was allowed to retain the remuneration already received and also to recover the remaining remuneration for the period of service even if her appointment was found to be void under Section 24(2) of the Criminal Procedure Code, 1973.<sup>48</sup>

Where a teacher due for retirement at the age of 55 obtained a stay order contending that he was entitled to continue up to 60 and remained in service beyond 55 before the matter was decided against him, he was allowed to recover the monetary benefits of his entitlement for the overlapping period. His conduct was not unlawful. He remained in service not by usurpation but under superior orders.<sup>49</sup>

### *Non-gratuitous acts*

In the fifth place, the person rendering services should not have intended to act gratuitously. The decision of the Madras High Court in *Damodara Mudaliar v Secy of State for India*<sup>50</sup> is the leading authority.

A number of villages were drawing irrigation waters from a tank. Some of the villages were under direct State tenancy, others under *Zamindars*.

45. AIR 1962 SC 779: 1962 Supp (1) SCR 876.

46. *State of U.P. v Chandra Gupta & Co*; AIR 1977 All 28.

47. *Fakir Chand Seth v Dambarudhar Bania*, AIR 1987 Ori 50.

48. *Indu Mehta v State of U.P.*, AIR 1987 All 309.

49. *Ramakrishnan Nair v State of Kerala*, (1989) 2 KLJ 100. *Ashwani Kumar v State*, AIR 2015 J&K 99, auction amount was deposited for all the 12 months of the year. The bidder could not recover anything for a part of the year because the State collected the amount itself. He was allowed proportional refund out of the money deposited.

50. ILR (1895) 18 Mad 88.

The Government carried out repairs to the tank for its preservation. The Zamindars also enjoyed the benefits of the repairs.

They were accordingly held liable to make proportional contribution towards the expenses of repair. The case shows that even where the party making payment or rendering services is personally interested in the matter, he can recover proportional contribution from those who have enjoyed the benefits of his services. Similarly, where the owners of a *hat* were required at the pain of termination of their licence to make certain improvements in the *hat*, one of them who carried out the improvements recovered compensation from his co-owners.<sup>51</sup>

#### *Lender of money*

A party admitted receipt of money as a loan. The transaction was oral, wholly dependent upon the faith reposed by the lender. The circumstances showed it to be a contract of loan. The court said that it could direct the borrower to pay back the money at appropriate interest. It was not material that there was no stamped paper acknowledging receipt of money.<sup>52</sup>

“ENJOYS THE BENEFIT.”—Lastly, the defendant must have derived a direct benefit from the payment or services. Where the works done by a railway company developed the adjoining lands and consequently the municipality received more taxes, this was held to be not a sufficient benefit to enable the railway company to recover compensation from the municipality.<sup>53</sup>

Services rendered to a person incompetent to contract at the time cannot be made the basis of an action under this section.<sup>54</sup>

Similarly, where no services have been rendered at all, for example, where the Government cancelled a lease granted to the plaintiff by an officer who was not so authorised, no relief can be allowed under the section.<sup>55</sup> Where

51. *Jarao Kumari v Basanta Kumar Roy*, ILR (1905) 32 Cal 374.

52. *Narayan Venkatesh Pandit v Syed Nuroddin Khadri*, (1999) 2 Kant LJ 449. *Nannapaneni Venkata Rao Coop Sugars Ltd v SBI*, (2003) 6 An LT 199: (2003) 6 ALD 307, money left with bank under a share deposit scheme, interest became payable notwithstanding the RBI directive that no interest would be paid on Savings Bank Accounts. The account in question did not come into the category of SB account.

53. *Governor General in Council v Madura Municipality*, (1947–48) 75 IA 213: AIR 1949 PC 39. See also the decision of the Supreme Court in *Srinivas & Co v Inden Biselers*, (1971) 3 SCC 725: AIR 1971 SC 2224. Advance payment for purchasing paddy in ignorance of control order allowed to be recovered because the payee had the benefit of the payment. *Fakir Chand Seth v Dambarudhar Bania*, AIR 1987 Ori 50.

54. *Ambika Textiles Ltd, re*, AIR 1950 Cal 491.

55. *Kirorilal v State of M.P.*, AIR 1977 Raj 101. Payments made and accepted under an express contract did not attract S. 70 although the parties were mistaken about the distance. *Kochu Devassey v State of Kerala*, AIR 1982 Ker LR 180. Person claiming restitution under the section has to offer proof of the work done by him: *Mulamchand v State of M.P.*, AIR 1968 SC 1218: (1968) 3 SCR 214. The section was not applied to the case of a person who was not party to the transaction though he was the beneficiary, *Paidi Lakshmayya v Indian Bank Ltd*, AIR 1982 Kant 338. *Aeries Advertising Bureau v C.T. Devaraj*, (1995) 3 SCC 250: AIR 1995 SC 2251, no liability of the financier only because he approved the advertisement for the circus. He derived no benefit. *Sangamesh Printing Press v Taluk Development Board*, (1999)

a road building contractor claimed an extra amount for the reason that he had to spend more on the haulage of material than expected but he had been told at the time of contracting to take care of all possibilities, the court said that any disadvantage suffered by the contractor during the execution of the work could not be made a ground of making an additional claim over and above the contract rates.<sup>56</sup>

### *Provision for refund of price*

A clause in a contract stipulated for reimbursement of the price of goods which had already been paid in case of delayed delivery or delayed arrival or non-delivery. The clause was held to be valid. Even in the absence of such a clause, the price would have been refundable for failure to deliver.<sup>57</sup> Where a part payment was made by way of purchase price and not as an earnest money, it could not be forfeited. In such a case, the remedy by way of damages for breach of contract is available.<sup>58</sup> Where the contracting process had been completed by acceptance of the bid at an auction but the bidder did not sign the agreement papers saying that it had become impossible for him to perform, the court said that this could not be regarded as a frustration of the contract and therefore forfeiture of the security deposit in accordance with the applicable rules was proper.<sup>59</sup>

### *Appropriate pleadings*

It has been held that absence of pleadings to the effect that the transaction between the parties did not involve any contract or involved a contract which was not valid, the plaintiff would not be entitled to take aid of Section 70.<sup>60</sup>

#### *4. Finder of goods [S. 71]*

Section 71 lays down the responsibility of a finder of goods.

**S. 71. Responsibility of finder of goods.**—A person who finds goods belonging to another and takes them into his custody, is subject to the same responsibility as a bailee.

Thus in respect of duties and liabilities a finder is treated at a par with bailee. The finder's position, therefore, has been considered along with bailment.

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6 SCC 44, the case under the section was not canvassed before the High Court at appeal stage, but there were findings of fact by the trial court and those could be used for considering the claim at the High Court level.

56. *State of Karnataka v Stellar Construction Co*, AIR 2002 Kant 6; (2002) 5 Kant LJ 474.

57. *Phulchand Exports (P) Ltd.v O.O.O. Patriot*, (2011) 10 SCC 300. *Satish Batra v Sudhir Rawal*, (2013) 1 SCC 345; (2013) 1 SCC (Civ) 483, purchaser of property of Rs 70,00,000 deposited Rs 7,00,000 as earnest money. The whole of this amount was allowed to be forfeited on his failure to complete the purchase.

58. *Satish Batra v Sudhir Rawal*, (2013) 1 SCC 345; (2013) 1 SCC (Civ) 483.

59. *Mary v State of Kerala*, (2014) 14 SCC 272; (2013) 4 KLT 466.

60. *Kishanlal Panch v State of Orissa*, AIR 2010 NOC 535 (Ori).

The Supreme Court has ruled in *Union of India v Amar Singh*<sup>61</sup> that the statutory fiction by which a contract of bailment is inferred between a finder of goods and the real owner should not be enlarged by analogy or otherwise and, therefore, a railway authority which took into its custody wagons containing the plaintiff's goods and which were left across the border in Pakistan became the contractual bailees of goods, and it was not necessary to regard them as finders within the meaning of Section 70.

### 5. Mistake or coercion [S. 72]

Section 72 deals with payments made or things delivered under mistake or coercion.

**S. 72. Liability of person to whom money is paid, or thing delivered, by mistake or under coercion.**—A person to whom money has been paid, or anything delivered, by mistake or under coercion, must repay or return it.

#### *Illustrations*

- (a) A and B jointly owe 100 rupees to C. A alone pays the amount to C, and B, not knowing this fact, pays 100 rupees over again to C. C is bound to repay the amount to B.
- (b) A railway company refuses to deliver up certain goods to the consignee, except upon the payment of an illegal charge for carriage. The consignee pays the sum charged in order to obtain the goods. He is entitled to recover so much of the charge as was illegally excessive.

#### *Mistake of fact or of law*

Money paid under mistake is recoverable whether the mistake be of fact or of law.<sup>62</sup> The controversy between High Court decisions as to whether money paid under mistake of law could be recovered was set at rest by the Privy Council in *Sri Sri Shiba Prasad Singh v Maharaja Srish Chandra Nandi*.<sup>63</sup>

"Payment 'by mistake' in Section 72 must refer to a payment which was not legally due and which could not have been enforced; the 'mistake' is on thinking that the money paid was due when, in fact, it was not due. There is nothing inconsistent in enacting on the other hand that if parties enter into a contract under mistake in law that contract must stand and

61. AIR 1960 SC 233: (1960) 2 SCR 75.

62. Expressly so held by the Privy Council in *Sri Sri Shiba Prasad Singh v Maharaja Srish Chandra Nandi*, (1948–49) 76 IA 244: AIR 1949 PC 297. See also *J&K Bank Ltd v Attar-ul-Nisa*, AIR 1967 SC 540: (1967) 1 SCR 792, money credited by a bank under Government Orders to the account of a customer by mistake, not allowed to be recovered under the section. Similarly, sales tax paid by a Government in pursuance of a contract was not allowed to be recovered. *Union of India v Lal Chand & Sons*, AIR 1967 Cal 310.

63. (1948–49) 76 IA 244: AIR 1949 PC 297. In *Wolf & Sons v Dadybha Khimji & Co*, ILR (1919) 44 Bom 631, the Bombay High Court and in *A.M. Appavoo Chettiar v South Indian Rly Co*, AIR 1929 Mad 177, the Madras High Court had held as influenced by S. 21 and English Law that S. 72 could not apply to payments made under mistake of law, whereas the Calcutta High Court in *Jagadish Prosad Pannalal v Produce Exchange Corpn Ltd*, ILR (1945) 2 Cal 41: AIR 1946 Cal 245 had taken the contrary view.

is enforceable, but, on the other hand, that if one party acting under mistake of law pays to another party money which is not due by contract or otherwise, that money must be repaid. Moreover, if the argument based on inconsistency with Section 21 were valid, a similar argument based on inconsistency with Section 22 would be valid and would lead to the conclusion that Section 72 does not even apply to mistake of fact.... It may be well to add that their Lordships' judgment does not imply that every sum paid under mistake is recoverable, no matter what the circumstances may be. There may in a particular case be circumstances which disentitle a plaintiff by estoppel or otherwise."

#### *Refund of tax money paid without being due*

The Supreme Court in its decision in *STO v Kanhaiya Lal Mukund Lal Saraf*<sup>64</sup> has accepted this interpretation of Section 72.

A certain amount of sales tax was paid by a firm under the U.P. Sales Tax law on its forward transactions and subsequently to the payment, the Allahabad High Court ruled the levy of sales tax on such transactions to be *ultra vires*.<sup>65</sup> The firm sought to recover back the tax money.

Rejecting the contention based on English, American and Australian laws which do not allow payments made under mistake of law to be recovered, the Supreme Court allowed the recovery. "The section in terms does not make any distinction between a mistake of law or a mistake of fact. The term 'mistake' has been used without any qualification or limitation whatever...."<sup>66</sup> The court found no ground for any estoppel against the firm and disapproved the following statement of the Nagpur High Court.<sup>67</sup> "If the reason for the rule is that a person paying money under mistake is entitled to recover it, because it is against the conscience of the receiver to retain it, then when the receiver has no longer the money with him or cannot be considered as still having it, as in a case where he has spent it on his own purposes, different consideration must necessarily arise."

In reference to this, the Supreme Court said that "no such equitable consideration can be imported when the terms of Section 72 are clear and unambiguous".

If a mistake either of law or of fact is established, the assessee is entitled to recover the money and the party receiving it is bound to return it irrespective of any other consideration. Money paid under a mistake of law comes

64. AIR 1959 SC 135: 1959 SCR 1350. *Masand Transport v Addl Transport Commr*, (1996) 4 AIHC 3556, reassessment, original demand lapsed being impliedly struck down by reassessment, taxpayer entitled to refund.

65. Vide *Budh Prakash Jai Prakash v STO*, 1952 All LJ 322; confirmed by the Supreme Court, (1955) 1 SCR 143. *Somaiya Organics (India) Ltd v State of U.P.*, (2001) 5 SCC 519: AIR 2001 SC 1723, the principle of unjust enrichment cannot be extended to give a right to the State to recover or realise vend fee after the statute has been struck down.

66. BHAGWATI J, 1959 SCR 1359, 1364.

67. In *Nagorao Govindrao Ayachit v Governor-General in Council*, AIR 1951 Nag 372, 374.

within "mistake" in Section 72 of the Contract Act and there is no question of estoppel when the mistake of law is common to both the assessee and the taxing authority.<sup>68</sup>

• *Scope of the word "mistake" in context of overpaid taxes*

The scope of the word "mistake" has been further exemplified by the Supreme Court in *Tilokchand Motichand v H.B. Munshi*.<sup>69</sup>

A firm paid sales tax of more than twenty-six thousand rupees in respect of sales to consumers outside the State of Bombay and which were, therefore, not liable to any sales tax. The firm had itself collected the tax money from its customers. The amount was ordered to be refunded. A cheque was given to the firm subject to the condition that within one month it should produce receipts from the customers outside Bombay showing that the refund in question had been passed over to them. The firm failed to do so and was, therefore, informed to return the tax money to the State failing which it would be recovered as arrears of land revenue. The firm petitioned to the Bombay High Court but lost it. It paid back the amount only when it received an order of attachment. When all this was going on but unknown to the firm, the Act under which the recovery was made from the firm had been declared by the Supreme Court to be *ultra vires*.<sup>70</sup> The firm sought to recover back the money as having been paid under either mistake of law or coercion.

The court adopted the view of "mistake" which had been taken in the earlier Privy Council and Supreme Court decisions to the effect that the word means mistake in thinking that the money was due when in fact it was not due and held that the firm in this case did not suffer from any such mistake. The firm fully appreciated the legal position and knew that the

68. *CST v Auriaya Chamber of Commerce*, (1986) 3 SCC 50: AIR 1986 SC 1556. Such relief can be had by means of a writ under Art. 226 of the Constitution and regular suit would not be needed. There should not have been any laches. See *Shiv Shankar Dal Mills v State of Haryana*, (1980) 2 SCC 437: AIR 1980 SC 1037; *Shri Vallabh Glass Works Ltd v Union of India*, (1984) 3 SCC 362: AIR 1984 SC 971; *Salonah Tea Co Ltd v Supt of Taxes*, (1988) 1 SCC 401: AIR 1990 SC 772; *Tilokchand Motichand v H.B. Munshi*, (1969) 1 SCC 110: AIR 1970 SC 898; *Mahabir Kishore v State of M.P.*, (1989) 4 SCC 1: AIR 1990 SC 313; *Union of India v Straw Products*, (1989) 2 Ori LR 356. Payment of taxes under an unconstitutional Act allowed to be recovered. *Kamalpur (Assam) Tea Estate (P) Ltd v Supt of Taxes*, (1988) 1 Gau LR 290. Refund of octroi illegally recovered. *Dharangadhra Municipality v Dharangadhra Chemical Works Ltd*, (1988) 1 GLH 324. Such refunds are allowable even if the relevant statute provides that there shall be no refund of mistaken payments. See *Mamta Drinks and Industries v Union of India*, (1990) 70 Cut LT 423. Remedy by way of writ would not, however, be available where taxes are not involved, or there is no other unconstitutional conduct and the dispute is about ordinary trade terms even if one of the parties is a Government. *Chandrika v D.R.M., Southern Rly*, (1985) 1 MLJ 369. Water charges paid under a rule which was struck down. Claim for refund was filed after the expiry of a reasonable period, not allowed, *Municipal Corpn of Greater Bombay v Bombay Tyres International Ltd*, (1998) 4 SCC 100: AIR 1998 SC 1629: (1998) 1 An LD 1.

69. (1969) 1 SCC 110: AIR 1970 SC 898.

70. Vide *Kanti Lal Babulal v H.C. Patel*, AIR 1968 SC 445: (1968) 1 SCR 735.

money was in fact due until the statute under which recovery was made was declared to be *ultra vires*. The court, however, held that the payment was made under coercion and would have been recoverable under Section 72, had it not been for the expiry of the period of limitation. MITTER J who spoke for the majority, held that the three years' period which was available in this case for filing a suit for refund began to run from the date on which the Act came into force and the petition was filed after more than three years from that date. HEGDE J rightly dissented from this aspect of the majority view. According to him time should begin to run from the date on which the Act was ultimately declared to be void and the petition was filed very soon thereafter.<sup>71</sup> But it seems that justice lay in the majority view, for, as between the firm and the State, the latter was better entitled to the money which belonged not to the firm but to its customers.<sup>72</sup>

Where subsequently to the payment of excise duty the Excise Commissioner declared that no duty was payable on those goods, it was held that the plaintiff's claim to refund could not be defeated on the ground that the refund would unjustly enrich him.<sup>73</sup> This should be contrasted with a decision of the Andhra Pradesh High Court.<sup>74</sup> Fee collected from consumers on the

71. Where the statute is unconstitutional and, therefore, refund is allowable under Art. 226, not the period of limitation, but the doctrine of laches would apply. *Finolex Cables Ltd v Union of India*, (1988) 35 ELT 343 (Bom). Where, on the other hand, the Act is valid but the payment is mistaken and recovery is allowable under S. 72, the general law of limitation would apply. *Mamta Drinks and Industries v Union of India*, (1990) 70 Cut LT 423, 427-28. It was held that the period of limitation would run not from the date of judgment but from the date of the petitioner's knowledge. *Maruthy Enterprises v Corpn of City of Bangalore*, AIR 1999 Kant 41, where overpaid property tax was held to be refundable to the extent of the amount paid within the preceding three years, the rest became time-barred.
72. In *Newabganj Sugar Mills Co Ltd v Union of India*, (1976) 1 SCC 120: AIR 1976 SC 1152, refund allowed with a scheme for assuring refund to those who had paid the tax money to the assessee firm; *Shiv Shankar Dal Mills v State of Haryana*, (1980) 2 SCC 437: AIR 1980 SC 1037, refund money ordered to be paid over to payers; *U.P. SEB v City Board, Mussoorie*, (1985) 2 SCC 16: AIR 1985 SC 883.
73. R. Parthasarthy v Dipsi Chemicals, 1987 Mah LJ 900; *Agra Beverages Corpn Ltd v Union of India*, (1988) 18 ECR 261: (1988) 34 ELT 465 (All). The Supreme Court has again reiterated in *Commlr, Andaman v Consumer Coop Stores Ltd*, (1999) 1 SCC 507: AIR 1999 SC 696 that the State should not resist the demand for refund of tax money (excise in this case) on the ground of unjust enrichment, where the money has been illegally collected from the taxpayer. *Mafatlal Industries Ltd v Union of India*, (1997) 5 SCC 536, a person claiming restitution must show that he has suffered loss or injury. If the assessee has passed on the tax burden to third persons, a suit for refund on the ground of payment under mistake of law would not be maintainable. The dissenting judge (SEN J) was of the view that even in such cases refund should be allowed. *Pfizer Ltd v Union of India*, (1996) 4 Bom CR 119, claim for refund of excise duty paid under mistake on an item which was exempt, exemption was subject to certain conditions, held, without proof of compliance with those conditions, refund could not be claimed.
74. N.V. Ramaiah v State of A.P., AIR 1986 AP 361. Also to the same effect, *Dharangadhra Municipality v Dharangadhra Chemical Works Ltd*, (1988) 1 Guj LH 324, illegal octroi. Followed in *Union of India v Wood Papers Ltd*, (1989) 2 Guj LR 1323 with this observation that no recovery can be allowed to a person who has suffered no loss. Accordingly, taxes illegally collected and paid over to the State not allowed to be recovered by a dealer who was not in a position to refund to his customers. Also following *State of M.P. v Vyankatlal*, (1985) 2 SCC 544: AIR 1985 SC 901. Refund is allowed prospectively from the date of judgment

sale of denatured spirit and paid into the Government account, though the fee was illegal, the amount paid under it was not allowed to be recovered back because it would have gone to enrich the seller at the cost of the various buyers whom he would not have been able to pay back. As against this recovery was allowed to a person who was compelled without authority to pay Rs 5 per quintal on the food exported by him under his export licence, the source of payment being his own pocket and not the money collected from customers.<sup>75</sup>

### Excess stamp duty

Excess stamp duty happened to be paid voluntarily under some mistake. The court said that it had to be refunded even though the payment was wholly voluntary. An application for refund was also made as required by the Bombay Stamp Act, 1958.<sup>76</sup>

### Limitation and latches

Recovery proceedings generally are instituted by way of writ petition. There is no period of limitation applicable to writs. The only requirement is that there should not be unreasonable delay amounting to laches. It has been held that the period of limitation would not begin to run until the applicant has discovered the mistake or could have discovered it with reasonable diligence. The claim was laid within one month of the mistake of law becoming known. It was held that the claim could not be defeated on the ground of limitation.<sup>77</sup>

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declaring the levy to be unconstitutional. *Kesoram Industries Ltd v Coal India Ltd*, AIR 1993 Cal 78. No refund was allowed where proof was not offered of the fact that the incidence of the excise duty was not passed off to the buyers of the goods. *Union of India v ITC Ltd*, 1993 Supp (4) SCC 326: AIR 1993 SC 2135, distinguishing *Tata Engg and Locomotive Co Ltd v Municipal Corpns, Thane*, 1993 Supp (1) SCC 361: because in this case there was material on record that Telco had not recovered the amount paid by them by way of octroi duty from any third person. Also to the same effect, *Birla Cement Works v State of Punjab*, AIR 1993 P&H 274, octroi ordered to be refunded because the goods were taken out of the State. *Sharma Transport v State of Karnataka*, (2005) AIR Kant 94: 2005 AIHC 583, levy and collection of cess on motor vehicles was found to be illegal, the amount was passed to the travelling public by vehicle operators, order of refund not to be passed. *Municipal Corpns, Kota v J. K. Synthetics Ltd*, AIR 2008 NOC 1123 (Raj), octroi duty paid, not refunded because the payer had collected the amount from the purchaser.

75. *State v Bansilal Chatarlal*, 1985 Raj LR 325. The Bombay decision to the same effect is in *Garware Plastics & Polyester Ltd v Municipal Corpns of Aurangabad*, AIR 1999 Bom 431, octroi duty was paid and there was a claim for refund. The claimant did not plead that the amount paid was not added to the cost of the product and, therefore, was not passed on to buyers. He was not allowed to claim refund. *Shree Digvijay Cement Co Ltd v Union of India*, (2003) 2 SCC 614: AIR 2003 SC 767, no refund allowed where the burden of the tax had already been passed on to customers. *Alco Chem Ltd v Hyderabad Chemical Pharmaceutical Works Ltd*, (2003) 3 BC 508 (AP), no refund of tax amount which was paid after collecting from others. For further study see Meena H. Rao, *Refund of Tax Paid under Mistake of Law*, 1993 Tax LR 505 (Journal Section).

76. *Hitesh D. Desai v Supt of Stamps and Inspector General of Registration*, AIR 2016 Guj 62.

77. *Chrisine Hoden (P) India Ltd v N. D. Gadag*, (1993) 2 Bom CR 169.

A petition was filed for refund of extra property tax paid under mistake. The petitioner failed to explain the delay and latches in approaching the court. The fact that he received belated advice was not considered to be sufficient. The fact that the money was utilised by the municipal corporation for the welfare of the people was held to be no defence. The court restricted recovery of overpayment to the preceding three years and not for the whole period.<sup>78</sup>

### *Some other examples of mistake*

Another obvious case is a mistaken credit entry in a customer's account in a bank and the customer withdrawing the amount. He would be bound to pay back the amount along with interest under the Interest Act.<sup>79</sup> Where rice-millers were paid an amount in excess of the agreed rate because of a mistake in classification according to quality, they were required to disgorge the unjust enrichment.<sup>80</sup>

Where a sum of money was paid to a bank as a price of the goods and the bank issued delivery orders which were not accepted by the warehouse-keeper, the Calcutta High Court held that this was not a payment under mistake and Section 72 was not applicable.<sup>81</sup> Where the railway authorities charged extra fare under the mistaken belief that the goods would have to be carried by a longer route, they were ordered to refund the extra fare.<sup>82</sup> Where the vendor of mortgaged property allowed the purchaser to retain

78. *Maruthy Enterprises v Corpn of City of Bangalore*, AIR 1999 Kant 41. *Confederation of Real Estate Developers Assn of India v State of M.P.*, 2015 SCC OnLine MP 2839; AIR 2015 MP 25, illegal levy of municipal tax, directed refund with interest at 9 per cent. *Vaidehi Akash Housing (P) Ltd v New D.N. Nagar Coop Housing Society Union Ltd*, AIR 2015 NOC 772 (Bom), a development agreement could not be specifically enforced by the developer because of breaches committed by him.

79. *S. Kotrabarsappa v Indian Bank*, AIR 1987 Kant 236. *Grindlays Bank P.L.C. v Centre for Dev of Instructional Technology*, AIR 1997 Del 164, foreign remittance credited by bank into defendant's account by mistake, defendant required to refund with 12 per cent interest. *Ameen Trading Co v Bank of Baroda*, (1993) 2 KLT 442, mistaken credit by bank, withdrawal by customer, liable to refund. *Indian Bank v Macro Electronics*, AIR 2005 AP 328: (2005) 6 ALD 234 (NOC) negligent Bank staff credit money into the defendant's account. The defendant did not inform the bank of the fact of excess entry and kept withdrawing the money. There was nothing to show a bona fide error on the part of the customer. He had already paid back the money in full, interest at the rate of 6 per cent was awarded from the date of suit to that of repayment. *Saseendrakumari v State Bank of Travancore*, AIR 2011 Ker 58, single payment into bank account, credited twice by mistake, refundable.

80. *Food Corporation of India v K. Venkateswara*, (1988) 1 An LT 930.

81. *Lohia Trading Co v Central Bank of India*, AIR 1978 Cal 468.

82. *Associated Cement Co Ltd v Union of India*, AIR 1998 MP 241. *Union of India v SAIL*, AIR 1997 Ori 77, where also the goods were carried by shorter route though fare charged was that of the longer route. *T. Ranganathan v Essau Alfred*, (1997) 1 Kant LJ 721, a tenant against whom a decree for recovery of rent was passed was not permitted to say that he had already paid the rents covered by the decree and, therefore, the landlord would be a double beneficiary. The doctrine of *res judicata* prevented him from saying so. He could have taken that defence in the suit itself. *Somnath Mahaswara v Orissa SRTC*, AIR 1995 Ori 186, payment made under arrangement which was not permissible under the applicable Act not allowed to be recovered back.

a part of the price for enabling him to pay off the mortgagee and no such payment became necessary because the relief was provided to him under a statutory provision with the result that the mortgage was redeemed without payment, it was held that the purchaser was bound to return the money retained by him for redemption.<sup>83</sup> A mistaken overpayment of rent has been held to be recoverable. The court said that when a person seeks recovery of money paid under a mistake of law, it is not necessary to establish that he had mistakenly believed that he was liable to make the payment. He has only to show that he would not have made the payment but for the mistake and possibly that the mistake was directly connected with the overpayment or connected to the relationship between the payer and the payee.<sup>84</sup>

*Kisan Vikas Patra* purchased by a Co-operative Bank unconscious of the fact that such banks were not allowed to do so under the Government Savings Certificates Act, 1959, the post office also remained oblivious to the restriction. It was held that the Post Office could not refuse interest accrued up to the date of maturity. The principle of unjust enrichment does not permit even the Government and its agencies of taking advantage of such errors.<sup>85</sup> Forfeiture of earnest money for not complying with the conditions of the tender consequent upon issue of letters of intent was held to be not an unjust enrichment.<sup>86</sup>

A consignment of goods was damaged during transportation. The District Forum under Section 13 of the Consumer Protection Act, 1986, ordered the common carrier to pay the price of the goods to the purchaser company. Such company had paid the price to the consignee. The consignee had also received the damaged goods. Thus the consignee, being the double beneficiary, was directed to return the damaged goods to the carrier. In case he had disposed them of, he was directed to pay the value of the damaged goods to the carrier.<sup>87</sup>

#### *Discovery of mistake after long period*

An accounting error was committed by the corporation in recovery of loan and interest. The mistake realised after more than a decade. An attempt was then made to recover the amount that remained unrecovered and interest on it. The court said that interest was not to be allowed. It would be

83. *Saraswathi Ammal v Shanmughavadiyammal*, AIR 1994 Mad 234.

84. *Nurdin & Peacock Plc v D.B. Ramsden & Co Ltd*, (1999) 1 WLR 1249; *Gujarat Steel Tubes Ltd v Port of Kandla*, AIR 2002 Guj 173, plea of refund at the stage of arguments not allowed. *K.T. Venkatagiri v State of Karnataka*, (2003) 9 SCC 1: AIR 2003 SC 1819 sole distributor, disputes arose, during pendency of litigation marketing done through others, this deprived the sole distributor of his sales commission, he was allowed to claim reimbursement to that extent. *Divyesh v Atam Gems*, (2006) 4 Bom CR 471, summary suit for price of diamonds handed over for showing to prospective customers but neither returned nor sale proceeds accounted for, the court allowed the responsible person leave to defend on deposit in court the probable value of the diamonds.

85. *Mahila Sewa Sahakari Bank Ltd v Chief Post Master*, AIR 2007 Guj 72.

86. *Infotech 2000 India Ltd v State of Punjab*, AIR 2007 P&H 58.

87. *Nagpur Golden Transport Co (Regd) v Nath Traders*, (2012) 1 SCC 555: AIR 2012 SC 357.

unjust enrichment at the cost of the other and also penalty for the fault of the creditor.<sup>88</sup>

*Change of position by payee in reliance on payment*

Every payment made under mistake is, however, not recoverable. "There may in a particular case be circumstances which disentitle a plaintiff by estoppel or otherwise."<sup>89</sup> The Calcutta High Court followed this principle in a case in which the facts were as follows:<sup>90</sup>

The plaintiff bank made payment of certain crossed cheques to the defendant bank. The latter informed their customer-payee of the cheques and that the payment had been received for the cheques. It then turned out that the cheques were forged. The plaintiff sued the defendant bank and his customer to recover back the amount contending that the payment had been made under the mistaken belief that the cheques were genuine.

The court came to the conclusion that if the defendant bank had not paid away the proceeds to its customer or if the customer had not yet delivered the goods, the money could have been recovered back under Section 72. The defendant bank and its customer were as much ignorant of the forgery as the plaintiff bank and they, having altered their position because of the cheques being cleared, it was too late to recover back. Neither were they guilty of any fraud nor had they been enriched by the mistake.<sup>91</sup>

This defence would be available to the payee only if he can show that he has changed his position to his disadvantage in consequence of the payment. Thus where certain films were delivered in pursuance to a contract for processing, developing and exhibition and certain instalments were paid by the recipient who had also spent some money on processing, etc, he was allowed to recover back the money paid when it was discovered that the contract was void. The payee was not prejudiced by the fact that he delivered the films because they would be restored to him. It was the payer who was prejudiced having expended money on processing, etc.<sup>92</sup>

DILLON and NICHOLLS L JJ were of the view that the right to refund is of absolute nature except for two limited cases, namely, where there is an

88. *Radha Flour Mills P Ltd v Bihar State Financial Corpn*, AIR 2009 Pat 12.

89. So observed by the Privy Council in *Kali Prasad Singha v Srish Chandra Nandi*, (1948-49) 76 IA 244: AIR 1949 PC 297. *Kerala SEB v Hindustan Construction Co Ltd*, (2006) 12 SCC 500: AIR 2007 SC 425, the Board in its meeting resolved to pay a particular sum to the claimant-contractor subject to adjustment of amounts as indicated by the Committee Report. The Supreme Court held that the resolution must be implemented irrespective of the fact whether it was confirmed at a subsequent meeting or not.

90. *Union Bank of India v A.T. Ali Hussain & Co*, AIR 1978 Cal 169.

91. Another example of the same kind is *Citibank N.A. v Brown Shipley & Co Ltd*, (1991) 2 All ER 690. A draft was issued by a bank on telephonic instructions confirmed by a letter purporting to be from the customer and handed over by the person receiving it to another bank which bank after getting confirmation of genuineness from the issuing bank paid the amount. The issuing bank was not allowed to recover back the amount from the receiving bank though the letter of authority turned out to be forged.

92. *Rover International Ltd v Cannon Films Sales Ltd*, (1989) 1 WLR 912.

estoppel by reason of the payer's conduct or where the payment had been made to an agent who paid it over to the principal. There was a total failure of consideration because the payee of the instalments had no right to hand over the films.<sup>93</sup>

The Supreme Court did not allow a party to recover back the amount of surcharge paid by him to a corporation for granting him an export licence, though the levy was subsequently found to be not authorised. Illegal taxes were considered by the court to be something different from payments made to comply with the terms and conditions of a permit.<sup>94</sup> But where extra payment happened to be made on procurement of paddy because of a mistake about its quality, it was allowed to be recovered back.<sup>95</sup>

The payment of a sum of money by way of part payment of the price in advance for purchase of goods was allowed to be recovered back even where the buyer himself made a default in buying the goods. The court said that the result would have been different if the contract had contained a forfeiture clause. The court allowed interest at 9 per cent p.a.<sup>96</sup>

### Acceptance of less sum under court orders

In a contract for supply of gas, the seller's attempt to increase prices (price escalation) was challenged. The court directed by an interim order that the supply should be continued at original prices. The proposed enhancement was finally found to be valid. It was held that the consumers were liable to pay the difference in prices since the first notice of escalation and also interest on delayed payments. The court applied the principles of deemed renewal and restitution.<sup>97</sup> The terms of the original contract had expired. No new contract could be made because of the consumers refusal to accept the new

93. Applying *Warman v Southern Counties Car Finance Corp Ltd*, (1949) 2 KB 516.

94. *Dharyalakshmi Rice Mills v Commr of Civil Supplies*, (1976) 4 SCC 723: AIR 1976 SC 2243. A transaction entered into at a police station was presumably held to be under coercion. *Mathew v Kuruvilla*, 1983 KLT 104. Quite obviously the section does not apply where no mistake is made out as touching the transaction in question. *Union of India v Jal Rustomji Modi*, (1970) 3 SCC 368: AIR 1970 SC 1490.

95. *Food Corporation of India v K. Venkateswara*, (1988) 1 An LT 930. Liability under the Negotiable Instruments Act, 1881 for negligent handling of collection of cheques cannot be evaded by saying that action should be brought under S. 72 for payment made under mistake, *United Bank of India v. Bank of Baroda*, AIR 1997 Mad 23.

96. *Baldev Steel Ltd v Empire Dyeing & Mfg Co Ltd*, AIR 2001 Del 391. Where payments were made to the owner of the property to be bought and also to the person acting for him in making the agreement and the sale having fallen through, recovery was allowed against both though the owner was saying that there was no dealing with him, *K.S. Satyanarayana v V.R. Narayana Rao*, (1999) 6 SCC 104: AIR 1999 SC 2544. *SBI v National Open School Society*, AIR 2004 Del 306, saving bank account credited by bank by mistake. On realising the mistake on information by customer the entry was reversed and interest sought to be recovered from the customer for using the money, held not allowable. While attempting to recover the principal money, the bank appropriated an equal amount of money from the customer's another account. This was held to be misappropriation and breach of trust.

97. *ONGC v Assn of Natural Gas Consuming Industries*, (2001) 6 SCC 627: AIR 2001 SC 2796.

price. The continuance of the supply and its acceptance by consumers under the court order became the foundation of a deemed renewal.<sup>98</sup>

### *Coercion*

The word "coercion" is used in this section in its general sense and not as defined in Section 15.<sup>99</sup> Thus money paid under pressure of circumstances, such as prevention of the execution of a decree on a property in which the party paying is interested, may be recovered even though "coercion" as defined in Section 15 is not established.<sup>100</sup>

The WESCO extracted arrears of the electricity bill of the previous consumer from the subsequent purchaser of the property by refusing to supply them with electricity unless they paid, contrary to the statute. It was held to be an unjust enrichment by depriving a man of his money without authority of law.<sup>101</sup>

## QUASI-CONTRACTS IN ENGLISH LAW

The variety of *quasi-contractual* obligations recognised by English Law may now be noted.

### **Payments to the defendant's use**

Two principles seem to govern this kind of *quasi-contractual* liability. One of them is that the payment should have been made under pressure and not voluntarily and the other is that the defendant should have been bound to pay and has been relieved of his liability by the payment made by the plaintiff.

An expenditure or payment made purely voluntarily will not do. If, for example, a person pays premiums due upon the policy of another without his request and without any compulsion, he cannot recover.<sup>102</sup> Similarly,

98. *Ibid.*

99. *Seth Kanhaya Lal v National Bank of India Ltd*, (1912–13) 40 IA 56. *Commr. of Customs (Import) v Finacord Chemicals (P) Ltd*, (2015) 15 SCC 697; (2015) 319 ELT 616, imported liquor was confiscated by customs for undervalue, the purchaser deposited certain amounts for release of the goods, held, payment was not part of customs duty, it was only for release of the goods, hence refundable.

100. *Ibid.* Where an alleged surety was compelled to pay a guaranteed loan of which he was not aware, nor his property was charged under it, held coercion within the meaning of S. 72, 1988 Reports 25, 440 Kar. Demand of guaranteed minimum payment by a State Electricity Board does not become unconscionable only because the Government has ordered cut in supply of energy to certain consumers on daily basis. There is no unjust enrichment of the Electricity Board by that reason alone and, therefore, no remedy under S. 72, *W.B. SEB v Siddharta Ferro Alloys Ltd*, AIR 1997 Cal 221. *Hasi Mazumdar v W.B. SEB*, AIR 2006 Cal 59; *Punjab SEB Ltd v Zora Singh*, (2005) 6 SCC 776, unauthorised use of electricity, supply disconnected, payment made by consumer of the charges demanded for restoration of his supply, held, payment under coercion, refundable. *Punjab SEB Ltd v Zora Singh*, (2005) 6 SCC 776, agriculturist applicant paid security amount but provided no connection. Board directed to provide connection and pay interest at the rate of 9 per cent on the deposited amount and compensations of Rs 5000.

101. *Ajay Kumar Agarwal v OSFC*, AIR 2007 Ori 37 (DB).

102. *Falcke v Scottish Imperial Insurance Co*, (1886) LR 34 Ch D 234 (CA).

where a municipal corporation, having no legal liability to do so, carried out repairs of a canal bridge, which it was the obligation of the canal authority to maintain, the corporation could not recover, although the bridge was, for want of repair, endangering the road and although the corporation had without success requested the defendant to carry out the repairs. They were still volunteers.<sup>103</sup> There was no legal compulsion on them to carry out the repairs. The only compulsion was the damage being done to the road and the expenditure made by them in protecting the road may give remedy under some other principle but definitely not under *quasi-contract*.

The kind of compulsion or pressure that the law recognises for the purposes of this remedy is evidenced by *Exall v Partridge*.<sup>104</sup> Here the plaintiff had left his carriage upon the premises in which the defendant was living as a tenant. The landlord lawfully seized all the goods on the premises including the carriage for non-payment of rent and would have sold them in execution of his claim. The plaintiff paid the outstanding rent to get back his carriage and then sued the defendant for the amount. He was held entitled to it.

Another illustration is *Brook's Wharf & Bull Wharf Ltd v Goodman Bros*.<sup>105</sup> This was a case in which the plaintiffs, who were warehousemen, had taken into their bonded warehouse furs which were imported and were liable to duty. A man keeps a bonded warehouse on the terms that he will be responsible to the Commissioner of Customs and Excise if those goods go out of his bonded warehouse before the duties have been paid. The defendants had imported skins and put them in the plaintiff's warehouse. The goods were stolen from the warehouse and the Commissioner recovered the duty from the warehousemen. "They had no answer, they had held the bonded goods, the bonded goods had left their warehouse and could be made available by the thieves on the home market, and the bonded warehousemen had to pay. They were held entitled to recover from the importers the amount which they had paid because it was primarily the importer's duty to have paid the import duties as soon as the goods were imported into this country."

The conditions of this action were restated by LYNKEY J in *Monmouthshire County Council v Smith*.<sup>106</sup>

"The essence of the rule is that there must be a common liability to pay money to a particular person; that the plaintiff has been compelled to pay it by law; that the defendant is liable to pay that money; and that the defendant's debt or liability has been discharged by the plaintiff's payment."

103. *Macclesfield Corpn v Great Central Rly Co*, (1911) 2 KB 528 (CA). This is so because common law does not favour volunteers. For details see *AGENCY OF NECESSITY, post*.

104. (1799) 8 Term Rep 308: (1775–1802) All ER Rep 341 (KB).

105. (1937) 1 KB 534: (1936) 3 All ER 696 (CA).

106. (1956) 1 WLR 1132; affirmed in, *Monmouthshire County Council v Smith*, (1957) 2 QB 154: (1957) 2 WLR 33 (CA).

This statement was affirmed by the Court of Appeal. The appeal was heard along with *Metropolitan Police Distt Receiver v Croydon Corpn.*<sup>107</sup> The two appeals raised exactly the same point. A police constable was injured through the negligence of the defendants and had to remain off duty during the period of illness. The police authorities had under statutory regulations paid them off-duty wages. The police authorities brought an action to recover the amount so paid away as off-duty wages. The contention was that if the police authorities had not paid them, the constables could have recovered from the defendants, the loss of wages and that the liability of the defendants was thereby reduced. But the Court of Appeal did not allow any remedy under *quasi-contract*. In each case the defendant was liable to pay compensation to the injured constable and their liability did not include loss of wages. Thus the payment by the police authorities did not relieve the defendant of any liability.

### Voluntary payments

#### *Payments made under mistake of fact*

Payments made under a mistake of fact can be recovered provided that the party paying would have been liable to pay if the mistaken fact were true. Thus where money was paid under a life insurance policy which to the knowledge of the company had lapsed, but the fact of lapse having been forgotten at the moment, the company was held entitled to recover back the money.<sup>108</sup> PARKE B pointing out that it would be against conscience for a person receiving such payment to retain it. The principle of this case was applied subsequently to a case where payment was made under a policy of marine insurance under the mistaken knowledge that the cargo of lemons had perished whereas in fact it was only sold *en route*, the Privy Council held that the money was recoverable.<sup>109</sup>

One of the essential conditions of this action is that "the mistake must be as to a fact which, if true, would make the person paying liable to pay the money". This suggestion was made in *Aiken v Short*<sup>110</sup> and was approved by the Court of Appeal in *Morgan v Ashcroft*.<sup>111</sup> The facts as summarised by the court were as follows:

The respondent is a book-maker. The plaintiff is a publican who was a regular customer of the respondent for betting transactions. The nature of the mistakes which led to the alleged overpayment of about £24 upon which the action was brought, was proved in evidence to have been a clerical error by the respondent's clerk which led her to give the appellant

107. (1957) 2 QB 154; (1957) 2 WLR 33 (CA).

108. *Kelly v Solari*, (1841) 9 M&W 54: 11 LJ Ex 10.

109. *Norwich Union Fire Insurance Society Ltd v Price Ltd*, 1934 AC 455.

110. (1856) 1 H & N 210, 215: 25 LJ Ex 321.

111. (1938) 1 KB 49 (CA).

credit for the sum of about £24 twice over; thus causing the respondent to pay to the appellant £24 too much.

The action was to recover back the overpayment, and it was lost on two grounds. Firstly, the court was forbidden by the Gaming Act, 1845, from looking into betting transactions and, secondly, even if the mistaken over-credit were taken to be true, there would have been no liability to pay.

In the subsequent case of *Larner v LCC*<sup>112</sup> the Court of Appeal relaxed the principle to this extent that a belief that there is a moral liability to pay is sufficient to prevent the payment from being regarded as purely voluntary. In that case an employer whose servants were called up for military service proposed to pay them the difference between their pay and the pay given to them by the military authorities. The plaintiff to whom such difference had to be paid did not inform the employer of the difference and consequently he was overpaid. When he came back the employer began to deduct from his pay the extra payment which he tried to stop. But the employer was allowed to recover the extra payment. The scheme was no doubt voluntary, but once announced, the payments made under it could not be regarded as voluntary.

It is also necessary for this kind of action to succeed that the mistake must be one of fact and not of law. The distinction may often be difficult to draw and the rule may for this reason have often been criticized, it is still a part of the law. Thus, payment of extra rent made under an agreement to increase rent made in violation of a Rent Control Act could not be recovered.<sup>113</sup> Similarly, the duty paid on an item which the House of Lords had held in another case to be not dutiable, could not be recovered.<sup>114</sup> So was true of an extra gratuity paid on a mistaken view of the relevant regulations.<sup>115</sup>

Where a private document has been construed by a court of law, that interpretation becomes a part of the law. Thus, where an undertaking in a separation deed to pay the wife an annual sum of money "free of any deductions whatever" had already been construed as excluding deduction for income tax, a payment in ignorance of this interpretation without deducting income tax could not be recovered.<sup>116</sup>

#### *Payments made under an ineffective contract*

Three kinds of situation are generally considered under this head, namely, total failure of consideration, money paid under a void contract and money paid under an illegal contract. The effects of void and illegal contracts have already been considered, only the effect of total failure of consideration will be taken up here. Where one of the parties to a contract has paid money in the performance of his part but the other party fails to do his part, the

112. (1949) 2 KB 683 (CA).

113. *Sharp Bros & Knight v Chant*, (1917) 1 KB 771 (CA).

114. *National Pari-Mutual Assn Ltd v R.*, (1930) 47 TLR 110.

115. *Holt v Markham*, (1923) 1 KB 504.

116. *Ord v Ord*, (1923) 2 KB 432.

former has an option, namely, either to sue the other for the breach of contract or to treat the contract as at an end and recover back his money under quasi-contract. Quasi-contractual remedy arises when there has been a total failure of consideration as opposed to partial. For example, where a shareholder of a company transferred his shares to the plaintiff for which the price was paid, but the company on account of certain conduct on the part of the transferor himself refused to register the transfer of his shares, this was held to be a total failure of consideration enabling the plaintiff to recover back his price.<sup>117</sup>

Other instances can be seen in transactions relating to sale of goods. If the buyer has to return the goods on account of there being no title on the part of the seller to sell, the buyer can recover the whole of his price without any deduction for use value, for there is, in such cases, a total and not a partial failure of consideration.<sup>118</sup> The same principle shall apply where the goods have been taken under hire-purchase and the buyer had to return them to the true owner.<sup>119</sup>

Partial failure of consideration will not have the same effect. Thus, where a boy was registered as an apprentice with a watchmaker for a period of six years on payment of a premium and the master died when the boy had learned only for one year, he could not recover any part of his premium, there being only a partial failure of consideration.<sup>120</sup> The same result followed where a party occupied a premises on paying the agreed rent but left soon thereafter on account of the landlord's failure to carry out his part of the promise, he could not recover back the rent.<sup>121</sup>

### *Payments made under compulsion*

Where the owner of a market realised tolls from a shopkeeper by seizing his goods and it being subsequently held that he had no such authority, the shopkeeper was allowed to reclaim the toll money.<sup>122</sup> But where any such fee or toll is paid without improper pressure or compulsion, there would be no right of recovery;<sup>123</sup> so also where the payment is in response to summons issued by a court of law.<sup>124</sup> Payments extorted under colour of authority which is unfounded are recoverable.<sup>125</sup>

117. *Wilkinson v Lloyd*, (1845) 7 QB 27: 4 LT (OS) 432.

118. *Rawland v Dival*, (1923) 2 KB 500.

119. *Warman v Southern Counties Car Finance Corpn Ltd*, (1949) 2 KB 516.

120. *Whincup v Hughes*, (1871) LR 6 CP 78.

121. *Hunt v Silk*, (1804) 5 East 449. No refund was allowed to an auction-purchaser who after paying the initial 10 per cent deposit backed out. Forfeiture of his deposit, the court said, was not akin to a penalty or liquidated damages. *Zembunt (Holdings) v Control Securities*, 1991 Scottish LT 653: 1991 CLY 5101.

122. *Maskell v Horner*, (1915) 3 KB 106 (CA).

123. *Twyford v Manchester Corpn*, (1946) 1 Ch 236.

124. *Moore v Vestry of Fulham*, (1895) 1 QB 399 (CA).

125. *Newdigate v Davy*, (1694) 1 Lord Ragn 742.

### Quantum meruit

Where a party has in the performance of his contract done some work or rendered some service and the further performance has been made useless by the other party, he may recover reasonable compensation for the work or service. *Plinche v Colburn*<sup>126</sup> is an authority for this principle.

The plaintiff was the author of several dramatic entertainments. He was engaged by the defendants, who were the publishers of a work called "The Juvenile Library" to write for that work an article to illustrate the history of armour and costumes from the earliest times, for which he was to be paid 100 guineas. The plaintiff made various drawings and prepared a considerable portion of manuscript when the defendants discontinued the Juvenile Library. The plaintiff claimed a sum of 50 guineas for the part which he had prepared, and the trouble he had taken in the business. He was held entitled to it.

Similarly, where a printer, having printed most of the work, refused to complete it because the dedication was libellous, he was held entitled to recover on *quantum meruit*.<sup>127</sup> A similar recovery is allowed where a person has rendered services under a supposed contract which turns out to be a nullity. *Craven-Ellis v Canons Ltd*<sup>128</sup> is an authority for this.

The plaintiff was appointed managing director of a company. The appointment was made by the other directors who were disqualified by reason of having not taken their qualification shares. The plaintiff also did not take his qualification shares. But he continued to act as managing director and sued the company for his agreed remuneration or for a reasonable remuneration on the basis of *quantum meruit*.

The Court of Appeal rejected the claim for the agreed remuneration, the contract of appointment being void, but allowed him to recover on the basis of *quantum meruit*. GREEH LJ emphasised that a claim of this kind does not depend upon implied contract arising by virtue of the services having been accepted or upon inference of law, but upon a rule of law.

"The obligation to pay reasonable remuneration for the work done when there is no binding contract between the parties is imposed by a rule of law, and not by an inference of fact arising from the acceptance of services or goods. It is one of the cases which are referred to in books on contract as obligations arising *quasi ex contractu* of which a well-known instance is a claim based on money which had been received."<sup>129</sup>

126. (1831) 5 C&P 58: 172 ER 876.

127. *Clay v Yates*, (1856) 1 H&N 73: 156 ER 1123.

128. (1936) 2 KB 403 (CA).

129. At p. 412. A was a licensed builder who did work and supplied materials pursuant to an oral building contract. He sued for the value of the work done and materials supplied. The defendant relied upon the Building Licensing Act, 1971, which provided that a contract was not enforceable by a builder unless it was made in writing and signed by the parties, held, action on the basis of a *quantum meruit* such as that brought by the builder rested not on

Though the remedy is independent of contract, but the contract, if any, shall not be wholly irrelevant. Thus where a ship was delivered for repairs and the contractor used more expensive material than that authorised by the contract, he could not recover under the contract because he had not carried it out precisely, nor under *quasi-contract*, because the shipowner had no chance to reject the expensive material. He could not have rejected the ship after it was already repaired and the mere taking of his own property was not the same thing as an acquiescence in or acceptance of the work done.<sup>130</sup>

Where adequate relief is available under the contract itself, the court may not provide any relief under quasi-contract.

In the course of the performance of a contract to construct a power dam, the owner was in several important respects in breach of the contract. The breach was so fundamental as to justify termination of the contract. However, the contractor continued to work and completed the project. He claimed compensation for the owner's breach on *quantum meruit* basis.

It was held that the contractor, having continued to work the contract in the face of the owner's breach, was entitled to recover under the contract. Since the contractor had completed the contract, and had adequate remedy under the contract, there was no need for law to fashion a restitutive remedy. Nor would it be right for the contractor to obtain a possibly higher rate of compensation than that under the contract.<sup>131</sup>

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implied contract but on a claim for restitution and the liability to pay a reasonable remuneration arose from the operation of the law upon the circumstances. A *quantum meruit* is an obligation or debt imposed by operation of law which arises in the defendant having taken the benefit of the work done, goods supplied or services rendered. *Pavey and Matthews Pty v Paul*, (1987) 162 CLR 221: (1990) 6 Const LJ 59, High Court of Australia, 1990 CLY 662.

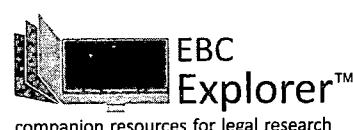
130. *Forman & Co Ltd v Liddesdale*, 1900 AC 190 (PC). Such claims have been dealt with under S. 65 of the Contract Act.

131. *Morrison Knudsen & Co v B.C. Hydro and Power Authority*, (1978) 85 DLR (3rd) 186 (Br Col CA). The Supreme Court did not allow escalated rates where the rates already fixed under the contract seemed to be quite reasonable. *Gautam Constructions & Fisheries Ltd v National Bank for Agriculture and Rural Development*, (2000) 6 SCC 519: AIR 2000 SC 3018.

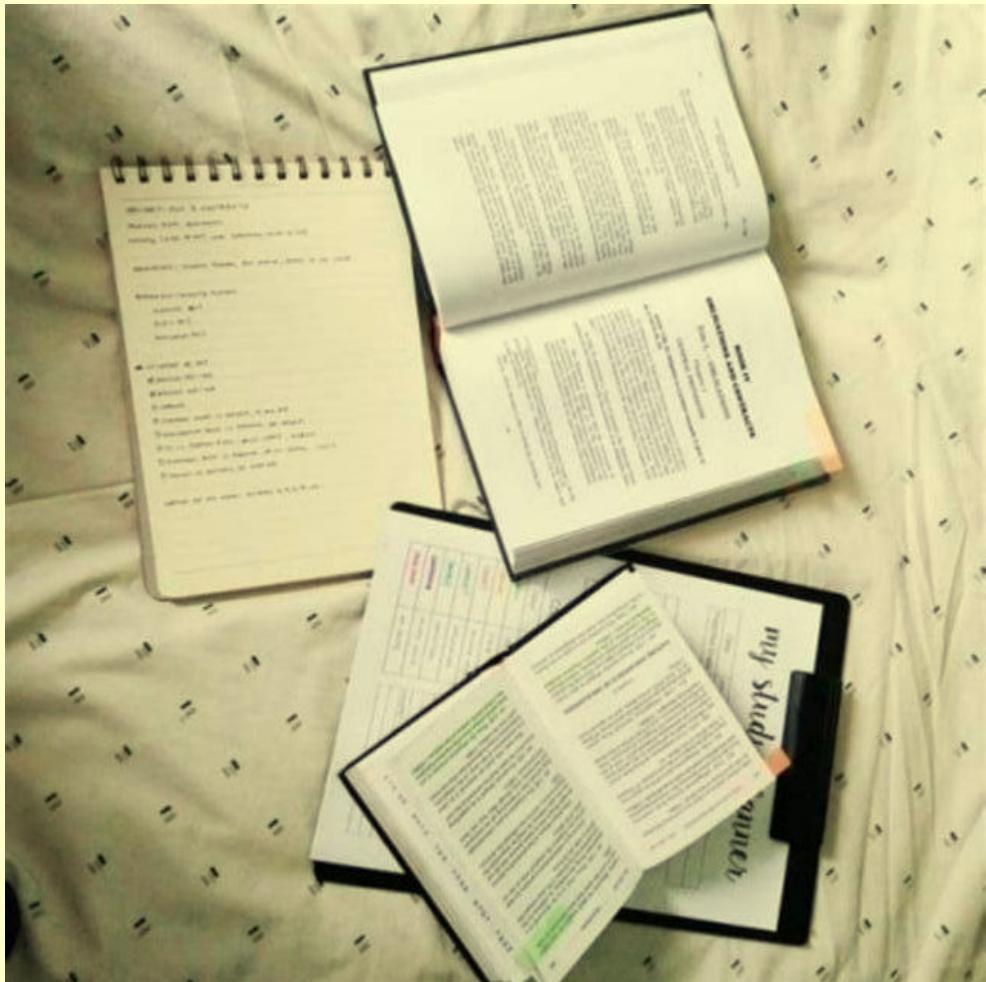
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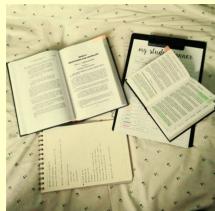
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PART II

**SPECIFIC CONTRACTS**  
**(Ss. 124–238)**

# Contract of Indemnity

## Definition and nature

### Definition in English Law

An illustration in English law of the meaning and effect of a contract of indemnity is to be found in the facts of *Adamson v Jarvis*:<sup>1</sup>



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The plaintiff, an auctioneer, sold certain cattle on the instruction of the defendant. It subsequently turned out that the livestock did not belong to the defendant, but to another person, who made the auctioneer liable and the auctioneer in his turn sued the defendant for indemnity for the loss he had thus suffered by acting on the defendant's directions.

The court laid down that the plaintiff having acted on the request of the defendant was entitled to assume that, if, what he did, turned out to be wrongful, he would be indemnified by the defendant.

Thus "indemnity" in English law means a promise to save a person harmless from the consequences of an act. The promise may be express or it may be implied from the circumstances of the case. Thus, for example, in *Dugdale v Lovering*:<sup>2</sup>

The plaintiffs were in possession of certain trucks which were claimed both by the defendants and one K.P. Co. The defendants demanded delivery and the plaintiffs asked for an indemnity bond, but received no reply. Even so they delivered the trucks to the defendants.

K.P. Co, having successfully sued the plaintiffs for conversion of their property, the plaintiffs were held entitled to recover indemnity from the defendants on an implied promise as evidenced by the fact that by demanding an indemnity, they made it quite clear that they had no intention to deliver except on indemnity. Similarly, in *Sheffield Corpn v Barclay*,<sup>3</sup> a corporation, having registered a transfer of stock on the request of a banker, was held entitled to recover indemnity from the banker when the transfers were discovered to be forged.

1. (1827) 4 Bing 66: 29 RR 503.

2. (1875) LR 10 CP 196: 44 LJ CP 157: 32 LT 155.

3. 1905 AC 392. In similar circumstances in *Starkey v Bank of England*, (1903) AC 114 (HL), a bank was allowed to recover indemnity from an agent who presented a transfer document on which one out of three signatures were forged, though he did not know this fact.

The English definition of indemnity is wide enough to include a promise of indemnity against loss arising from any cause whatsoever, e.g., loss caused by fire or by some other accident. Indeed, every contract of insurance, other than life assurance, is a contract of indemnity.<sup>4</sup>

### *Definition in Section 124 narrower*

But the definition of “indemnity” in Section 124 of the Indian Contract Act is somewhat narrower. It is like this:

**S. 124. “Contract of Indemnity” defined.**—A contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person, is called a “contract of indemnity”.

#### *Illustration*

A contracts to indemnify B against the consequences of any proceedings which C may take against B in respect of a certain sum of 200 rupees. This is a contract of indemnity.

The only illustration appended to the section says that if a person promises to save another from the consequences of a proceeding which may be commenced against him it is a contract of indemnity.<sup>5</sup>

The person who gives the indemnity is called the “indemnifier” and the person for whose protection it is given is called the “indemnity-holder” or “indemnified”.

4. See *Oriental Fire and General Insurance Co v Savoy Solvent Oil Extractions Ltd*, (1997) 6 ALD 1, the following propositions are noticeable from the judgment: in a claim under an insurance policy, if the insurer is refusing payment, the burden lies upon him to show that the assured violated the conditions of the policy; if the assured presents a bogus claim (in this case that the whole stock was burnt, which was not found to be true) he would forfeit all benefits under the policy, he has to observe good faith throughout; a provision in the policy that the insurer may enter upon the affected premises and may remain there for the purposes of assessment, does not make it his duty to do so. *State of Orissa v United India Insurance Co Ltd*, (1997) 5 SCC 512: AIR 1997 SC 2671, insurance from port to port, cancellation by the insurer at a subsequent stage, valid. *United India Insurance Co Ltd v T. Venkata Narsaiah*, AIR 2002 NOC 119 (AP), the insurer held liable for stock of *bidis* destroyed in fire, figures of the stock were known to the insurer. Shifting of the insured stock from one specified ground to another to protect it from rain could not be regarded as contrary to the insurance policy. *Vishan Narain v Oriental Insurance Co Ltd*, AIR 2002 Del 336 vehicle insured for Rs 1,00,000, it was stolen and became a total loss, the insurer not permitted to say that his liability was only up to market value of the vehicle. *Eastern Counties Leather plc v Eastern Counties Leather Group Ltd*, 2002 EWHC 494: 2002 Env LR 34, right to indemnity which became exercisable on account of the repair works for protection of water pollution caused by a tannery. *National Insurance Co Ltd v Arumugham*, (2006) 2 CTC 368, a contract of vehicle insurance, indemnity, insurer could not depend upon exclusion clauses.

5. For another illustration see *Mangladha Ram v Ganda Mal*, AIR 1929 Lah 388, where a vendor's promise to the vendee to be liable if title to the land was disturbed was held to be one of indemnity. Other illustrations are service bonds executed by the employees to serve the master for a particular period or persons claiming payment of money or delivery of goods on indemnity bonds having lost the original documents of title. *M. Sham Singh v State of Mysore*, (1973) 2 SCC 303: AIR 1972 SC 2440, an employee, sent abroad for training on scholarship, undertaking to serve the State on coming back.

Thus the scope of "indemnity" is by the very process of definition restricted to cases where there is a promise to indemnify against loss, caused: (a) by the promisor himself, or (b) by any other person. The definition excludes from its purview cases of loss arising from accidents like fire or perils of the sea. Loss must be caused by some human agency.<sup>6</sup> Contracts of insurance against loss are covered by the chapter on Contingent Contracts.<sup>7</sup>

Secondly, situations like those in *Adamson v Jarvis*<sup>8</sup> where cattle were sold under the instruction of a wrongful owner, are also outside the scope of this definition. Such cases and the case of a loss arising from an act done at the request of the promisor are covered by Section 223 of the Act which provides for indemnity between principal and agent.<sup>9</sup>

The promise of indemnity, as envisaged by the section, may be express or implied. An illustration of implied indemnity is the decision of the Privy Council in *Secy of State for India in Council v Bank of India Ltd.*<sup>10</sup>

A note with forged indorsement was given to a bank which received it for value and in good faith. The bank sent it to the Public Debt Office for renewal in their name. The true owner of the note recovered compensation from the State and the State was allowed to recover from the bank on an implied promise of indemnity.

An indemnity bond which permits an employee to leave the employment earlier than the minimum agreed period only at the cost of the forfeiture of his bond money is valid provided both the period of restriction and the bond money are reasonable. Only that part of the bond money can be retained which is necessary to indemnify the employer for his loss.<sup>11</sup>

The question before the Supreme Court was whether the document contained a contract of indemnity or of bank guarantee. The document purported to indemnify the party against losses, claims, damages etc. which may be suffered by it. It did not employ the usual words which are found in a bank guarantee like unequivocal conditions, unconditional and absolute. It was held to be a contract of indemnity. The claim made by the assured on termination of the contract need not be honoured by the bank without proof of loss.<sup>12</sup>

6. See *Gajanan Moreshwar Parelkar v Moreshwar Madan Mantri*, AIR 1942 Bom 302: (1942) 203 IC 261.

7. See *Tropical Insurance Co v Zenith Life Assurance*, (1941) 196 IC 198 (Lah); *LIC v S. Simdhu*, (2006) 5 SCC 258: AIR 2006 SC 2366, lapsed insurance policy, paid up amount payable. No interest is liable to be paid on such amount.

8. (1827) 4 Bing 66: 29 RR 503.

9. The Illustrations to S. 223 refer to situations like that in *Adamson v Jarvis*, (1827) 4 Bing 66: 29 RR 503.

10. (1937-38) 65 IA 286: AIR 1938 PC 191: (1938) 175 IC 327.

11. *P.N.V.S.V. Prasad v Union of India*, (1995) 1 An WR 126, minimum period of compulsory service three years, three months' remuneration to be recovered if the employee left earlier. Neither penal under S. 74, nor unenforceable under S. 23.

12. *SBI v Mula Sahakari Sakkar Karkhana Ltd.*, (2006) 6 SCC 293: AIR 2007 SC 2361.

### *Insurance indemnity*

Almost all insurances other than life and personal accident insurance are contracts of indemnity. The insurer's promise to indemnify is an absolute one. A suit can be filed immediately upon failure of performance, irrespective of actual loss. If the indemnity holder incurred liability and that liability was absolute, he would be entitled call upon the indemnifier to save him from that liability by paying it off.<sup>13</sup>

### **Extent of liability**

Section 125 lays down the extent of liability.

**S. 125. Rights of indemnity-holder when sued.**—The promisee in a contract of indemnity, acting within the scope of his authority, is entitled to recover from the promisor—

- (1) all damages which he may be compelled to pay in any suit in respect of any matter to which the promise to indemnify applies;
- (2) all costs which he may be compelled to pay in any such suit if, in bringing or defending it, he did not contravene the orders of the promisor, and acted as it would have been prudent for him to act in the absence of any contract of indemnity, or if the promisor authorised him to bring or defend the suit;
- (3) all sums which he may have paid under the terms of any compromise of any such suit, if the compromise was not contrary to the orders of the promisor; and was one which it would have been prudent for the promisee to make in the absence of any contract of indemnity, or if the promisor authorized him to compromise the suit.

The indemnity-holder, acting within the scope of his authority, is entitled to recover the following amounts—

- (1) All damages which he may be compelled to pay in any suit in respect of any matter to which the promise of indemnity applies;<sup>14</sup>
- (2) all costs which he may be compelled to pay in such suits if, in bringing or defending it, he did not contravene the order of the promisor, and acted as it would have been prudent for him to act in the absence of any contract of indemnity, or, if the promisor authorised him to bring or defend the suit;<sup>15</sup>

13. *New India Assurance Co Ltd v State Trading Corpn of India*, AIR 2007 NOC 517 (Guj). *Subhash v National Insurance Co*, (2010) 4 Mah LJ 582, the insurer was held not liable to indemnify the insured when the cheque issued by the insured under the contract of insured was dishonoured.

14. *Parker v Lewis*, (1873) LR 8 Ch App 1035, 1056; *Nallappa Reddi v Virdhachala Reddi*, ILR (1914) 37 Mad 270, right arises as soon as the decree is passed against the promisee; *Chiranji Lal v Naraini*, ILR (1919) 41 All 395; *National Overseas v Export Credit Guarantor Corpn of India Ltd*, AIR 2008 All 18, liability to indemnify did not arise where the exporter consigned his shipment at his own risk without resorting to the terms of the policy.

15. *Pepin v Chunder Seekur Mookerjee*, ILR (1880) 5 Cal 811; *Gopal Singh v Bhawani Prasad*, ILR (1888–90) 10 All 531.

- (3) all sums which he may have paid under the terms of any compromise of any such suit, if the compromise was not contrary to the orders of the promisor, and was one which it would have been prudent for the promisee to make in the absence of any contract of indemnity, or if the promisor authorised him to compromise the suit.<sup>16</sup>

A person who encashes an indemnity bond which is in the nature of a bank guarantee can retain only that part of the amount of the bond which represents the damage or loss suffered by the bond-holder as a result of the contracting party's breach. Anything more would be undeserved windfall for one party and penalty of the other.<sup>17</sup>

Where a motor vehicle (truck) was under indemnity insurance for Rs 2,00,000 and it was stolen with no chances of recovery, it was held that the proper amount of indemnity was as fixed by the surveyor at Rs 1,87,492 and that it was payable with 18 per cent interest for the delay period. The settlement of claim at a lesser amount by insurance authorities was arbitrary and unfair under Article 14 of the Constitution.<sup>18</sup>

### Commencement of liability

An important question in this connection is when does the indemnifier become liable to pay, or, when is the indemnity-holder entitled to recover his indemnity? The original English rule was that indemnity was payable only after the indemnity-holder had suffered actual loss by paying off the claim. The maxim of law was: "you must be damned before you can claim to be indemnified." But the law is now different. The process of transformation is well-explained by CHAGLA J [afterwards CJ] of the Bombay High Court in *Gajanan Moreshwar Parelkar v Moreshwar Madan Mantri*:<sup>19</sup> "It is true that under the English common law no action could be maintained until the actual loss had been incurred. It was very soon realized that an indemnity



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16. See *Pepin v Chunder Seekur Mookerjee*, ILR (1880) 5 Cal 811; *Venkatarangayya Appa Rao v Varaprasada Rao Naidu*, ILR (1920) 43 Mad 898; (1921) 60 IC 164, and also the decision of the Supreme Court in *Ramaswami v Muthu Krishna*, AIR 1967 SC 359. See further, *Union of India v Amarendra Nath Sarkara*, AIR 1967 Cal 119; *Bishal Chand Jain v Chattur Sen*, AIR 1967 All 506. Where a seller promised to the purchaser to indemnify him against dues, if any, it was held that such indemnity clause would include only then existing dues and not those subsequently imposed retrospectively. *Elizabeth v Algesendran Chettiar*, 1986 KLT 521. See also *E.E. Caledonia v Orbit Valve Co*, (1994) 2 Lloyd's Rep 230 (CA), where the question was as to the scope of the indemnity clause on an employee's death and whether the clause covered acts of negligence and breaches of statutory duty. *Sujir Ganesh Nayak & Co v National Insurance Co Ltd*, AIR 1996 Ker 49, the fire policy carried "riot and strike endorsement", this was held to be applicable to partial cessation or interruption of work resulting in loss. *Raigad Concrete Industries v ICICI Bank Ltd*, (2009) 4 Mah LJ 923, indemnifier agreed to pay the amount to indemnity holder subject to the condition that he must pursue his remedy against the party liable and refund recovery to indemnifier, held valid.

17. *Cargill International SA v Bangladesh Sugar & Food Industries Corp*n, (1996) 4 All ER 563 (CA).

18. *Mohit Kumar Saha v New India Assurance Co Ltd*, AIR 1997 Cal 179.

19. AIR 1942 Bom 302, 304; (1942) 203 IC 261. Followed in *Khetrapal Amarnath v Madhukar Pictures*, AIR 1956 Bom 106.



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might be worth very little indeed if the indemnified could not enforce his indemnity till he had actually paid the loss. If a suit was filed against him he had actually to wait till a judgment was pronounced and it was only after he had satisfied the judgment that he could sue on his indemnity. It is clear that this might under certain circumstances throw an intolerable burden upon the indemnity-holder. He might not be in a position to satisfy the judgment and yet he could not avail himself of his indemnity till he had done so. Therefore, the court of equity stepped in and mitigated the rigour of the common law. The court of equity held that if his liability had become absolute then he was entitled either to get the indemnifier to pay off the claim or to pay into court sufficient money which would constitute a fund for paying off the claim whenever it was made.”<sup>20</sup>

This principle was expounded in *Richardson, re*,<sup>21</sup> where BUCKLEY LJ observed: “Indemnity is not necessarily given by repayment after payment. Indemnity requires that the party to be indemnified shall never be called upon to pay....”<sup>22</sup> The High Court of Calcutta in its well-known decision in *Osman Jamal & Sons Ltd v Gopal Purshottam*<sup>23</sup> followed this principle.

A company was acting as the commission agents of the defendant firm and in that capacity bought certain goods for the defendants which they failed to take. The supplier became entitled to recover from the company certain sum of money as damages for breach. The company went into liquidation before paying the claim.

It was held that the Official Liquidator could recover the amount even though the company had not actually paid the vendor. The court, however, directed that the amount should be set apart so that it is used in full payment of the vendor in respect of whose contract the company had incurred liability.<sup>24</sup>

20. The court distinguished the case from its earlier decision in *Shanker Nimbaji v Laxman Sapdu*, AIR 1940 Bom 161.

21. (1911) 2 KB 705 (CA).

22. *Supra* at p. 715; cited by Lord WILLIAMS J of the Calcutta High Court in *Osman Jamal & Sons v Gopal Purshottam*, ILR (1929) 56 Cal 262, 266, where the learned judge reviewed all the English authorities. Earlier to this KENNEDY LJ observed in *Liverpool Mortgage Insurance Co's, re*, (1914) 2 Ch 617, 638 (CA) that indemnity does not merely mean to reimburse in respect of moneys paid, but to save from loss in respect of the liability against which the indemnity has been given because otherwise indemnity may be worth very little if the indemnity-holder is not able to pay in the first instance.

23. ILR (1929) 56 Cal 262. See also to the same effect, *Kumar Nath Bhattacharjee v Nobo Kumar*, ILR 26 Cal 241.

24. Followed in *Prafulla Kumar v Gopi Ballabh*, AIR 1964 Cal 159.

The High Courts of Allahabad<sup>25</sup>, Madras<sup>26</sup> and Patna<sup>27</sup> have all expressed their concurrence in the principle that as soon as the liability of the indemnity-holder to pay becomes clear and certain he should have the right to require the indemnifier to put him in a position to meet the claim. But contrary views have also been expressed.<sup>28</sup>

Where an authorised agent of the insurance company collected the premium amount from the assured against proper receipt, the liability of the insurer began from that moment though the agent deposited the collection with the company after the occurrence.<sup>29</sup>

#### *Specified time for notice*

An insured motor vehicle was lost by theft. The insurance policy required the assured to send notice to the insurer immediately after theft or any other criminal act. The assured made police report of the theft immediately after the incident, but informed the insurer after one month. The question was whether this could be regarded as a notice given immediately. The court said that the expression immediately implies notice to be given with promptitude avoiding unnecessary delay. Immediate police report showed the *bona fides* of the assured in the matter. Report to the insurer after one month could not be regarded as unreasonable. Indemnification could not be denied.<sup>30</sup>

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25. See *Shiam Lal v Abdul Salam*, AIR 1931 All 754; *ILR* 53 All 246; *Abdul Majeed v Abdul Rashid*, AIR 1936 All 598.

26. *Ramalingathudayar v Unnamalai Achi*, (1915) 38 Mad 791; (1914) 24 IC 423.

27. *Chunibhai Patel v Natha Bhai Patel*, AIR 1944 Pat 185; *Abdul Hussain Jambawala v Bombay Metal Syndicate*, AIR 1972 Bom 252, order of direct payment of sales tax to authorities from the person due without the intervention of the seller. An action can be brought by the indemnity-holder within three years from the date of payment by him. *Shanti Swarup v Munshi Singh*, AIR 1967 SC 1315; (1967) 2 SCR 315. The indemnifier has the right under the principle of subrogation to sue the person who caused the loss. *Maharana Shri Jarvat Singhji v Secy of State for India*, ILR 1889 14 Bom 299.

28. See for example, *Shanker Nimbaji v Laxman Sapdu*, AIR 1940 Bom 161.

29. *Oriental Insurance Co Ltd v Asha Paul*, 1996 AIHC 2043 (J&K); *Sandhya Sah v New India Assurance Co*, AIR 2004 Pat 42, bank providing benefit of insurance to its customers, no direct contract between customers and insurer. For any delay in payment of insurance the customer could proceed only against bank.

30. *Praful Kumar Mohanty v Oriental Insurance Co Ltd*, 1997 AIHC 2822 (Ori). The court cited ROLE B in *Thompson v Gibson*, 10 LJ Ex 243 to the effect that "immediately implies that the act to be done should be done with all convenient speed. In other words, the thing to be done should be done as quickly as is reasonably possible".

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The following cases from this chapter are available through EBC Explorer™:

- *Adamson v Jarvis*, (1827) 4 Bing 66: 29 RR 503
- *Gajanan Moreshwar Parelkar v Moreshwar Madan Mantri*, AIR 1942 Bom 302: (1942) 203 IC 261
- *Mohit Kumar Saha v New India Assurance Co Ltd*, AIR 1997 Cal 179



# 12

## Guarantee

### DEFINITION

**S. 126. "Contract of guarantee", "surety", "principal debtor" and "creditor".**—A "contract of guarantee" is a contract to perform the promise, or discharge the liability, of a third person in case of his default. The person who gives the guarantee is called the "surety"; the person in respect of whose default the guarantee is given is called the "principal debtor", and the person to whom the guarantee is given is called the "creditor". A guarantee may be either oral or written.

### Economic functions of guarantee

The function of a contract of guarantee is to enable a person to get a loan, or goods on credit, or an employment. Some person comes forward and tells the lender, or the supplier or the employer that he (the person in need) may be trusted and in case of any default, "I undertake to be responsible". For example, in the old case of *Birkmyr v Darnell*<sup>1</sup> the court said:

"If two come to a shop and one buys, and the other to give him credit, promises the seller, 'If he does not pay you, I will'."

This type of collateral undertaking to be liable for the default of another is called a "contract of guarantee". In English law a guarantee is defined as "a promise to answer for the debt, default or miscarriage of another".<sup>2</sup> It is a collateral engagement to be liable for the debt of another in case of his default. "Guarantees are usually taken to provide a second pocket to pay if the first should be empty."<sup>3</sup>

### Parties

The person who gives the guarantee is called the "surety", the person in respect of whose default the guarantee is given is called the "principal debtor" and the person to whom the guarantee is given is called the "creditor".

1. 91 ER 27: 1 Salk 27.

2. S. 4, Statute of Frauds 1677, 29 Car, II, C 3.

3. Wood, LAW AND PRACTICE OF INTERNATIONAL FINANCE (1980) 295.

### Independent liability different from guarantee

There must be a conditional promise to be liable on the default of the principal debtor. A liability which is incurred independently of a “default” is not within the definition of guarantee.<sup>4</sup> To refer again to *Birkmyr v Darnell*,<sup>5</sup> where referring to the buyer’s companion, the court further said that if the companion had said: “Let him have the goods, ‘I will be your pay master’ or ‘I will see you paid.’” “This would have been an undertaking as for himself and is not a guarantee.”<sup>6</sup> This principle was applied in *Taylor v Lee*<sup>7</sup> decided in the US:

A landlord and his tenant went to the plaintiff’s store. The landlord said to the plaintiff: Mr Parker will be on our land this year, and you will sell him anything he wants, and I will see it paid.

This was held to be an original promise, and not a collateral promise to be liable for the default of another and, therefore, not a guarantee.<sup>8</sup>

The undertaking by a bank in the shape of a bank guarantee is also in the nature of an independent obligation payable on demand. It has nothing to do with the state of relations between the parties to the contract. It is a suitable method of securing payment in commercial dealings. The beneficiary is entitled to realise the whole of the amount under the guarantee irrespective of pending disputes between the parties.<sup>9</sup>

Where only an assurance for repayment of amount due from the loanee was given by means of a letter, the court said that it could not be construed as a deed of guarantee. The writer of the letter was accordingly held not liable.<sup>10</sup> Where a letter of comfort was issued by a holding company in favour

4. See *Punjab National Bank v Sri Vikram Cotton Mills*, (1970) 1 SCC 60: AIR 1970 SC 1973. The liability of both (the principal debtor and surety) is just the same.

5. 91 ER 27: 1 Salk 27.

6. Observations to the same effect appear in *Punjab National Bank v Sri Vikram Cotton Mills*, (1970) 1 SCC 60: AIR 1970 SC 1973; *Nanak Ram v Mehin Lal*, ILR (1877) 1 All 487; *Varghese v Abraham*, AIR 1952 TC 202, undertaking to see that the creditor would be paid.

7. Supreme Court of North Carolina, (1924) 121 SE 659: 187 NC 393. Collected from Shepherd & Wellington: CONTRACTS AND CONTRACT REMEDIES, (1957, 4th Edn) 373; see also *Juggutt Indar Narain Ray Chowdery v Nistiarinee Dassee*, (1931) 151 IC 981 (PC).

8. See also *Mountstephen v Lakeman*, (1871) LR 7 QB 196; affd 1874 LR 7 HL 17 where the chairman of a Board, speaking personally, assured payment to a contractor for certain works. This was held to be a personal undertaking and not a guarantee. An undertaking to discharge the liability of another without any request from him creates an independent liability and not collateral as that of a guarantor. *N.S. Varghese v Dhanalakshmi Bank Ltd*, 1997 AIHC 1820 (Ker), repayment of bank loan en route co-operative society, did not make the latter a guarantor for the loan. *Chanana Steel Tubes (P) Ltd v Jaitu Steel Tubes (P) Ltd*, AIR 2000 HP 48, a party introduced to a businessman a certain person as a customer. It did not mean that the introducer became a guarantor for the person. *Kinkar Santananda Sanyasi v SBI*, AIR 2002 Ori 114, joint holders of FDR in a bank, payable to either or survivor, on the death of one of them, the other can no doubt collect payment but he is accountable to the legal heirs of the deceased joint-depositor. *United Bank of India v Rafiulla Tea and Industries (P) Ltd*, AIR 2002 Gau 101, bank cash certificate, payment not allowed to be refused on the ground that there was a litigation with the certificate holder.

9. *Pollen Dealcom (P) Ltd v Chambal Fertilizers & Chemicals*, (2010) 92 AIC 695 (Cal).

10. *Indian Overseas Bank v SNG Castorete (P) Ltd*, AIR 2002 Del 309.

of its associate company that it had capabilities of meeting its financial and contractual obligations, the court said that the letter was in the nature of a recommendatory document. It could not be construed as a guarantee there being nothing in it showing that the holding company was understanding to discharge any liability of its associate in the event of the latter's default.<sup>11</sup>

### ESSENTIAL FEATURES OF GUARANTEE

The following are the requisites of a valid guarantee:

#### 1. Principal debt

##### *Recoverable debt necessary*

The purpose of a guarantee being to secure the payment of a debt, the existence of a recoverable debt is necessary.<sup>12</sup> It is of the essence of a guarantee that there should be someone liable as a principal debtor and the surety undertakes to be liable on his default.<sup>13</sup> If there is no principal debt, there can be no valid guarantee.<sup>14</sup> "A contract of guarantee is a tripartite agreement which contemplates the principal debtor, the creditor and the surety."<sup>15</sup> This was so held by the House of Lords in the Scottish case of *Swan v Bank of Scotland*,<sup>16</sup> decided as early as 1836.

The payment of the overdraft of a banker's customer was guaranteed by the defendant. The overdrafts were contrary to a statute, which not only imposed penalty upon the parties to such drafts but also made them void. The customer having defaulted, the surety was sued for the loss.

But he was held not liable. The court said that "if there is nothing due, no balance, the obligation to make that nothing good amounts itself to nothing. If no debt is due, if the banker is forbidden from having any claim against his customer, there is no liability incurred by the co-obligors".<sup>17</sup>

11. *United Breweries (Holding) Ltd v Karnataka State Industrial Investment and Development & Corpn*, AIR 2012 Kar 65 (DB).

12. *Mountstephen v Lakeman*, (1871) LR 7 QB 196, 202.

13. *Harburg India Rubber Comb Co v Martin*, (1902) 1 KB 778 (CA).

14. A guarantee for a debt already barred by time, held, void. *Manju Mahadev v Shivappa Manju Shetti*, ILR (1918) 42 Bom 444.

15. *Mahabir Shum Sher v Lloyds Bank*, AIR 1968 Cal 371, 377 per RAY J, reiterated by the Supreme Court in the case cited in Note 5 above. The surety agrees to run the risk on express or implied request. *K.V. Periyamianna Marakkayar and Sons v Banians & Co*, ILR (1925) 49 Mad 156: AIR 1926 Mad 544; *Ramachandra B. Loyalka v Shapurji N. Bhownagree*, AIR 1940 Bom 315; *Jagannath Baksh Singh v Chandra Bhushan Singh*, AIR 1937 Oudh 19: (1936) 12 Luck 484. The signing of a solvency certificate does not make one a guarantor for the debt of the person whose solvency is certified. *Joseph Abraham v Tabsildar Meenachil*, AIR 1971 Ker 334.

16. (1836) 10 Bligh NS 627. See also *Lima Leitao & Co Ltd v Union of India*, AIR 1968 Goa 29; *Mahabir Shum Sher v Lloyds Bank*, AIR 1968 Cal 371; A.V. Varadarajulu Naidu v K.V. Thavasi Nadar, AIR 1963 Mad 413.

17. See also *Lima Leitao & Co Ltd v Union of India*, AIR 1968 Goa 29; *Agencia Agenda National Ltd v A. Socie-dade Chowgule & Cia Ltd*, AIR 1967 Goa 88.

### *Guarantee for void debt, when enforceable*

But sometimes a guarantee even for a void debt may be held enforceable. Where, for example, the directors of a company guaranteed their company's loan which was void as being *ultra vires*, the directors were nevertheless held liable.<sup>18</sup> The reason "may be that the voidness of a contract to guarantee the debt of a company acting *ultra vires* is different in its consequence from the voidness brought about by the express and emphatic language of a statute".<sup>19</sup>

### *Guarantee of minor's debt*

A similar problem arises when the debt of a minor has been guaranteed. The debt being void, is the surety liable? The Court of King's Bench considered the question in *Coutts & Co v Browne Lecky*<sup>20</sup> and held that no liability should be incurred by the surety. The head note to the report says:

"A loan, by way of overdraft made by a bank to an infant being void under Section 1, of the Infants' Relief Act, 1874, the guarantors of the loan, where the fact of infancy is known to all parties, cannot be made liable in an action on the guarantee."

OLIVER J said: "Apart from authority it would certainly seem strange if a contract to make the debt default or miscarriage of another, could be binding where, by statute, the loan guaranteed is, in terms, made absolutely void. Looking at the matter broadly, how, in these circumstances, can the omission by an infant to pay what is made void by statute be described as either a debt, a default or a miscarriage? There is no debt here because the Act of 1874 says so;<sup>21</sup> there is no default, for the infant is entitled to omit to pay, and there is no miscarriage for the same reason."<sup>22</sup>

In India it has been held, following earlier English authorities, that where a minor's debt has been knowingly guaranteed, the surety should be held liable as a principal debtor himself.<sup>23</sup> In *Kashiba Bin Narsapa Nikade v Narshiv Shripat*<sup>24</sup> the Bombay High Court observed: "A surety to a bond passed by a minor for moneys borrowed for purposes of litigation not found to be necessary, is liable to be sued on it whether the contract of the minor is considered to be void or voidable. We see no reason why a person cannot contract to guarantee the performance by a third person of a duty of

18. *Yorkshire Railway Wagon Co v Maclure*, 1881 19 Ch D 478 (CA); *Garrard v James*, (1925) 1 Ch 616.

19. OLIVER J in *Coutts & Co v Browne Lecky*, 1947 KB 10.

20. 1947 KB 10: (1946) 2 All ER 207.

21. The Infants' Relief Act, 1874, S. 1.

22. For a criticism of this decision see E.J. Cohn, *Validity of Guarantees for Debts of Minors*, (1947) 10 Mod LR 40.

23. *Narsapa Nikade v Narshiv Shripat*, ILR (1895) 19 Bom 697, following *Wathier v Wilson*, (1911) 27 TLR 582. For other decisions see *Sohan Lal v Puran Singh*, (1916) 54 Punj Rec 165; *Tikki Lal Jaithu Teli v Komalchand*, AIR 1940 Nag 327.

24. ILR (1895) 19 Bom 697. See also *Inder Singh v Thakar Singh*, (1921) 2 Lah 207: AIR 1921 Lah 20; *Jagannath Ganeshram v Shivnarayan Bhagirath*, AIR 1940 Bom 247: ILR 1940 Bom 387.

imperfect obligation. If the debt is void, the contract of the so-called surety is not collateral, but a principal contract.”<sup>25</sup>

## 2. Consideration

Like every other contract, a contract of guarantee should also be supported by some consideration. A guarantee without consideration is void.<sup>26</sup> But there need be no direct consideration between the surety and the creditor.<sup>27</sup> Section 127 clearly says:

**S. 127. Consideration for guarantee.**—Anything done, or any promise made, for the benefit of the principal debtor, may be a sufficient consideration to the surety for giving the guarantee.

### Illustrations

- (a) *B* requests *A* to sell and deliver to him goods on credit. *A* agrees to do so, provided *C* will guarantee the payment of the price of the goods. *C* promises to guarantee the payment in consideration of *A*'s promise to deliver the goods. This is a sufficient consideration for *C*'s promise.
- (b) *A* sells and delivers goods to *B*. *C* afterwards requests *A* to forbear to sue *B* for the debt for a year, and promises that, if he does so, *C* will pay for them in default of payment by *B*. *A* agrees to forbear as requested. This is a sufficient consideration for *C*'s promise.<sup>28</sup>
- (c) *A* sells and delivers goods to *B*. *C* afterwards, without consideration, agrees to pay for them in default of *B*. The agreement is void.

Thus where a loan is given or goods sold on credit on the basis of a guarantee that is sufficient consideration.<sup>29</sup> Similarly, where a credit has already been given and the payment having become due, the creditor refrains from

25. In England also it has been held that in such cases the guarantor should be held liable as an indemnifier, *Yeoman Credit Ltd v Latter*, (1961) 1 WLR 828; (1961) 2 All ER 294 (CA). *Allahabad Jal Sansthan v State of U.P.*, AIR 2004 All 366, rates of premium not allowed to be unilaterally increased. *Siddhiwinayak Realities (P) Ltd v Tulip Hospitality Services Ltd*, (2007) 4 SCC 612; AIR 2007 SC 1457, agreement for purchaser of hotel property, default, matter to be decided by escrow agents jointly, there was a possibility of a detailed cross-examination of an escrow agent on the aspects of default, hence, he could not be a judge in his own cause.

26. *Janaki Paul v Dhokar Mall Kidarbux*, (1935) 156 IC 200; *Ram Narain v Hari Singh*, AIR 1964 Raj 76; ILR (1963) 13 Raj 973.

27. BEST CJ observed in *Marely v Boothby*, (1825) 3 Bing 107 that “no court of common law has ever said that there should be a consideration directly between the persons giving and receiving the guarantee. It is enough if the person for whom the guarantor becomes surety receives a benefit, or the person to whom the guarantee is given suffers inconvenience, as an inducement to the surety to become guarantor for the principal debtor”.

28. The Patna High Court similarly held that a guarantee on the implied request of the principal debtor is binding. A guarantee given after the execution of the loan document is valid. *Prasanjit Mahtha v United Commercial Bank Ltd*, AIR 1979 Pat 151.

29. *SBI v Kusumi Vallabhdas Thakkar*, (1994) 1 GLH 62; (1994) 1 Guj LR 655, forbearance on the part of the creditor in filing a suit against one of the debtors was held to be a good consideration for the guarantee. *Union Bank of India v Monin Enterprises*, AIR 2002 Kant 270, the borrower was enjoying cash-credit facility from the bank without any guarantee, the facility was also enhanced from time to time, guarantee taken after the facility was finally enhanced and withdrawal allowed without guarantee, the guarantee did not mention anything about past debts. Hence there was nothing done on the basis of the guarantee either in the present or in the past. The guarantee was without consideration.

suing the principal debtor, that would be a sufficient consideration for giving a guarantee.<sup>30</sup>

Where the consideration failed, the court said that there was no question of recovering anything from the principal debtor or of enforcing his bank guarantee. In this case, the contract was for cutting and removing timber from a forest. Payment for the same was guaranteed by a bank guarantee. The forest authorities did not permit the cutting. Consideration failed. Neither the bank guarantee could be invoked nor the contractor's earnest money could be forfeited.<sup>31</sup>

### *Guarantee for past debt*

But a guarantee for a past debt should be invalid. The section says that "anything done...for the benefit of the principal debtor" is good consideration.<sup>32</sup>

But will the words "anything done" include things done before the guarantee was given? The Oudh High Court in *M. Gulam Husain Khan v M. Faiyaz Ali Khan*<sup>33</sup> answered this question in the affirmative.

A lessee agreed to pay the sum due under a lease by certain instalments and after a few days a person executed a surety bond binding himself to pay a certain amount in default of the payment of instalments.

The court held that the bond was not without consideration.<sup>34</sup> The decision has been criticised in Pollock and Mulla. The learned editors observe: "This seems to attribute an unnatural meaning to the word, which, it is submitted and as the rest of the section shows, refers to an executed as distinguished from an executory consideration."<sup>35</sup>

The decision also seems to be contrary to the third illustration to the section.<sup>36</sup>

30. *Madan Lal Sobe v Rajasthan State Industrial Development & Investment Corp Ltd*, (2006) 135 DLT 554, guarantee for securing forbearance.

31. *Ujjal Transport Agency v Coal India Ltd*, AIR 2011 Jha 34.

32. It is not necessary that the guarantor should draw some personal benefit. *Sornalinga Mudali v Pachai Naickan*, ILR (1915) 38 Mad 680; *Pestonji Manekji Mody v Bai Meherbai*, AIR 1928 Bom 539. The consideration must also be lawful. *Cooper v Joel*, (1859) 45 ER 350, a consideration which failed; *Het Ram v Devi Prasad*, (1881) 1 All WN 2, withdrawal of a non-compoundable case.

33. AIR 1940 Oudh 346. *SBI v Premco Saw Mills*, AIR 1984 Guj 93, forbearance to sue on the part of the creditor is a good consideration for a guarantee.

34. Reliance was placed upon the following decisions: *Mathra Das v Shamboo Nath*, AIR 1929 Lah 203; *Kalicharan v Abdul Rehman*, (1919) 10 LW 34: AIR 1918 PC 226.

35. INDIAN CONTRACT AND SPECIFIC RELIEF ACTS (8th Edn by Setalvad and Gooderson, 1957) 517.

36. The Andhra Pradesh High Court has supported the view that past consideration is not good. *Mir Niyamat Ali Khan v Commercial & Industrial Bank*, AIR 1969 AP 294. But the judicial opinion is still in conflict. See *Kalicharan v Abdul Rehman*, (1919) 10 LW 34: AIR 1918 PC 226, a guarantee for leasing transactions was held not to cover leasing agreements which were concluded before the date of the guarantee. *Perrylease Ltd v Imecar A.G.*, (1988) 1 WLR 463 (QB). The Bombay High Court has observed in *Union Bank of India v Avinash P. Bhonsle*, 1991 Mah LJ 1004 that: It is well settled that just as illustrations should not be read

In a case before the Bombay High Court<sup>37</sup>, a guarantee was executed subsequent to release of financial assistance to the borrower. The court held that it could not be said that there was no consideration for the guarantee. In the view of the court, “past consideration is valid consideration”.

### *Past as well as future debt*

A guarantee for a past as well as a future debt is enforceable provided some further debt is incurred after the guarantee. But there should be a clear undertaking to be liable for a past debt<sup>38</sup> and as soon as some fresh obligation is incurred, the liability for all the obligations is coupled up.<sup>39</sup>

### *Benefit of principal debtor, enough consideration*

If the principal debtor gets a benefit, that suffices to sustain the guarantee. It will be of no consequence to say that the principal debtor had never requested for a guarantee or that it was given without his knowledge or consent. A contention of this kind was refuted by the Patna High Court in a case<sup>40</sup> where the directors of a company who guaranteed the company's loans argued that the company had never asked for the guarantee. The court relied upon the following statement of Lord LOREBURN:<sup>41</sup> “There are three possible variations in the parties to contract of suretyship. The first and the simplest case is that in which all the three parties concerned are parties to the contract in the sense that both the principal debtor and creditor agree that the surety's liability is a secondary liability only, and that the principal debtor is primarily liable for the obligations guaranteed. But it is also possible that the contract of suretyship may be recognised only as between the principal debtor and the surety, or as between the creditor and the surety,

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as extending the meaning of a section, they should also not be read as restricting its operation, especially so, when the effect would be to curtail a right which the plain words of the section would confer. It is, therefore, clear that when the language of the text of S. 127 of the Contract Act is clear and unambiguous, the sweep of the text cannot be curtailed by using Illustration (c) to impose a limitation on the expression “any thing done or any promise made for the benefit of the principal debtor” that it should be done at the time of giving the guarantee. The language is wide enough to include any thing that was done or a promise made before giving the guarantee and would not restrict the application of the section only to what was contemporaneously done. See further *Allahabad Bank v S.M. Engg Industries*, (1992) 1 Cal LJ 448 where the bank was not allowed to sue the surety without further or any advance made after the date of the guarantee.

37. *SICOM Ltd v Padmashri Mahipatrai Shah*, (2005) 3 Mah LJ 125. The court further held that where a guarantee was given in consideration of an amount lent and advanced, it was not required in law that there should be an independent consideration for each of the clauses.
38. *Morrell v Cowan*, (1877) 7 Ch D 151.
39. See, e.g., *Carlesberry Brewery Malaysia v Soon Heng A.W. & Sons*, (1989) 1 MLJ 104 (Malaysia) Kota Bahri, where the court on going through the guarantee found that it was within the contemplation of the parties that the guarantors were to be saddled with liabilities not only after but also before the signing of the guarantee. Following, *Esso Standard Malaya v Southern Cross Airways*, (1972) 1 Mal LJ 168.
40. *Prasanjit Mahtta v United Commercial Bank Ltd*, AIR 1979 Pat 151.
41. *Duncan Fox & Co v North & South Wales Bank*, (1880) LR 6 AC 1 (HL).



in which event the rights and duties arising out of the contract of suretyship only affect those parties.”

#### *Counter-guarantee*

A counter guarantee is for protection of the original guarantor. When the original guarantor is called upon to pay and he has fulfilled his obligation under his guarantees, he can call upon the counter guarantor to pay him.<sup>42</sup> The documents filed by the plaintiff showed that the defendant had given a counter-guarantee in favour of the plaintiff to cover the contingency of the plaintiff having to pay any amount as a result of the invocation of the bank guarantee. The defendant failed to pay. The plaintiff was held to be entitled to a decree against the defendant.<sup>43</sup>

### **3. Misrepresentation and concealment**

A contract of guarantee is not a contract *uberrimae fides* or one of absolute good faith.<sup>44</sup> Thus where a banker received a guarantee with knowledge of circumstances seriously affecting the credit of the customer, it was held that there was no duty to disclose this fact to the surety.<sup>45</sup> Yet “it is the duty of a party taking a guarantee to put the surety in possession of all the facts likely to affect the degree of his responsibility; and if he neglects to do so, it is at his peril. A surety ought to be acquainted with the whole contract entered into with his principal.” Where a person purchased land without disclosing that he was doing so on behalf of a society for which the surety would not have given the guarantee because the society was already embroiled in litigation, the court held that it could be said that the consent of the surety was taken by suppressing the vital fact from him and therefore he was not bound by the guarantee.<sup>46</sup> Sections 142 and 143 implement these principles. Sections 142 and 143 provides:

**S. 142. Guarantee obtained by misrepresentation, invalid.**— Any guarantee obtained by means of misrepresentation made by the creditor or with his knowledge and assent, concerning a material part of the transaction, is invalid.

**S. 143. Guarantee obtained by concealment, invalid.**— Any guarantee which the creditor has obtained by means of keeping silence as to material circumstances is invalid.

42. *Karnataka State Industrial Investment Corpn v State Bank of India*, (2005) 1 CLT 437 (Kant, DB); (2004) 3 CCC 568, limitation for claim against counter guarantor starts running from the date of payment by the guarantor.

43. *Punjab National Bank v Maya Enterprises*, AIR 2003 NOC 299 (Del); (2002) 62 DRJ 729.

44. See *Davies v London & Provincial Marine Insurance Co*, (1878) LR 8 Ch D 469.

45. *National Provincial Bank of England Ltd v Glanusk*, (1913) 3 KB 335. See also *Bank of Scotland v Morrison*, 1911 SC 593; *Cooper v National Provincial Bank Ltd*, 1946 KB 1. A creditor's failure to disclose to a guarantor a material fact known to him will vitiate the guarantee if the non-disclosure amounts to a misrepresentation. The suppression of a fact will amount to misrepresentation if the fact is inconsistent with the presumed basis of the contract of guarantee, *Westpac Securities v Dickie*, (1991) 1 NZ LR 657 (CA).

46. *Shrinivas Shankar Potnis v Raghukul Sahakari Griharachana Sanstha Maryadit*, (2010) 1 Mah LJ 368.

*Illustrations*

- (a) A engages B as clerk to collect money for him. B fails to account for some of his receipts, and A in consequence calls upon him to furnish security for his duly accounting. C gives his guarantee for B's duly accounting. A does not acquaint C with B's previous conduct. B afterwards makes default. The guarantee is invalid.
- (b) A guarantees to C payment for iron to be supplied by him to B to the amount of 2000 tons. B and C have privately agreed that B should pay five rupees per ton beyond the market price, such excess to be applied in liquidation of an old debt. This agreement is concealed from A. A is not liable as a surety.

Guarantees for the good conduct of a servant have invited more frequent applications of this principle. A very illustrative case is *London General Omnibus Co v Holloway*.<sup>47</sup>

The defendant was invited to give a guarantee for the fidelity of a servant. The employer had earlier dismissed him for dishonesty, but did not disclose this fact to the surety. The servant committed another embezzlement.



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The surety was held not liable. "The surety believed that he was making himself answerable for a presumably honest man, not for a known thief." Every surety undertakes the risk of default, which is more in some cases and less in others depending upon circumstances. If the creditor is aware of circumstances affecting the risk, he should make the surety equally aware. Similarly, in a case before the Lahore High Court, fresh guarantees were obtained for the fidelity of a manager of a bank without disclosing his previous defalcations, the sureties were held not liable for further defalcation.<sup>48</sup>

Lord CHELMSFORD observed with regard to a guarantee other than a guarantee of fidelity that a creditor is under no obligation to inform an intended surety of matters affecting the credit of the debtor, or of any circumstances connected with the transaction in which he is about to engage which will render the position hazardous.<sup>49</sup> To the same effect is an observation in a Scottish case. There is nothing in "authorities for holding that the fact that suspicious circumstances arise to the knowledge of a creditor, and are not communicated at once to the cautioner is a ground for holding a cautioner freed from his obligation".<sup>50</sup> Referring to the position of a bank, it was observed in the same case: "There is no authority for the view that it is the duty of a bank, whenever it becomes aware of any circumstances seriously affecting the credit of a customer, to communicate at once with

47. (1912) 2 KB 72 (CA).

48. *Coop Commission Shop Ltd v Udhamp Singh*, AIR 1944 Lah 424.

49. *Wythes v Labouchere*, (1859) 3 De G&J 593.

50. *Bank of Scotland v Morrison*, 1911 SC 593, Scotland. Where the nature of the transaction showed that the whole tenor of guarantee papers was concealed from the surety and he was made to sign the last page only, the court held that the guarantee letter did not seem to be genuine. Facts further showed that the borrower was prosecuting a criminal case against the surety. *Union Bank of India v M.P. Sreedharan Kartha*, AIR 1993 Ker 285.

any of that customer's friends who may have cash credits on his behalf or guarantees for his pecuniary obligation.”<sup>51</sup>

#### 4. Writing not necessary

Section 126 expressly declares that a guarantee may be either oral or written.<sup>52</sup> But in England under the provisions of the Statute of Frauds a guarantee is not enforceable unless it is “in writing and signed by the party to be charged”.<sup>53</sup>

### EXTENT OF SURETY'S LIABILITY

The fundamental principle about the surety's liability, as laid down in Section 128, is that the liability of the surety is co-extensive with that of the principal debtor. The surety may, however, by an agreement place a limit upon his liability. The section is as follows:

**S. 128. Surety's liability.**—The liability of the surety is co-extensive with that of the principal debtor, unless it is otherwise provided by the contract.

51. The creditor (a bank in this case) is under a duty to disclose to the surety contractual arrangements between the principal debtor and the creditor which made the terms of the principal contract something materially different in a particularly disadvantageous respect to those which the surety might actually expect, *Levett v Barclays Bank plc*, (1995) 1 WLR 1260. In a suit on a deed of guarantee, the plea that the blanks in the deed were filled in subsequently was not sustainable because all entries were initialled.
52. Since an oral guarantee is also valid, a person who otherwise appeared to be a guarantor was held liable though his signature did not appear on guarantee papers. *P.J. Rajappan v Associate Industries (P) Ltd*, (1990) 1 KLJ 77. A written guarantee may be spelled out from more than one documents. *S. Chattanatha Karayalar v Central Bank of India Ltd*, AIR 1965 SC 1856: (1965) 3 SCR 318. A written guarantee would have to satisfy the requirements of the Stamp Act. *Karnataka State Industrial Investment & Development Corp Ltd v State Bank of India*, (2005) 1 CLT 437: (2004) 3 CCC 568 (Kant), a guarantee in writing remains enforceable even if stamp duty is not paid, because stamp duty can be paid at any subsequent stage. *Shri Bishwakarma Furniture Workshop v Santanu Sarkar*, (2006) 5 AIR Kant (NOC) 762 (Jha): AIR 2006 Jhar 89: 2006 AIHC 2511, defendant guaranteed repayment of loan, failure of borrower to pay back amount deducted from the guarantor's fixed deposit. Guarantor sued the borrower and the latter was held liable to reimburse the guarantor. But registration is not compulsory. See *Karnataka State Industrial Investment and Devp Corp Ltd v SBI*, (2004) 4 Kant LJ 266 (DB), where the court also held that though the transaction is a tripartite arrangement, all the parties have not to execute it simultaneously.
53. S. 4. *Actionstrength Ltd v International Glass Engg IN.GL.EN SpA*, (2002) 1 WLR 566 (2) (CA), a person may incur liability under an oral guarantee if he is estopped by reason of his representations or conduct from contending that the guarantee was oral. However, no such estoppel could be shown in this case. There was no representation by the employer company to the sub-contractor that it would honour the agreement despite the absence of writing or that it would confirm the oral agreement by writing. Another off shoot of the same litigation was in *Actionstrength Ltd v International Glass Engg IN.GL.EN SpA*, (2002) 1 WLR 566 (2): (2002) 4 All ER 468 (CA), a promise is not capable of becoming a guarantee if the promiser undertakes liability in respect of assets or sources within his control, vide S. 4, Statute of Frauds, 1877. *C.S. Co v Punjab & Sind Bank*, (2003) 3 KLT 808, no suit can safely be decreed on the photostat copy of the bank guarantee, terms and conditions can be given effect to only when the guarantors are produced.

*Illustration*

A guarantees to B the payment of a bill of exchange by C, the acceptor. The bill is dishonoured by C. A is liable not only for the amount of the bill but also for any interest and charges which may have become due on it.

### 1. Co-extensive

The first principle governing surety's liability is that it is co-extensive with that of the principal debtor. The expression "co-extensive with that of the principal debtor" shows the maximum extent of the surety's liability. He is liable for the whole of the amount for which the principal debtor is liable and he is liable for no more.<sup>54</sup> The only illustration appended to the section says that if the payment of a loan bond is guaranteed, the surety is liable not only for the amount of the loan, but also for any interest and charges which may have become due on it.<sup>55</sup> Where the principal debtor acknowledges liability and this has the effect of extending the period of limitation against him the surety also becomes affected by it.<sup>56</sup>

Where the overdrafts of a company were guaranteed by the company's directors and the banker had recovered a part of the loan by disposing of

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54. Thus a guarantor of rent was held not liable for interest on rent because the principal debtor himself was not so liable. *Maharaja of Benares v Har Narain Singh*, ILR (1906–07) 28 All 25. Under the agreement in this case, and even otherwise, the surety is liable not only for the principal amount but for interest on the principal amount and charges incurred in enforcing the liability. The court held that the trial court erred in decreeing the suit against the surety for only the principal amount excluding interest and costs. *Indian Over Seas Bank v G. Ramulu*, (1999) 2 ALD 104.

55. For a parallel case see *Nandlal Chogalal v Surajmal Gangaram*, AIR 1932 Nag 62. The expression "co-extensive" also shows the nature of liability. Thus where in a suit against the principal debtor and surety, the principal debtor was ordered to pay in instalments and the suit against the surety was dismissed, this dismissal was held to be not proper. *SBI v Sajita Engg Works*, AIR 1992 Ori 237. The court followed the decision of the Supreme Court in *Bank of Bihar Ltd v Damodar Prasad*, AIR 1969 SC 297: (1969) 1 SCR 620 and *Nanda Dulal Sen v Rao & Sons*, (1972) 38 Cutt LT 959 where it was held that the decree against the surety would not be executed till the principal debtor paid off the dues by instalments allowed by the court and thus the liability of the guarantor was not wiped out. In all proceedings against the principal debtor, his sureties are a proper party. *Industrial Finance Corpn of India v P.V.K. Papers Ltd*, AIR 1992 All 239. This is so because the liability is joint and several. *Suresh Narain Sinha v Akhaura Balbhadr Prasad*, AIR 1957 Pat 256; *Madho Sah v Sitaram Sah*, AIR 1962 Pat 405. The period of limitation against the principal debtor and the surety is the same, *Union Bank of India v Suresh Bhailal Mehta*, AIR 1997 Guj 48; *D. Pandi v Dhanalakshmi Bank Ltd*, AIR 2001 Mad 243, signature of the surety on bank loan and guarantee documents proved, surety liable. *E.P. George v Bank of India*, AIR 2001 Ker 107, a guarantor is also a debtor and if the creditor is demanding a security from the surety also, he should be able to provide security by an equitable mortgage of his property.

56. *Bank of India v Surendra Kumar Mishra*, (2003) 1 BC 45 (Jhar): (2003) 1 Bankmann 551; *Vyasya Bank Ltd v DGFT*, (2003) 6 ALD 241, liability wholly depends upon the terms of the contract. Writ petition not allowed for knowing whether interest was payable. Civil suit advised. *Kailash Nath Agarwal v Pradeshiya Industrial & Investment Corpn of U.P. Ltd*, (2003) 4 SCC 305: AIR 2003 SC 1886, joint and several liability created under a guarantee bond.

certain goods belonging to the company, the Madras High Court held that the liability of the surety had gone down accordingly.<sup>57</sup>

Under the guarantee clause, the guarantor agreed to be bound by any judgment or award obtained by the lender bank against the principal debtor. It was accordingly held that a settlement or compromise between the bank and the principal debtor was binding upon the guarantor. The mere absence of knowledge on the part of the guarantor of the joint settlement memo was of no consequence.<sup>58</sup>

One of the requirements of an auction notice under the SARFAESI Act, 2002, is that the details of the borrower must be given. The auction notice in this case stated the details only of the guarantor. This was held as not affecting validity of the notice because a guarantor is also a buyer because he is equally (co-extensive) liable with the borrower.<sup>59</sup>

The liability of the guarantor cannot go beyond the terms of the guarantee. A bank was not allowed to recover from the guarantor liability due under pre-existing debts when there was no mention of such liability in the guarantee which had been framed by the bank itself. The Supreme Court however pointed out that this does not mean that no liability can be fastened upon a guarantor for pre-existing debts.<sup>60</sup>

A guarantee was given to a bank for the borrower's loan. The guarantor gave a notice to the bank withdrawing his guarantee. The guarantee carried a provision to the effect that it would cease to exist after the expiry of three months from the date of notice. The court said that the guarantor could not be held liable after such expiry of time.<sup>61</sup>

### *Condition precedent*

Where there is a condition precedent to the surety's liability, he will not be liable unless that condition is first fulfilled. A partial recognition of this principle is to be found in Section 144 which says:<sup>62</sup>

Where a person gives a guarantee upon a contract that creditor shall not act upon it until another person has joined in it as co-surety, the guarantee is not valid if that other person does not join.

57. *Hargopal Agarwal v SBI*, AIR 1956 Mad 211; *Syndicate Bank v K. Manohara*, AIR 2003 Ker 284, the surety and the borrower were held liable jointly and severally. *Central Bank of India v Antony Hardware Mart*, (2006) 3 CTC 285 (Mad), no notice has to be given to the surety before filing a case on him. A decree can be executed against the surety without first proceeding against the principal debtor.

58. *Central Bank of India v C.L. Vimla*, (2015) 7 SCC 337: (2015) 3 SCC (Civ) 601.

59. *Jagdish Sarda v SBI*, AIR 2016 Cal 2.

60. *Central Bank of India v Virudhunagar Steel Rolling Mills Ltd*, (2016) 3 SCC (Civ) 664: (2016) 2 CHN 98.

61. *Amal Krishna Ray v Bank of Baroda*, AIR 2014 (NOC) 179 (Ori).

62. This shows that rights and liabilities of a surety and borrower are different and distinct and everything depends upon the terms of the guarantee. See, *Global Trade Finance Ltd v Sudarshan Overseas Ltd*, (2010) 4 Mah LJ 367.

An illustration in point is *National Provincial Bank of England v Brackenbury*.<sup>63</sup>

The defendant signed a guarantee which on the face of it was intended to be a joint and several guarantee of three other persons with him. One of them did not sign. There being no agreement between the bank and the co-guarantors to dispense with his signature, the defendant was held not liable.

The same result followed where the signature of the co-guarantor was forged so as to make it appear that he had joined.<sup>64</sup> The facts were:

The plaintiff supplied timber to a company of which the defendant was a director. The company being unable to pay, the plaintiff agreed to suspend the claim for a year provided that the debt was jointly and severally guaranteed by the company's three directors. A guarantee apparently signed by the defendant and other directors was duly provided. The company went into liquidation. The plaintiff sought to enforce the guarantee. Before the trial of the action it was discovered that the signature of one of the directors had been forged.

The court said: "A joint guarantor under a guarantee which showed on its fact that the other joint guarantors were intended to be parties is not liable at law if the signature of one of the other guarantors is forged, since there is no contract of guarantee unless all the anticipated parties to the contract in fact became bound."

#### *Proceeding against surety without exhausting remedies against debtor*

Where the liability is otherwise unconditional, the court cannot of its own introduce a condition into it. This was pointed out by the Supreme Court in *Bank of Bihar Ltd v Damodar Prasad*.<sup>65</sup>



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63. (1906) 22 TLR 797.

64. *James Graham & Co (Timber) Ltd v Southgate Sands*, 1986 QB 80.

65. AIR 1969 SC 297: (1969) 1 SCR 620. See also *Lakhi Ram Ram Dass v Har Prasad Syal*, (1972) 3 SCC 337: AIR 1971 SC 1956. In *Satwant Singh Kochhar & Co v Punjab National Bank*, (1985) 27 DLT 441, where it was held that there was nothing wrong in directing the sale of guarantor's share in the property first. In *Chalamani Narasa Reddy v Collector*, (1987) 2 An LT 969, where it was held that it was not legal for the mortgagee to proceed against guarantor straightforwardly. *Tirputti Plywood Product (P) Ltd v Pradeshk Industrial Investment Corp of U.P. Ltd*, AIR 1997 All 364, guarantor can be sued directly without seeking remedies against principal debtor. *Naba Kishore Sahoo v United Bank of India*, 1995 AIHC 2176 (Ori), the guarantor cannot say that the decree should first be executed against the borrower and against him only for the balance. *P.C. Ravi v Union Bank of India*, 1995 AIHC 2168 (Ker), failure to implead legal representatives of the principal debtor is not a ground for setting aside the suit against the surety. *Pawan Kumar Jain v Pradeshiya Industrial and Investment Corp of U.P. Ltd*, 1998 AIHC 1360 (All), initiation of recovery proceedings only against the guarantor held to be illegal. *Vasundhara Oil Industries (P) Ltd v Collector*, (1998) 33 ALR 29, recovery officers first proceeding against the pledged and mortgaged property of the guarantors, held, nothing illegal. *Govt of A.P. v State Bank of Hyderabad*, (1993) 2 An WR 65 (DB), Government guarantor, could not say that other avenues of liability should be tried first. *Kantilal R. Shah v Central Bank of India*, (1995) 2 GLH 952, proceedings against surety

The defendant guaranteed a bank's loan. A default having taken place, the defendant was sued. The trial court decreed that the bank shall enforce the guarantee in question only after having exhausted its remedies against the principal debtor. The Patna High Court confirmed the decree. But the Supreme Court overruled it.

Explaining that a condition of this kind would defeat the parties' intention, the court said: "The very object of the guarantee is defeated if the creditor is asked to postpone his remedies against the surety. Is the creditor to ask for imprisonment of the principal? Is he bound to discover at his peril all the properties of the principal and sell them; if he cannot, does he lose his remedy against the surety? Has he to file an insolvency petition against the principal? The trial court gave no reason for this extraordinary direction. It said that the principal was solvent. But the solvency of the principal is not a sufficient ground for restraining execution of the decree against the surety. It is the duty of the surety to pay the decretal amount. On such payment he will be subrogated to the rights of the creditors."<sup>66</sup>

And as so subrogated may exhaust his remedies against the creditor. "Before payment the surety has no right to dictate terms to the creditor and ask him to pursue his remedies against the principal in the first instance. The surety is a guarantor; and it is his business to see that the principal pays, and not that of the creditor."

The Allahabad High Court<sup>67</sup> has also taken the similar view although without reference to the Supreme Court ruling. The loans of a company were guaranteed. The guarantee stipulated that the liability of the surety would arise on demand. There was no condition that the financial corporation should first proceed to recover the amount from the hypothecated property. The corporation could straightaway proceed against the surety without first proceeding against the company. The order directing the corporation to first proceed against the company was held to be not proper.

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alone, maintainable. *D.F.C. Financial Services v Coffey*, (1991) BCC 218 PC, guarantor of a debenture allowed to be proceeded against without making any demand on the company for payment. *P.N. Ravi v Kottayam Coop Urban Bank*, (1993) 1 KLJ 538, notice of default to the surety and proof of default are necessary. *Hiranyaprava Samantray v Orissa State Financial Corpn*, AIR 1995 Ori 1, guarantor is entitled to prior notice on principles of natural justice. Without such notice an action against the guarantor for shortfall cannot be instituted. Such notice should have been given before the auction sale of security. *Varghese v Dhanalakshmi Bank Ltd*, (1997) 1 KLT 843, the secretary of a society guaranteed a loan in his individual capacity, it was not necessary to join the society as a pro forma defendant. *Ram Bahadur Singh v Tehsildar*, AIR 2002 All 344, the creditor may proceed straightway against the guarantor without first proceeding against the principal debtor.

66. *Bank of Bihar Ltd v Damodar Prasad*, AIR 1969 SC 297; (1969) 1 SCR 620. *Sunder Singh v Punjab National Bank*, AIR 1992 All 132, execution of decree against surety before proceeding against principal debtor and hypothecated property. *Kerala State Financial Corpn Ltd v C.J. Thampi*, AIR 2000 Ker 36, it was not proper for the court to direct that an order against the surety should not be passed because the defaulting chitty subscriber's husband was financially well off.

67. *U.P. Financial Corpn v Garlon Polyfab Industries*, AIR 2001 All 286.

In a subsequent case, the Supreme Court held that the creditor must proceed against the mortgaged property first and then only against the surety for the balance,<sup>68</sup> even if the decree is a composite one against the principal debtor, mortgaged property and the guarantor. In that case only a portion of the decree was covered by the mortgage and the court did not consider it relevant whether the two portions of the decree were severable or not. This decision has been overruled by the Supreme Court in *SBI v Indexport Registered*.<sup>69</sup> In this case a composite decree was passed against the surety, the borrower and the mortgaged property of the borrower. The High Court of Delhi<sup>70</sup> directed that the decree-holder should first proceed against the mortgaged property and levy execution against the surety only for the balance. YOGESHWAR DAYAL J said:<sup>71</sup> "In the present case the decree does not

68. *Union of India v Manku Narayana*, (1987) 2 SCC 335: AIR 1987 SC 1078. In contrast to this see *Kwong Yik Finance v Mutual Endeavour*, (1989) 1 Mal LJ 135 (HC Kuala Lumpur) where it was held that guarantors' liabilities are personal liabilities and are in no way affected by the charge created in favour of the creditor and, therefore, the guarantors cannot say that the creditors could only proceed against them if there was a shortfall in the proceeds of the sale realised by the foreclosure of the charged property; *Punjab National Bank v Surendra Prasad Sinha*, 1993 Supp (1) SCC 499: AIR 1992 SC 1815 where the Supreme Court permitted the securities deposited by the guarantor to be realised though the debt had become time-barred.

69. (1992) 3 SCC 159: AIR 1992 SC 1740.

70. In its decision of 23-4-1990, Civil Appeal No. 7434 of 1990.

71. *SBI v Indexport Registered*, (1992) 3 SCC 159: AIR 1992 SC 1740. Followed by the Kerala High Court in *SBI v G.J. Herman*, AIR 1998 Ker 161 where the court held that in the case of a composite decree, the court or the co-surety cannot insist that the creditor should proceed against other sureties before proceeding against him. It is the creditor's option to decide for himself against whom he should proceed first. The surety so selected for recovery would have the right to recover contribution from the co-sureties and indemnity from the principal debtor. The absence of decree against the principal borrower is no ground for setting aside the decree against the surety, *Balakrishnan v H. Chunnil Bagmar*, AIR 1998 Mad 175; *SBI v M.P. Iron and Steel Works (P) Ltd*, AIR 1998 MP 93, action against directors guaranteeing the company's loan was held to be maintainable even when proceedings against the principal debtor company were pending. The bank was not bound to wait for the result of the action against the company. The application of the bank to attach the proceeds of the director's personal account in the bank was allowed. *Permata Merchant Bank v Glove Seal*, (1994) 1 Curr LJ 389 (Malaysia), the bank was not bound to exhaust other remedies before embarking on the action based on the guarantee agreement. The lending bank was under no duty to the guarantors as to how it dealt with the other securities. *SBI v Goutmi Devi Gupta*, AIR 2002 MP 61: (2003) 1 BC 165, the decree holder cannot be directed to proceed against the hypothecated property first. *Industrial Investment Bank of India v Biswanath Jhunjhunwala*, (2009) 9 SCC 478, the SC reiterated that the decree holder can execute the decree against the guarantor without proceeding against the principal debtor. *Bansilal v Punjab National Bank*, (2010) 1 Mah LJ 101, money decree obtained by the bank against the principal debtor and guarantor, if the bank could execute the decree against one or the other as per its choice. *Bank of Baroda v J.K. Chemicals*, (2010) 5 Mah LJ 448, guarantors were not allowed the defence that their signatures were under duress, they alongwith other defendants were held jointly and severally liable to pay the decree with interest at 12 per cent.

This position was reaffirmed by the Supreme Court in *Central Bank of India v C.L. Vimla*, (2015) 7 SCC 337: (2015) 3 SCC (Civ) 601, where it was observed that it is a prerogative of the creditor alone whether he would move against the principal debtor first or surety for realising the loan amount. Rulings on the point, however, continue to be contradictory. It is too much that a helper should be put under the whole burden and the borrower should be allowed to enjoy his enriching assets. *Ram Kishun v State of U.P.*, (2012) 11 SCC 511: (2012) 173 Comp Cas 105: (2012) 4 All LJ 653, in this case a farmer had taken a loan, he died

postpone the execution. The decree is simultaneous and it is jointly and severally (passed) against all the defendants including the guarantor. It is the right of the decree-holder to proceed with it in a way he likes.”

The court conceded that the way in which a decree is drawn up is an important fact to be considered. “If the composite decree is a decree which is both a personal decree as well as a mortgage decree, without any limitation on its execution, the decree-holder, in principle, cannot be forced to first exhaust the remedy by way of execution of the mortgage decree alone and told that only if the amount recovered is insufficient, he can be permitted to take recourse to the execution of the personal decree.

Where, on the other hand, the sale proceeds of the hypothecated truck were already realised and adjusted against the decreed amount, it was held that the guarantor had no right to say that the decree-holder should have first tried to recover the balance of the decreed amount by enforcing the decree against the guarantor. The decree-holder may at his choice enforce the decree either against the principal debtor or surety.<sup>72</sup> A decision of the Punjab and Haryana High Court has the effect of introducing a human aspect. The court said that if the principal debtor is financially well off and can discharge his liability under the decree, the creditor should in the first instance require him to pay and only then he may be allowed to proceed against the surety.<sup>73</sup>

The Supreme Court<sup>74</sup> has also held that where the management of a company has been taken over under an Act<sup>75</sup>, that does not discharge the guarantors of the company's loans. VENKATRAMIAH J said:<sup>76</sup> “Under Section 128 of the Indian Contract Act, 1872, save as provided in the contract, the liability of the surety is coextensive with that of the principal debtor. The surety thus became liable to pay the entire amount. Their liability was immediate and it was not deferred until the creditor exhausted his remedies against the principal debtor. The Act does not say that when a notification is issued under Section 7(1)(b) the remedies against the guarantors also stood suspended.”

#### *Action against principal debtor alone*

The creditor can proceed against the principal debtor alone. His suit cannot be rejected on the ground that he has not joined the guarantor as a defendant to the suit.<sup>77</sup> Dismissal of the suit against the principal debtor

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without paying back, within a year his father who was a guarantor also died, his legal heirs were hauled up, their lands sold, whereas the principal debtor had more land resources, he remained untouched. The legal heirs had lost everything, might be with no means to recover their indemnity. This is one of the consequence of creating multiplicity of proceedings.

72. *Nikunja Kishore Pradhan v SBI*, (1990) 70 Cut LT 416.

73. *Panpori v Central Bank of India*, (2002) 1 ICC 838 1 (P&H).

74. *SBI v Saksaria Sugar Mills Ltd*, (1986) 2 SCC 145: AIR 1986 SC 868.

75. Sugar Undertaking (Taking over of Management) Act, 1978.

76. *SBI v Saksaria Sugar Mills Ltd*, (1986) 2 SCC 145 (146): AIR 1986 SC 868.

77. *Union Bank of India v Noor Dairy Farms*, (1997) 3 Bom CR 126.

does not of itself absolve the surety of his liability under the contract of guarantee.<sup>78</sup>

A surety was allowed to be impleaded where his liability had already been reduced and his position would have been prejudiced if in the proceedings against the principal debtor this fact was not brought to the notice of the deciding authority.<sup>79</sup>

### *Suit against surety alone*

A suit against the surety without even impleading the principal debtor has been held to be maintainable. In this case, the creditor, in his affidavit, had shown sufficient reasons for not proceeding against the principal debtor.<sup>80</sup> A contract of guarantee was made enforceable by its terms against the guarantors severally and jointly with that of the principal debtor company. It was held that the creditor had the option to sue the company along with guarantors as co-defendants or guarantors alone.<sup>81</sup>

This makes the position of sureties specially vulnerable. The court may rescue the surety where he was prevailed upon and, therefore, his consent was not free. A surety may be described as vulnerable where there is a relationship of trust and confidence between him and the debtor.<sup>82</sup> In this case, the wife stood surety for her husband's debts. She received no independent

78. *Karnataka State Industrial Investment and Devp Corp Ltd v SBI*, (2004) 4 Kant LJ 266 (DB); *Kurnool Chief Funds (P) Ltd v P. Narasimha*, AIR 2008 AP 38, suit against the principal debtor was dismissed for default and that decision had become final, no liability survived against the principal debtor, liability of the surety ended.

79. *B.R. Thadani v Oriental Bank of Commerce*, (2002) 2 Bom CR 263.

80. *N. Narasimhaiah v Karnataka State Financial Corp*n, AIR 2004 Kant 46, a surety can be proceeded against without suing the principal debtor. *Infrastructure Leasing & Financial Services Ltd v Vijaya V. Prabhu*, AIR 2010 Bom 72, to the same effect.

81. *Vijay Singh Padode v Sicom Ltd*, (2000) 4 Mah LJ 772; *Kailash Chand Jain v U.P. Financial Corp*n, AIR 2002 All 302, S. 29 of the State Financial Corp Act, 1951 permits certain remedies to the corporation, one of which is to proceed against the guarantors who were directors of the borrower company. They were not permitted to say that the corporation should have first tried to realise the value of the unit of the borrower company which it had taken over. *State of Gujarat v State Bank of Saurashtra*, AIR 2003 NOC 437 (Guj); guarantor allowed to be sued despite takeover of the unit of the borrower. *Syndicate Bank v Wilfred D'Souza*, AIR 2003 Kant 337, exercising lien over the bank balance of the guarantor after default by the borrower held to be valid and not violative of Article 14, the step being necessary to protect the bank's financial interest. *H.P. Jalajakshi v Karnataka Bank*, AIR 2003 Kant 280, attachment of the salary of the surety not allowed where the principal debtor was regularly paying the instalments. *V. Ramanujam v Karnataka State Financial Corp*n, 2002 SCC OnLine Kar 616: 2003 AIR Kant R 473, the right of the principal to proceed against surety alone is not affected by other laws unless there is a provision to that effect. *SICOM Ltd v Harjindersingh*, AIR 2004 Bom 337, guarantors cannot argue that where no suit was instituted against the principal debtor, a suit against guarantors alone would not be permissible. *Sheila B. Das v P. R. Sugasree*, (2006) 3 Mah LJ 567, the trial court not correct in directing the plaintiff to first proceed against principal debtor. *Don Ayengia v State of Assam*, (2016) 3 SCC 1, a person guarantees the payment of a cheque, may become liable as a guarantor and if the obligation remains unfulfilled, he may also become liable to be prosecuted under Section 138 of the Negotiable Instruments Act, 1881, if the other requirements of the section are fulfilled, e.g., that the cheque was issued for discharge of a debt or other liability.

82. *Barclays Bank Plc v O'Brien*, (1994) 1 AC 180: (1993) 3 WLR 786 (HL).

advice. The court freed her from liability either because of undue influence or mis-representation. Such vulnerability is not limited to spouses. It would include co-habitants and others, e.g. elderly parents.

In such cases relationship of trust and confidence often exists and is provable. It is necessary that the bank should have notice of the fact that the surety was in a position of manifest disadvantage and this should put the bank on enquiry as to whether to accept such a surety or not.<sup>83</sup>

#### *Proceeding against guarantor's mortgaged property*

A financial corporation cannot take possession of the mortgaged property of the guarantor without notice to him. The corporation also cannot issue a public notice for auction sale of the property without notice to the guarantor. The reason is that the liability of the guarantor is secondary and arises only when the borrower fails in repayment. A guarantor is bound by his own separate agreement to which the principal debtor is not a party.<sup>84</sup> The petitioner was a surety for a loan advanced by the State Industrial Corpn to the borrower. It was held that the corporation had no power to take possession of the property of the surety under Section 29 of the State Financial Corporations Act, 1951 and bring the property for sale without aid of the court.<sup>85</sup> The LIC policy which had been deposited by the guarantor in support of his guarantee was held to be available to the creditor for the amount due under it.<sup>86</sup> The property of the surety which has been offered as a security can be proceeded against without exhausting remedies against the principal debtor. In this particular case the whereabouts of the principal debtor were not known even to the surety. He could not seek protection under the guise that he was ignorant of the consequences of offering his property as a security for the loan of the principal debtor.<sup>87</sup>

#### *Agreement to be bound by any acknowledgement, etc by principal debtor about indebtedness*

The sureties had agreed in the deed of guarantee to be bound by any admission, acknowledgement or part payment by the borrower. The sureties were held to be bound by such agreement. They were not allowed to disown

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83. *Royal Bank of Scotland v Ettridge (No. 2)*, (1998) 4 All ER 705 (CA).
  84. *Amulya Lal Chowdhury v Tripura Industrial Development Corpn Ltd*, AIR 2007 Gau 113.
  85. *Prakashwati Jain v Punjab State Industrial Development Corpn*, AIR 2012 P&H 13, the Full Bench ruling of P&H High Court in *Paramjit Singh Abuja v PSIDC*, 2006 RD P&H 8393 in which such action of the corporation was held to be justified was regarded as not good law in view of implied overruling by the Supreme Court in *Karnataka State Financial Corpn v N. Narasimhaiah*, (2008) 5 SCC 176: AIR 2008 SC 1797. The sale was set aside.
  86. *Vimal Kishore Tiwari v District Development Authority, Lucknow*, AIR 2010 NOC 401 (All DB).
  87. *A. Mohamed Ali v T.N. Industrial Investment Corpn Ltd*, AIR 2009 Mad 44 (DB); *Central Bank of India v Sion Bakers and Confectioners (P) Ltd*, (2008) 5 Mah LJ 772, a person who signs a document which contains a contractual assumption is normally bound by it even though he might not have read it or ignored the precise legal effect.

the acknowledgement made by the borrower. There was nothing in it which could be taken to be contrary to law or opposed to public policy.<sup>88</sup>

#### *Prosecution of guarantor-surety for bouncing of his cheque*

Where the guarantor had issued a cheque as a security for repayment of loan, but the cheque bounced, the court said that he was liable to be prosecuted under Section 138 of the Negotiable Instruments Act. It was no defence that he had not issued the cheque for discharge of personal liability or debt.

#### *Death of principal debtor*

A suit was filed against the principal debtor and surety. The suit against the principal debtor was found to be void *ab initio* because of his death even before institution of the suit. The surety was held to be not discharged. The suit could proceed against him. It was in the interest of the surety to implead under Order 1, Rule 10, CPC, the legal representatives of the deceased principal debtor, because if the suit was decreed against him, the surety could enforce against the legal representatives his rights under Section 145.<sup>89</sup>

#### *Winding up of principal debtor company*

The lending corporation had failed to recover the debt from the borrower company. The liability of the company was held to be confined only to the debt when winding up order was passed. Debt and interest freezed on such order. The corporation was a party to the winding up proceedings. It did not opt out of the same, nor sought permission of the court under Section 446 of the Companies Act to start its own case. Hence, it could not claim anything beyond the amount determined by the official liquidator.<sup>90</sup>

## **2. Surety's right to limit his liability or make it conditional**

It is open to the surety to place a limit upon his liability. He may expressly declare his guarantee to be limited to a fixed amount, for example, that "my liability under this guarantee shall not at any time exceed the sum of £250".<sup>91</sup> In such a case, whatever may be owing from the principal debtor,

88. *P. Jagdeshwar Reddy v Bank of Maharashtra*, AIR 2011 NOC 397 (AP).

89. *Syndicate Bank v A.P. Manjunath*, (1999) 2 Kant LJ 362. The court followed the decision in *Orissa Agro Industries Corp v Sarbeswar Guru*, AIR 1985 Ori 270, where also the suit was allowed to proceed against the surety. Since the creditor has the option of suing either the principal debtor or the surety or any one of the sureties without impleading the principal debtor, it cannot be said that the dismissal of the suit under Order 1, CPC against the principal debtor would automatically discharge the surety.

90. *Anil Kumar v Haryana Financial Corp*, AIR 2011 P&H 140.

91. See *Hobson v Bass*, (1871) LR 6 Ch App 792. The surety may insert any other condition to his liability, e.g. that he would be liable if the performance was defective in certain respects. See *Nanyang Insurance Co v A Chin Kim Hin*, (1992) 1 Curr LJ 454 (Malaysia), following, *Edward Owen Engg Ltd v Barclays Bank International Ltd*, 1978 QB 159; *Malayan United Bank v Straits Central Agencies (Sarawak)*, (1990) 2 MLJ 254.

the liability of the surety cannot go beyond the sum so specified. Thus in a case before the Andhra Pradesh High Court,<sup>92</sup> a clause in a contract of suretyship making the surety liable up to Rs 15,000 further declared that he would be liable for any amount that might be finally decreed. It was held that the clause should be construed as meaning not exceeding Rs 15,000.

A surety can attach any other condition to his liability. Thus where the letter of guarantee made it a condition precedent to the guarantor's liability that on default on the part of the borrower a demand for payment should be made upon the guarantor, it was held that an independent demand was necessary and the mere service on the guarantor of the carbon copies of the demand meant for the borrower was not sufficient.<sup>93</sup>

#### *Guarantor's insistence upon collateral security*

Whether the obtaining of a collateral security by a lender is a term or condition precedent to liability being imposed on a guarantor under his guarantee depends on a proper analysis of the contractual relationship between the lender and the guarantor. Where a guarantor seeks to make his guarantee dependent on a third party giving some other valid collateral security, the guarantor has to establish that the giving of the security by the third party formed part of the contract under which the guarantee was given and, accordingly, in the absence of that being established, the guarantor was not permitted to rely on any failure by the lender to provide himself with a valid collateral security even though he might have indicated that he was going to do so. In this case the guarantor, who was also the director and principal shareholder of the company, of his company's debts was not allowed to escape saying that the collateral security in the shape of a company's debenture obtained by the company was not a valid security, the court finding that no proof was available to show that there was any such condition that there should be a valid debenture.<sup>94</sup> The court surveyed authorities on the point.

The authorities appear to be clear that in the final event whether the obtaining of a collateral security by the lender is a term of or a condition precedent to liability on a guarantor under his guarantee is to be determined

92. *Yarlagadda Bapanna v Devata China Yerkayya*, AIR 1966 AP 151; *Aditya Narayan Chouresa v Bank of India*, AIR 2000 Pat 222, the guarantors bound themselves to a particular maximum limit. Their liability was limited to that amount and not beyond that.

93. *Orang Kaya Menteri Paduka Wan Ahmad Isa Shakur v Kwong Yik Bank Berhad Bhd*, (1989) 3 MLJ 155 (SC Kuala Lumpur). Following, *Mokffin With v U.M.B.C.*, (1987) 2 Mal LJ 610 (Malaysia), see also *TCB Ltd v Gray*, 1987 Ch 458 (CA), where the condition was that the lender should obtain from the borrower company a collateral security and he obtained a debenture, it was held that the condition was satisfied even if the debenture turned out to be invalid. *Ganga Lahari v Har Narain*, 1986 Raj LR 538, where the court said that if the decree was not fully satisfied by execution against the principal debtors (also judgment-debtors), then execution petition should be filed against the surety. The court referred to *Tan Kin Shan v V. Che Si*, AIR 1925 Rang 135 where on the basis of S. 145, CPC it was held that a notice required to be given to a surety under this section is a condition precedent to the validity of the order for execution against him.

94. *TCB Ltd v Gray*, 1987 Ch 458 (CA).

by a proper analysis of the contractual relationship between the lender and the guarantor. The starting point is *Traill v Gibbons*.<sup>95</sup> The direction to the jury of ERLE CJ was in these terms: "Then as to the equitable plea, it states an agreement with the defendant that Nixey should sign the deed as co-surety with him; that the society should procure him to execute it, and that if they should not do so the defendant should not be liable. Has such an agreement been proved? The *lender* is usually the party who requires an additional surety, and so it seems to have been here. Still it may be sometimes for the interest of a surety to say, 'unless you get co-sureties to join with me, I will not become surety'. And that is the defence set up here. Has it been proved? The evidence is very slight of any such agreement with the defendant. The defendant himself does not say that *he* required that Nixey should join, but merely that he knew that the society had required it. Did the defendant require it for his own benefit or security, or was there any agreement or understanding on his part, as a condition of his own execution, that Nixey should join? Does it appear that the defendant, before he signed, looked to Nixey at all? On the contrary, he says he did not know until some time afterwards that Nixey had *not* signed." (ERLE CJ's emphasis.)

The same approach was taken in the opinion of the Privy Council expressed by Sir ROBERT COLLIER in *Ward v National Bank of New Zealand Ltd.*<sup>96</sup> "But where it is no part of the contract of the surety that other persons shall join in it, in other words, where he contracts only severally, the creditor does not break that contract by releasing another several surety, the surety cannot, therefore, claim to be released on the ground of breach of contract. It is true that he is entitled to contribution against other several sureties to the same extent as if they had been joint, but the right of contribution among such sureties depends not upon contract but on principles established by Courts of Equity."

In *Greer v Kettle*,<sup>97</sup> the agreement under which the guarantee was given related to a debt "effectively secured by (*inter alia*) 275,000 fully paid shares in the Insurance company" and this fact was specifically referred to in the recital to the guarantee agreement. "The agreement of guarantee must be referred to in greater detail. In it, Mercantile Marine is called 'the corporation', while the words 'the guarantors' mean Parent Trust". It contains one recital only, which runs thus: "Whereas the corporation have at the request of the guarantors advanced to the Austin Friars Trust, Ltd the sum of £2,50,000 on the security of a charge dated March 20, 1929, on the shares particulars of which are set out in the schedule hereto." ... "In these circumstances, it would seem that the legal rights and liabilities of these parties depend upon the true construction and effect of the agreement of guarantee. Indeed, this view was not disputed by either side.... Once it is

95. (1861) 2 F&F 358: 175 ER 1095.

96. (1883) LR 8 AC 755, 765 (PC).

97. 1938 AC 156 (HL).

realised that the debt which Parent Trust are undertaking to guarantee is a debt described as a debt the repayment of which by the principal debtor is secured by a charge on (amongst other shares) the 2,75,000 shares in Iron Industries Ltd, the case (apart from the question of estoppel) becomes, in my opinion, a simple one. It is not a case, as BENNETT J seems to have treated it, of seeking to imply a condition the implication of which is alleged to be inconsistent with other provisions in the document. In other words, as ROMER LJ said, it is not a case of Parent Trust being released from a contractual engagement. It is a case of an attempt to impose upon them a liability which they have never undertaken. The only debt the repayment of which by the principal debtor they undertook to guarantee was a debt secured by a charge on the 2,75,000 shares in Iron Industries, and a debt so secured never in fact existed."

These authorities were considered again in *Byblos Bank S.A.L. v Al-Khudhairy*:<sup>98</sup>

#### *Bank's failure to obtain other securities*

"Counsel for the defendant submitted that where an underlying transaction envisages additional security for the principal indebtedness, a guarantor is released if the additional security is not taken, at least where it is shown that it was the intention of the guarantor that such additional security should be taken. In this case the additional security envisaged but not taken was Al Bunnia's personal guarantee, the deposit by Ron Holdings and (validly executed) charges on Rushingdale's property. In the course of the hearing before this court we were referred to many authorities in support of rival submissions on the formulation of the applicable legal principles, counsel's initial submission for the defendant as set out above being plainly too wide. It is too wide because it would include a case where a lender stipulated for additional security for its own protection and nothing was said or done to cause the lender acting reasonably to know or suspect that the intention of the guarantor was that the giving of such security was a fundamental prerequisite to the validity of his guarantee. [There is] no principle, at law or in equity, why in such a case the giving of the additional security should be treated as an essential prerequisite to the validity of the guarantee, and none of the authorities to which we were referred establishes or supports the existence of such a principle. [U]ltimately counsel for the defendant accepted that to succeed on this appeal on this point he had to show that he had an arguable case on the facts under one or other of the three heads: (a) that on the true scope and ambit of the contract made between the bank and Al-Khudhairy it was an implied term (counsel accepted that it was not an express term) of the contract that Al-Khudhairy's liability on his guarantee was conditional on one or more of the three items of additional security

98. 1987 BCLC 232, 239 *per* NICHOLLS LJ.

being taken by the bank, (b) that it was the continuing common intention of both the bank and Al-Khudhairy that Al-Khudhairy's liability should be conditional in this way; or (c) estoppel. It is clearly impossible to spell out of the documentary evidence that it was a precondition of Al-Khudhairy's liability under his guarantee that the bank should obtain a guarantee from Al Bunnia."

Where the guarantor was supposed to have deposited title deeds by way of equitable mortgage, but no such proof was there because the bank did not produce the original title deeds or even their copy, the guarantor was held not liable.<sup>99</sup>

### Impossibility of main contract

A loan for development and maintenance of bee culture was guaranteed. The surety undertook to be liable jointly and severally to pay off instalments in case of failure on the part of the debtor. The bees died in consequence of a viral infection. There was a total failure of business. The debtor became disabled from paying instalments. The surety could not escape liability under the doctrine of impossibility of performance.<sup>100</sup>

The liability of the surety does not depend upon possibility of the surety being able to realise the amount from the principal debtor.<sup>101</sup> The law on this point was settled by the decision of the Supreme Court in a case where it was observed that the right of the creditor to recover from the guarantor arises out of the terms of the deed of guarantee which are not in any way superseded or brought to nullity merely because the creditor (or guarantor) may not be able to recover anything from the principal debtor.<sup>102</sup>

The guarantors of a company's loans could not escape liability by reason only of the fact that the company's management had totally changed.<sup>103</sup>

### Novation of main contract

Where a father guaranteed his son's business debts and the business was subsequently converted into a company and with the consent of the bank the loan was to be treated as that of the company and the son and his companions were accepted as guarantors, it was held that under the new arrangement, the father had been dropped from the guarantee and hence he was not liable. His property could not be attached for enforcement of the guarantee.<sup>104</sup>

99. *Lakshmi Vilas Bank Ltd v Shreechakra Enterprises*, AIR 2003 Mad 1.

100. *Florence Mabel R.J. v State of Kerala*, AIR 2001 Ker 19.

101. *Syndicate Bank v Narayana Iyer*, (2003) 3 KLT 726.

102. *Industrial Finance Corp of India Ltd v Cannanore Spg & Wvg Mills Ltd*, (2002) 5 SCC 54. To the same effect is *Punjab National Bank v State of U.P.*, (2002) 5 SCC 80.

103. *Punjab National Bank v Lakshmi Industrial & Trading Co (P) Ltd*, AIR 2001 All 28.

104. *Satish Chandra Jain v National Small Industries Corp Ltd*, (2003) 1 All LJ 238 (SC).

### *Changes in surety company*

The defendant company and its promoters borrowed a sum of money from the Industrial Development Corporation. Promoters could make any changes in their company only with the approval of the corporation. But without taking any such approval, they transferred their interest in the company to new company and changed the management of the company. The promoters were not allowed to claim discharge from their personal liability under the guarantee.<sup>105</sup>

**Limitation.**—Where a statutory provision or contract clause requires that first recovery should be effected from the assets of the principal debtor, the Supreme Court held that recovery should be effected against the guarantor only after it becomes ascertained as to how much could be recovered from the principal debtor. The period of limitation for suing the guarantor will start then and not from the date of issue of notice for recalling the amount.<sup>106</sup>

### **Liability under continuing guarantee**

**S. 129. "Continuing guarantee".**—A guarantee which extends to a series of transactions, is called a "continuing guarantee".

#### *Illustrations*

- (a) A, in consideration that B will employ C in collecting the rent of B's zamindari, promises B to be responsible, to the amount of 5000 rupees, for the due collection and payment by C of those rents. This is a continuing guarantee.
- (b) A guarantees payment to B, a tea-dealer, to the amount of £ 100, for any tea he may from time to time supply to C. B supplies C with tea to the above value of £ 100, and C pays B for it. Afterwards B supplies C with tea to the value of £ 200. C fails to pay. The guarantee given by A was a continuing guarantee, and he is accordingly liable to B to the extent of £ 100.
- (c) A guarantees payment to B of the price of five sacks of flour to be delivered by B to C and to be paid for in a month. B delivers five sacks to C. C pays for them. Afterwards B delivers four sacks to C, which C does not pay for. The guarantee given by A was not a continuing guarantee, and accordingly he is not liable for the four sacks.

A guarantee of this kind is intended to cover a number of transactions over a period of time. The surety undertakes to be answerable to the creditor for his dealings with the debtor for a certain time. A guarantee for a single specific transaction comes to an end as soon as the liability under that transaction ends. Take, for instance, the old case of *Kay v Groves*,<sup>107</sup> on which the third illustration given in the section is based. The guarantee was in these terms:

105. *HPSIDC v Manson India (P) Ltd*, AIR 2009 NOC 490 (HP).

106. *Deepak Bhandari v H.P. State Industrial Development Corp Ltd*, (2015) 5 SCC 518; (2015) 3 SCC (Civ) 123. It seems that all guarantors should be wise enough to put in such a clause.

107. (1829) 6 Bing 276: 130 ER 1287.

"I hereby agree to be answerable to *K* for the amount of five sacks of flour to be delivered to *T*, payable in one month." Five sacks were actually supplied and *T* paid for them. Further supplies were made during the same month, for which *T* failed to pay.

The surety was then sued. The court held that it was not a continuing guarantee and, therefore, there was no liability for parcels delivered for various subsequent periods.

Following is an illustration of a continuing guarantee:<sup>108</sup>

I do hereby guarantee the payment of goods to be delivered in umbrellas and parasols to *J* in the sum of £200.

Another instance of a continuing guarantee is:

Messrs Sea & Co, Sirs, the bearer, Mr Thomas Horan, wishes to deal with you for produce, and he asked me to speak for him. I can highly recommend him, and in fact, I will stand good for him to the amount of £50.<sup>109</sup>

The essence of a continuing guarantee is that it applies not to a specific number of transactions, but to any number of them and makes the surety liable for the unpaid balance at the end of the guarantee.<sup>110</sup> In Chorley & Tucker the distinction is thus explained:<sup>111</sup> "A specific guarantee provides for securing of a specific advance or for advances up to a fixed sum, and ceases to be effective on the repayment thereof, while a continuing guarantee covers a fluctuating account such as an ordinary current account at a bank, and secures the balance owing at any time within the limits of the guarantee...."

A guarantee for a cash-credit account has been held to be a continuing guarantee. The sureties could not claim to be discharged from their liability by reason of the fact that the goods in the hypothecated store were changed.<sup>112</sup>

108. *Hargreave v Smee*, (1829) 6 Bing 244: 8 LJCP 46: 31 RR 407.

109. *See v Farey*, (1889) 13 LR NSW 72.

110. The liability of the guarantor to pay remains alive as long as the principal debtor does not clear the account. *Union Bank of India v T.J. Stephen*, AIR 1990 Ker 180. Following the Supreme Court decision in *Margaret Lalita Samuel v Indo Commercial Bank Ltd*, (1979) 2 SCC 396: AIR 1979 SC 102, the court held that the period of limitation commences from the time when the payment is demanded and refused or otherwise denied by the surety. In *Bradford Old Bank Ltd v Sutcliffe*, (1918) 2 KB 833 (CA) it was pointed out that the contract of the surety is collateral and, therefore, a demand on him is necessary to complete the cause of action and set the statute running. The decision of the Supreme Court in *R. Lilavati v Bank of Baroda*, AIR 1987 Kant 2: ILR 1987 Kant 964 at p. 969 is authority for the proposition that in the case of a continuing guarantee, the question of limitation does not crop up at all. *Punjab National Bank v Surinder Singh Mandyal*, AIR 1996 HP 1, guarantee for loan for purchase of bus, debtor became irregular with his repayments, guarantor proposed to pay back if the bank would transfer the bus to him, no response from bank, guarantor not discharged by that reason alone.

111. LEADING CASES ON MERCANTILE LAW (4th Edn by Lord Chorley & Giles, 1962) 332.

112. *SBI v Gemini Industries*, (2001) 3 GCD 1885; *SICOM Ltd v Harjindersingh*, AIR 2004 Bom 337, in the case of continuing guarantee, the bar of limitation does not arise as long as guarantee is running.

A guarantee for the conduct of a servant appointed to collect rents has been held by the Calcutta High Court to be a continuing guarantee.<sup>113</sup> But a guarantee for the conduct of a tenant in paying rent due under the tenancy, whether it be a repeated payment or a single lump sum, has been held to be a guarantee for one transaction and not of continuing nature.<sup>114</sup> It is not permissible to construe a bank guarantee in the light of contemporaneous documents. A bank guarantee has to be construed on its own terms. It delinks itself with other documents of the transaction and operates independently of them. As compared with it, a contract has to be construed, when it is contained in more than one documents, by considering all the documents together.<sup>115</sup> The employment of a person is one transaction and the guarantee for his good conduct is not a continuing guarantee.<sup>116</sup>

### Liability under bank guarantee

A bank guarantee is a sort of an absolute undertaking to pay the amount whenever demanded by the guarantee-holder. It has nothing to do with the state of relations between the guarantee-holder and the person on whose behalf the guarantee was given. While ordinary guarantees are linked to and dependent on the underlying transaction, a bank guarantee is an arrangement where the guarantee is independent of the underlying transaction. There are professional guarantors for whom the issue of guarantees or bonds is a financial service, namely, banks, insurance companies or bond companies who issue guarantees at a certain fee.<sup>117</sup>

113. *Durga Priya Chowdhury v Durga Pada Roy*, AIR 1928 Cal 204: ILR (1928) 55 Cal 154. Liability under a continuing guaranteed can be enforced only after ascertaining the final amount due. See *Punjab National Bank v Sri Vikram Cotton Mills*, (1970) 1 SCC 60: AIR 1970 SC 1973 and *United Commercial Bank Ltd v Okara Grain Buyers Syndicate Ltd*, AIR 1968 SC 1115: (1968) 3 SCR 396, bank held liable in respect of its branches in Pakistan for amounts not forfeited by that Government.

114. *Hasan Ali v Waliullah*, AIR 1930 All 730.

115. *SBI v Mula Sahakari Sakkar Karkhana Ltd*, (2006) 6 SCC 293: AIR 2007 SC 2361.

116. *Sen v Bank of Bengal*, (1919–20) 47 IA 164. A guarantee for a sum certain though payable in instalments is not continuing guarantee. *Bhagvandas Rangildas Vani v Secy of State*, AIR 1926 Bom 465.

117. *State Trading Corpn of India Ltd v Golodetz Ltd*, (1989) 2 Lloyd's Rep 277 (CA). *K.L. Steels Ltd v Maharashtra SEB*, (1998) 2 Bom CR 31, independent nature of the transaction emphasised and no stay granted because there was no plea of irretrievable loss or fraud by the beneficiary. Also to the same effect, *Dwarkesh Sugar Industries Ltd v Prem Heavy Engg Works (P) Ltd*, (1997) 6 SCC 450: AIR 1997 SC 2477; *Orissa Construction Corpn Ltd v B. Engineers & Builders (P) Ltd*, (1996) 81 Cal LT 126, the sub-contractor executed 42 per cent of the total work, the total bank guarantee of Rs 50 lakhs could not be encashed. The court permitted encashment only up to Rs 35.40 lakhs. The court followed *U.P. State Sugar Corpn v Sumac International Ltd*, (1997) 1 SCC 568: AIR 1997 SC 1644; *NTPC Ltd v Flowmore (P) Ltd*, (1995) 4 SCC 515. The bank is not a party to the underlying contract, *State of Maharashtra v National Construction Co*, (1996) 1 SCC 735: AIR 1996 SC 2367. *Krishna Electrical Industries (P) Ltd v SBI*, AIR 1996 MP 188, amount recoverable quantified, requisite notice, opportunity to show cause not required, encashment not stayed. *Food Corporation of India v Arosan Enterprises Ltd*, AIR 1996 Del 126, bank guarantee encashment by buyer not stayed on the allegation that the seller had delivered the goods. *Syndicate Bank v Wilfred D'Souza*, AIR 2003 Kant 337, no term in the guarantee that encashment

A guarantee for the appointment of an agent has been held to be not a continuing guarantee. The use of the word "continued" in the guarantee bond did not make it a continuing guarantee. It only meant that the bond was to remain in force during the subsistence of the agency.<sup>118</sup> In a case on the subject before the Supreme Court:<sup>119</sup>

A bank undertook to pay to the SEB a sum not exceeding Rs 50,000 within 48 hours of demand. The guarantee was submitted on behalf of a supplier who had deposited with the bank sufficient securities. There was no condition to the bank's liability except demand by the Board. The Board demanded payment. The supplier was a company which went into liquidation. The liquidator sought to prevent the Board from realising the guarantee and the bank from paying it.

No such relief was allowed. The Board had the right to enforce payment of the guarantee and the bank had the right to reimburse itself out of the securities. If the liquidator thought that the Board's conduct in realising the guarantee was not proper, he should proceed against the Board.<sup>120</sup> Stating the reasons for the same the Delhi High Court said that if scrutiny is commenced in respect of the underlying contract, obviously the autonomy and independence of an absolute guarantee would be lost. Its enforcement would

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only after liability was determined by the Debt Recovery Tribunal, encashment not stayed. *Mak Impex Chemicals (P) Ltd v Union of India*, (2003) 3 Bom CR 440, failure to fulfil export obligation, encashment not stayed. *Rani Sati Investment & Finance Ltd v Union of India*, AIR 2004 Bom 424: (2004) 4 Bom CR 81, the exporter could not keep his export commitment, no extension of time was granted to him, encashment of his bank guarantee was not stayed.

118. *Mohd Nazeer Ahmed v Economic Transport Organisation*, (2005) 3 ALD 527 (AP).
119. *Maharashtra SEB v Official Liquidator*, (1982) 3 SCC 358: AIR 1982 SC 1497. The money is payable on demand and not on breach. *Dena Bank v Fertilizer Corpn of India*, AIR 1990 Pat 221. Suspension of the contract between the Department and the contractor on account of the latter's defaults did not have the effect of suspending the enforcement of the bank guarantee given by another person for the contractor's due performance. *SCIL (India) Ltd v Indian Bank*, AIR 1992 Bom 131. *Sri Palmar Devt and Construction v Transmetric*, (1994) 1 Curr LJ 224 (Malaysia), a performance bond between a contractor company and its sub-contractor, stay not granted, the court taking the bond as it found it. *Rampur Engg Co Ltd v United Construction Co*, AIR 2002 Del 170, revocation of bank guarantee, negligence of bank in taking necessary steps against debtor and his guarantor for realisation of debt within validity period of guarantee, bank liable to reimburse beneficiary, the court would not intervene only because of a dispute between the beneficiary and the debtor.
120. To the same effect, *Banwari Lal Radhe Mohan v Punjab State Coop Supply and Mktg Federation Ltd*, AIR 1982 Del 357 where the court said that a bank guarantee being absolute, the pendency of arbitration proceedings cannot stand in the way of payment. *Shreeram Cloth Stores v Trading Corpn of Bangladesh*, (1980) 1 CHN 132. The courts do not interfere with the operation of letters of credit due to their importance in international trade and also because the beneficiary is assured by the bank that he would be paid as soon as he complies with the terms of the letter of credit. This is irrespective of his non-compliance with the terms of his contract with the other party. Letters of credit become autonomous documents. *SBI v Economic Trading Co*, AIR 1975 Cal 145; *Kunjannamma v Kerala Fisheries Corpn*, 1986 KLT 37; *Rani Sati Investment & Finance Ltd v Union of India*, AIR 2004 Bom 424: (2004) 4 Bom CR 81, bank guarantee for performance of export contract, no export of cotton within specified time, encashment justified.



depend upon the result of an inquiry. This would defeat the very purpose of a bank guarantee.<sup>121</sup>

In *Hindustan Steelworks Construction Ltd v Tarapore & Co*<sup>122</sup> the Supreme Court laid down the law in terms of the following propositions:

“(A) A bank guarantee is an independent and distinct contract between the bank and the beneficiary and is not qualified by the underlying transaction and the primary contract between the person at whose instance the bank guarantee is given and the beneficiary.

(B) In the case of an unconditional bank guarantee the nature of the obligation of the bank is absolute and not dependent upon any dispute or proceeding between the party at whose instance the bank guarantee is given and the beneficiary.

(C) .....

(D) The commitment by banks must be honoured free from interference by the court and it is only in exceptional cases, that is to say, in case of fraud, or in a case where irretrievable injustice would be done if bank guarantee is allowed to be encashed, that the court would interfere.”

Some litigation in connection with bank or demand guarantees is generated by the fact that there can be abusive or unfair callings, which is to a large extent due to the independent nature of both documentary credits and unconditional on demand guarantees. The beneficiary's right to payment is absolute or almost absolute. Apart from the court stay order, one method which has been suggested and which has been put to actual use is the requirement that the beneficiary has to state in his letter invoking bank guarantee that there has been some kind of breach of the underlying transaction and what is the type of breach which is involved.<sup>123</sup> The person

121. *Banwari Lal Radhe Mohan v Punjab State Coop Supply and Mktg Federation Ltd*, AIR 1983 Del 86, 89. *Daewoo Motors India Ltd v Union of India*, (2003) 4 SCC 670: AIR 2003 SC 1786, bank guarantee for fulfilment of export obligations, encashment on failure to do so not stayed. *Virdichandji Garg v Fiat India (P) Ltd*, AIR 2004 Bom 462, it is necessary to state specifically in the letter invoking the guarantee details of the invoices and outstanding amount, invocation has to be in terms of the guarantee itself and not in terms of the contract between the parties.
122. (1996) 5 SCC 34: AIR 1996 SC 2268. *Himadri Chemicals Industries Ltd v Coal Tar Refining Co*, (2007) 8 SCC 110: AIR 2007 SC 2798, an injunction can be granted only in cases of egregious fraud and irretrievable loss, a dispute between the parties is not a sufficient ground in itself. *Org Informatic Ltd v Tulip Telecom Ltd*, AIR 2011 NOC 258 (Del), bank guarantee not stayed because there was neither any fraud in claiming encashment nor any chance of the money going beyond recovery.
123. See Lars Gordon, *Draft UNCITRAL Convention on Independent Guarantees*, (1997) JBL 240 at 244. Writ cannot be issued in the matter of enforcement of bank guarantee unless some public law element is involved, *A.C. Roy & Co v Union of India*, AIR 1995 Cal 246. See, for example, *National Telecom of India Ltd v Union of India*, AIR 2001 Del 236, the Government was required to show at least one of two conditions for invoking guarantee, i.e., either that the amount had become due because of loss caused by breach or that the amount was being forfeited by reason of the contractor's failure to perform his commitment. The letter invoking the guarantee stated that purchase orders had not been complied with despite extension of time. Another letter alleged breach. The court said that all this showed that the circumstances for invoking the guarantee were made out. The court further said that even

claiming under the guarantee must establish that conditions for invoking the guarantee do exist. In this case the Government made a counter-offer to the highest bidder and entered into negotiations which did not materialise into a contract. Hence, the guarantee could not be invoked.<sup>124</sup> A contract was held to have been formed where the parties, though not accepting all the printed terms, agreed to some of them. A contract thus came into existence outside the form. Stay of encashment of bank guarantee could not be ordered on the ground that no contract was formed.<sup>125</sup> Where the bank guarantee is conditional, the beneficiary cannot have unfettered right to invoke the guarantee and the court can issue an injunction against invocation on the facts of the case.<sup>126</sup> Where there was no reference in the invocation letter to any breach of contract having been committed nor to any loss or damage though the terms of the guarantee required such conditions to be fulfilled the plaintiff was allowed the relief of injunction.<sup>127</sup>

The Supreme Court again emphasised in *U.P. Coop Federation Ltd v Singh Consultants and Engineers (P) Ltd*,<sup>128</sup> that the operation of a bank



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if the beneficiary was made the sole judge of the circumstances, the bank was obliged to pay because the bank could not sit in judgment.

124. *Basic Tele Services Ltd v Union of India*, AIR 2000 Del 1.
125. *International (India) v Indian Sugar & General Industries Export Import Corp*n, AIR 2001 Guj 227.
126. *Hindustan Construction Co Ltd v State of Bihar*, (1999) 8 SCC 436: AIR 1999 SC 3710. But here there was a concluded contract and the guarantee was also absolute. Since a bank guarantee represents an independent contract between the bank and beneficiary, both of them are bound by its terms and they are extremely material. *Crest Communications Ltd v SBI*, (2000) 3 Mah LJ 163, the contract was performed and accepted to the extent of 100 per cent satisfaction and full payment made, an attempt to encash the bank guarantee was stayed.
127. *V.V. Gupta v MCD*, AIR 2006 NOC 1035 (Del).
128. (1988) 1 SCC 174. Refusal to take the material because of allegations as to quality is not a fraud in itself so as to prevent invocation of bank guarantee, *EMCO Pressmaster (P) Ltd v Union of India*, AIR 2000 Del 37. Conditions stated in the contract but not in the bank guarantee could not be used for staying encashment. *Assn of Corpn and Apex Societies of Handlooms v State of Bihar*, AIR 2000 Del 106. Breach of contract is not by itself enough to bring about stay of encashment, the bank cannot sit in judgment for deciding the question of breach, *Federal Bank Ltd v V.M. Jog Engg Ltd*, (2001) 1 SCC 663: AIR 2000 SC 3166; *Larsen & Tubro Ltd v Maharashtra SEB*, (1995) 6 SCC 68: AIR 1996 SC 334, where fraud or irretrievable injustice was not pleaded and the only plea was that there was no concluded contract. *G. Dayanand v Chief Conservator of Forests State Trading Circle*, (1997) 2 BC 195 (AP), contract cancelled, forfeitures carried out, if encashment of bank guarantee was not stayed and cancellation was afterwards found to be wrongful, there would be irreparable loss. *Man Industries India Ltd v NV Kharote Engineers & Contractors*, AIR 2005 Bom 311, absolute guarantee in favour of supplier, no link with actual supplies, encashment not restrained, supplier could not have run away with the money, hence no chance of irreparable loss. *Adani Exports Ltd v Mktg Service Incorporated*, AIR 2005 Guj 257, non-supply of goods of approved quality within specified time, also short supply, purchaser's letters of credit, encashment restrained. *Jindal Stainless Ltd v ICICI Banking Corp Ltd*, AIR 2005 Del 53, fraud was discovered only after the negotiating bank had already released payment. *Bhumiputra Commerce Bank v PVP Products Ltd*, (2006) 4 Bom CR 431, bank guarantee in the winding up of the company under orders of the Rajasthan High Court and confirmed by the Supreme Court up to a certain amount plus interest as accepted by the bank. The bank was not allowed to say at the time of renewal that the guarantee was to be confined only to the principal amount originally ordered. *BSES Ltd v Fenner India Ltd*, (2006) 2 SCC

guarantee should be stayed only in cases of serious dispute, fraud or special equities.

Two bank guarantees were furnished by a contractor for the proper construction and successful commissioning of a vanaspati plant. The bank was not to revoke the guarantees up to a fixed date and was to make unconditional payment on demand. The Board was to be the sole judge of the fact whether the contractor had fulfilled the terms of the contract. Disputes arose between the contractor and the Board as to the erection and performance of the plant.

The contractor sought an injunction to restrain the Board from enforcing the guarantee. The court found no serious ground for doing so. The court felt that respectability and reliability of the assured mode of payment through confirmed letters of credit in international trade and bank guarantees in national trade is necessary for the growth and promotion of trade. SHETTY J<sup>129</sup> cited Lord DIPLOCK:<sup>130</sup> “The whole commercial purpose for which the system of confirmed irrevocable documentary credits has been developed in international trade is to give to the seller an assured right to be paid before he parts with control of the goods and that does not permit of any dispute with the buyer as to the performance of the contract of sale being used as a ground for non-payment or reduction or deferment of payment.”

His Lordship cited American authorities<sup>131</sup> to the effect that the fraudulent use of guarantee papers by the seller is the only case in which court should stay misuse of a credit system. “The exception for fraud on the part of the beneficiary seeking to avail himself of the credit is a clear application of the maxim *ex turpi causa non oritur actio*, or, if plain English is to be preferred, ‘fraud unravels all’.”<sup>132</sup>

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728, guarantees given for advance payments, whole amount of advances was recovered from running bills, even so guarantees were invoked. The court did not stay invocation. There was pending arbitration in which also the stay was sought. There was no danger of money being lost forever. Even otherwise the other party had the right of encashment for all kinds of breach. *A.P. Electronics Development Corp v M.K. Mohan*, (2010) 1 LW 518 (Mad), a bank guarantee was not allowed to be invoked for non-performance of a contract which was found to be illegal. *Petroleum India International v Bank of Baroda*, (2008) 6 Mah LJ 487, no fraud or special equity proved.

129. *U.P. Coop Federation Ltd v Singh Consultants and Engineers (P) Ltd*, (1988) 1 SCC 174.
130. *United City Merchants (Investments) Ltd v Royal Bank of Canada*, (1983) 1 AC 168: (1982) 2 WLR 1039 (HL).
131. *Sztein v J. Henry Schorder Bkg Corp*, (1941) 3 HYS 2d 631, referred to with approval by the English Court of Appeal in *Edward Owen Engg Ltd v Barclays Bank International Ltd*, 1978 QB 159 (CA); *Bolivinter Oil S.A. v Chase Manhattan Bank N.A.*, (1984) 1 WLR 392 (CA).
132. The Supreme Court surveyed the whole range of authorities: *Hamzeh Malas & Sons v British Imex Industries Ltd*, (1958) 2 QB 127: (1958) 2 WLR 100 (CA), payment under letters of credit not stayed on the allegation that the first instalment contained defective goods; *Elian and Rabbath v Matsas and Matsas*, (1966) 2 Ll LR 495, where payment was stayed because the shipowners resorted to a new lien without any justification.

The court noted that in India also trend of law is on the same lines: *Tarapore & Co v V.O. Tractors Export*, (1969) 1 SCC 233: AIR 1970 SC 891, irrevocable letter of credit had

Fraud must be of egregious nature so as to vitiate the entire underlying transaction. The allegation of fraud must be specifically and explicitly pleaded. In this case there was no explanation as to how and in what manner the alleged fraud was committed. Encashment of bank guarantee was not stayed.<sup>133</sup>

The court alleviated the feelings of contractors and buyers who provide guarantees which go beyond their reach by saying that no irretrievable injustice is likely to be done because the party withdrawing the amount would remain accountable and, if he cannot justify himself, he would have to offer restitution or compensation.<sup>134</sup>

"The wholly exceptional case where an injunction may be granted is where it is proved that the bank knows that any demand for payment already made or which may hereafter be made will clearly be fraudulent. But the evidence must be clear both as to the fact of fraud and as to the bank's knowledge. It would certainly not normally be sufficient that this rests on the uncorroborated statement of the customer. A bank acting on such a statement may cause irreparable damage to its credit."<sup>135</sup>

In reference to the meaning of irretrievable injury, the Supreme Court said that it must be of the kind which was the subject-matter of the decision in *Itek Corp v First National Bank of Boston*:<sup>136</sup> "To avail of the exception, therefore, exceptional circumstances which make it impossible for the guarantor to reimburse himself if he ultimately succeeds will have to be decisively established. Clearly, a mere apprehension that the other party will not be able to pay is not enough."<sup>137</sup>

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a definite implication; *Centax (India) Ltd v Vinmar Impex Inc*, (1986) 4 SCC 136: AIR 1986 SC 1924. The court overruled the decision of the Allahabad High Court in *Union of India v Meena Steels Ltd*, AIR 1985 All 282.

133. *H.P. SEB Ltd v Ahluwalia Contracts (India) Ltd*, AIR 2015 HP 108.

134. A bank cannot justifiably pay under a guarantee, where it has expired or the business in respect of which it was given has been suspended, and, therefore, payment can be stayed. See *J.R. Enterprises v S.T.C.*, AIR 1987 Del 188. Similarly, the payment under a bank guarantee submitted along with a bid can be stayed if the bid is withdrawn before acceptance. *Kirloskar Pneumatic Co Ltd v NTPC Ltd*, AIR 1987 Bom 308.

135. SIR JOHN DONALDSON MR in *Bolivinter Oil S.A. v Chase Manhattan Bank N.A.*, (1984) 1 WLR 392 (CA) cited by the Supreme Court in *U.P. Coop Federation Ltd v Singh Consultants and Engineers (P) Ltd*, (1988) 1 SCC 174.

136. 566 Federal Supp 1210.

137. Observations to the same effect are to be seen, among others, in *Hindustan Steel Workers Construction Ltd v G.S. Atwal & Co (Engineers) (P) Ltd*, (1995) 6 SCC 76: AIR 1996 SC 131; *Larsen & Toubro Ltd v Maharashtra SEB*, (1995) 6 SCC 68: AIR 1996 SC 334. Observations of this kind are also to be seen in *TTI Team Telecom Ltd v Hutchinson 3G UK Ltd*, 2003 EWHC 762 (TCC) cited by the Supreme Court in *BSES Ltd v Fenner India Ltd*, (2006) 2 SCC 728: AIR 2006 SC 1148 "a failure by the beneficiary to provide an essential element of the underlying contract on which the bond depends: a misuse by the beneficiary of the guarantee by failing to act in accordance with the purpose for which it was given: a total failure of consideration in the underlying contract: a threatened call by the beneficiary for an unconscionable ulterior motive or a lack of an honest or *bona fide* belief by the beneficiary that circumstances, such as poor performance against which a performance bond had been provided actually exist." *Veer Probhu Mktg Ltd v National Supply Corp*, AIR 2006 Cal

In *General Electric Technical Services Co Inc v Punj Sons (P) Ltd*,<sup>138</sup> while dealing with a case of bank guarantee given for securing mobilisation advance, it was held that the right of a contractor to recover certain amounts under running bills would have no relevance to the liability of the bank under the guarantee given by it.<sup>139</sup>

A bank guarantee was unequivocal and unconditional. The bank agreed to pay without any demur and on demand the court did not accept the agreement that the beneficiary must show that he had suffered loss by reason of non-fulfilment of the contract. If such contentions were to be accepted the very purpose of such guarantees would be defeated. The court would have to record a finding and give a verdict in each case.<sup>140</sup>

The High Court of Delhi followed this decision so as to hold that the enforcement of the bank guarantee would not be stayed but that the authority would be told that they should enforce the guarantee only for the balance amount minus the amount already recovered from the contractor's running account payments.<sup>141</sup>

In *Escorts Ltd v Modern Insulators Ltd*<sup>142</sup> the High Court of Delhi refused to stay the payment because the alleged ground only showed an inconsistency in the two letters about the installation and working of machines and not a fraud or the possibility of an irretrievable injustice. The Supreme Court dealt with this matter at great length in *U.P. Coop Federation Ltd v Singh*

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301, supply of goods for which guarantee was given was completed, the plaintiffs as suppliers discharged their obligations. There was no complaint also. Requests were made for cancellation of guarantees but instead invocation was made. This was stayed *ad interim*, attempt to get it vacated failed.

138. (1991) 4 SCC 230.
139. Another ruling to the same effect is *Coronation Construction (P) Ltd v Indian Oil Corp Ltd*, AIR 1999 Del 268, no pleading that there was fraud in the main contract, the only allegation was that the other party was trying to encash the guarantee for an amount which it had already recovered; that was sufficient for establishing the exception of fraud or irretrievable injustice. *J.T. Mobiles Ltd v Deutsche Bank Ltd*, AIR 1999 Del 358, an injunction was vacated on the Attorney General giving undertaking that in the event of the party's suit being decreed, the Union of India will pay the amount. *A.L.N. Narayanan Chettiar v Official Assignee*, (1941) 54 LW 606: AIR 1941 PC 93, observations to the effect that "fraud like any other charge of criminal proceedings must be established beyond reasonable doubt". A finding as to fraud cannot be based on suspicion and conjecture. Cited in *DLF Cement Ltd v Inspector of Police*, AIR 1999 AP 359: (1999) 2 An LD 45, stay of encashment was held to be not proper where neither of the grounds was made out. The court, on directing the parties for reference to arbitration in terms of their agreement, stayed the encashment of the guarantee, this was held to be illegal. It is not the function of the courts to examine the merits of the dispute at that stage.
140. *Amrok Logistics Trading (P) Ltd v Digvijay Cement Co Ltd*, AIR 2001 Guj 299, there was no proof of fraud or irretrievable injustice.
141. *Madan Gopal Jajoo v Union of India*, AIR 1992 Del 253. *State Bank of Mysore v Pukhrajmal Sugarmal Lunkad*, AIR 2007 NOC 589 (Mad) (DB), bank guarantee issued without there being any applicant by the officer and also without any authority, decree passed against the bank on the basis of such guarantee was set aside. *Harcharan Das Gupta v DDA*, AIR 2007 Del 75 (DB), encashment of bank guarantee not stayed. There was no fraud on the tenderer because he was aware of the existence of nullah on the project site.
142. AIR 1988 Del 345.

*Consultants and Engineers (P) Ltd.*<sup>143</sup> The court reiterated that the bank must pay except in case of fraud or irretrievable injustice. There should be minimum interference in trade. Commitments of banks must be honoured free from interference by the courts. Otherwise, trust in commerce, internal and international, would be irreparably damaged.

The Supreme Court approved the observations of Lord DIPLOCK in *United City Merchants (Investments) Ltd v Royal Bank of Canada*,<sup>144</sup> where it was observed that “to this general statement of principle as to the commercial obligation of the confirming bank to the seller, there is one established exception, that is, where the seller, for the purpose of drawing on the credit, fraudulently presents to the confirming bank documents that contain, expressly or by implication, material representation of facts that to his knowledge are untrue.... The courts will not allow their process to be used by a dishonest person to carry out a fraud”. An example of a fraud of this kind was before the Bombay High Court in *Dai-Ichi Karkaria (P) Ltd v Oil and Natural Gas Commission*.<sup>145</sup> The court emphatically asserted that the law cannot allow the benefit of a bank guarantee to be claimed by unscrupulous methods. Here the party in question was compelled at the pain of stopping business with him to drop from his bank guarantee the original requirement that it would be encashable only when the parallel amount of import duty paid by him was refunded to him. As soon as ONGC

143. (1988) 1 SCC 174. See also *Fenner (India) Ltd v Punjab and Sind Bank*, (1997) 7 SCC 89: AIR 1997 SC 3450, encashment of bank guarantee on failure of payment up to a certain limit, not stayed. *Kamal Virdichandji Garg v Fiat India (P) Ltd*, AIR 2004 Bom 462, the contention for getting encashment stayed was that the matter had been settled by issuing cheques, but the cheques being post-dated and could not be encashed immediately, there was no fraud in invoking the bank guarantee. *Maharashtra State Handloom Corp. Ltd v Assn of Corpn & Apex Societies of Handlooms*, AIR 2006 NOC 1185 (Del), invocation stayed till the end of arbitration proceedings because the contract had been fully performed, attempted invocation was motivated by other reasons. *Hindustan Construction Co Ltd v Sathij Jal Vidyut Nigam Ltd*, AIR 2006 Del 169, bank guarantee furnished by the contractor for civil work. A dispute was referred to the Dispute Review Board. Bank guarantee was invoked at this stage without notice. It seemed to be an attempt to defeat the decision of DRB. The corporation was restrained from encasing guarantee. *Adani Agri Fresh Ltd v Mahaboob Sharif*, 2015 SCC OnLine SC 1302: (2016) 2 LW 56, a fruit supplier was given a guarantee by a fruit wholesaler to make supply to another wholesaler. Supply was accordingly made. The buyer wholesaler did not pay the bill and the bank guarantee was invoked. An injunction against invocation issued by the court below was held to be not proper. There was no allegation of any fraud or irretrievable loss.

144. (1983) 1 AC 168: (1982) 2 WLR 1039 (HL). *Rigoss Exports International (P) Ltd v Tartan Infomark Ltd*, AIR 2002 Del 285, bank guarantee obtained by an export agent fraudulently, encashment stayed. *Jagson International Ltd v Oil & Natural Gas Corp. Ltd*, (2003) 4 Mah LJ 733: (2004) 2 Bom CR 272, breach of rigging contract, failure to provide oil rigs in time, arbitrator's finding that the contractor committed breach, the court did not interfere with it, invocation of performance guarantee allowed. *National Highways Authority of India v Ganga Enterprises*, (2003) 7 SCC 410, invocation in accordance with the terms of the guarantee, encashment not stayed. The court further added that in matters of contract a petition under Article 226 is not the appropriate remedy.

145. AIR 1992 Bom 309. *Binfo Electronics (P) Ltd v BSNL*, AIR 2004 NOC 214 (Kant), where no purchase order was issued, the question of non-compliance did not arise and there being no failure on the part of the bidder, his bank guarantee was not allowed to be encashed.

attempted to enforce the altered guarantee, he applied for and was granted a stay against such encashment. He was the victim of undue influence bordering on fraud and the special equities thus generated created the necessity of rescuing the party from being victimised.

Where the terms of a bank guarantee required that the letter of invocation must mention the amount of loss caused, it was held that a letter of invocation which only stated that the contractor had failed to perform his contract was not a sufficient compliance with the requirements of invocation. Hence, encashment was stayed.<sup>146</sup> Where no purchase order was placed upon the bidder so that there was no concluded contract at all, invocation of bank guarantee was held to be not justified.<sup>147</sup>

In a case before the Calcutta High Court:<sup>148</sup>

The contract was for dredging and deepening a reservoir. Advance payment was made to the contractor for purchase of essential machinery on bank guarantee. SAIL sought encashment on account of the contractor's default. The contractor tried to prevent it on the ground that the work assigned to him was impossible and that important facts were suppressed from him. These grounds were held to be not sufficient to prevent encashment.

Where the provision in the contract was that the guarantee would be enforceable on the failure of the purchaser to take delivery and that the supplier's decision as to this would be final, the court did not interfere in the decision of the supplier to enforce the guarantee.<sup>149</sup> Even where the matter under dispute was referred to arbitration, the court did not stay the enforcement of the bank guarantee.<sup>150</sup> A bank guarantee was invoked where the contractor failed to make contribution towards certain welfare funds. The terms of the guarantee made the owner as the sole judge of the fact whether the contractor committed breach. The court did not oblige the contractor with an injunction restraining invocation of the guarantee.<sup>151</sup>

146. *Ansal Properties and Industries (P) Ltd v Engg Projects (India) Ltd*, AIR 1998 Del 176. A suit for invoking encashment was dismissed as withdrawn, a second suit for the same purpose was not allowed because there could not be fresh cause of action though the second suit was moulded into a different shape of seeking remittance of the amount mentioned in the guarantee, *Modi Korea Telecommunications Ltd v IndusInd Bank*, AIR 2001 Del 254: (2003) 1 Banker's Journal 383.

147. *Binfo Electronics (P) Ltd v BSNL*, AIR 2004 NOC 214 (Kant).

148. *D.T.H. Construction (P) Ltd v SAIL*, AIR 1986 Cal 31.

149. *Allied Resins of India Ltd v Minerals and Metals Trading Corp of India Ltd*, AIR 1986 Cal 346.

150. *Jute Corp of India Ltd v Konark Jute Ltd*, AIR 1986 Ori 238. The enforcement of bank guarantee cannot be stayed by means of a writ petition. *Modi Vanijya v Metal Scrap Trading Corp Ltd*, (1991) 1 Cal LT 156.

151. *Geo Tech Construction Co (P) Ltd v Hindustan Steel Works Construction Ltd*, AIR 1999 Ker 72. *Asif Enterprises v ONGC Ltd*, AIR 2002 Guj 264, fake bank guarantee, black listing of the contractor without hearing not wrong. His reply to the show cause notice was not tenable. Acceptance of fresh bank guarantee and resuming contracts with him before initiating action did not have the effect of condoning consequences of fake document.

Where a mobilisation advance was provided by the owner to the contractor against a bank guarantee and the contract having been terminated and the mobilisation advance thereby becoming recoverable, encashment of the bank guarantee was held to be justified. It could not be said that the encashment was not in accordance with the terms of the contract. Even if the first invocation was not in accordance with the terms of the contract, it could be followed by a second invocation. The court further said that reasons for requiring a bank guarantee may continue to persist even after termination of the contract to enable invocation up to the date of its expiry.<sup>152</sup>

Even the winding up of the company on whose behalf the guarantee was submitted would not enable the bank to refuse payment.<sup>153</sup> The fact that the company which was invoking bank guarantee was likely to be declared a sick industrial undertaking was held to be not a situation of a special equity or irretrievable injustice so as to justify an injunction against encashment.<sup>154</sup>

### Variation in terms of contract

The High Court of Delhi has expressed the view that a clause in a bank guarantee to the effect that the parties may vary the terms of the contract without affecting the liability of the bank would be valid. All that is necessary is that the guarantor's ultimate remedy against the principal debtor should remain unimpaired.<sup>155</sup>

### Bank guarantee separate transaction

The court cannot take recourse to surrounding circumstances unless an ambiguity exists in the terms and conditions of the contract. A bank guarantee is a separate transaction. It has to be construed on its own terms.<sup>156</sup> Where there were two separate contracts, the bank guarantee executed in respect of one of them was not allowed to be invoked in respect of the other.<sup>157</sup>

### Letters of credit and bank guarantees

SEN J of the Supreme Court observed in *Centax (India) Ltd v Vinmar Impex Inc*:<sup>158</sup> "Commitments of banks must be allowed to be honoured free from interference from the courts. Otherwise, trust in international commerce would be irreparably damaged."<sup>159</sup> The court did not grant an



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152. *Crown Maritime Co (India) Ltd v Econ Engg (P) Ltd*, AIR 2003 Bom 163.

153. *Gas Authority of India Ltd v Official Liquidator, Mumbai*, AIR 2004 Bom 220.

154. *Kamal Virdichandji Garg v Fiat India (P) Ltd*, AIR 2004 Bom 462.

155. *Lloyds Steel Industries Ltd v Indian Oil Corpn Ltd*, AIR 1999 Del 248.

156. *SBI v Mula Sahakari Sakkar Karkhana Ltd*, (2006) 6 SCC 293; AIR 2007 SC 2361.

157. *National Highways Authority of India v Jivanlal Joitram Patel*, AIR 2010 NOC 402 (Guj).

158. (1986) 4 SCC 136; AIR 1986 SC 1924.

159. At p. 1986 citing DENNING MR in *Elan v Matpas*, 1966 11 LR 595; *Akai Impex Ltd v General Steel Export*, (1998) 2 Bom CR 199, letters of credit are like bank guarantees. They are a dealing in documents. The banks are not concerned with the quality or quantities of the goods. Those things have to be sorted out between the parties. Their encashment can

injunction to stay the enforcement of letters of guarantee on the grounds that the goods were of inferior quality and the sellers had not sent the original shipping documents. The court cited the following statement of JENKINS LJ in *Hamzeh Malas & Sons v British Imex Industries Ltd*:<sup>160</sup>

“...the opening of a confirmed letter of credit constitutes a bargain between the banker and the vendor of the goods which imposes on the banker an absolute obligation to pay...and that this was not a case in which the court ought to exercise its discretion and grant the injunction.”

The court emphasised that a bank guarantee attracts the same consideration as a letter of credit and added: “A letter of credit sometimes resembles and is analogous to a contract of guarantee. A bank guarantee is very much like a letter of credit. The courts will do their utmost to enforce it according to its terms. They will not, in the ordinary course of things, interfere by way of injunction to prevent its implementation.” The court also cited an observation of KERR J in *Harbottle R.D. (Mercantile) Ltd v National Westminster Bank Ltd*:<sup>161</sup>

“It is only in exceptional cases that the court will interfere with the machinery of irrevocable obligations assumed by banks. They are the life-blood of international commerce.”

The type of rare case in which a court may intervene was before the Calcutta High Court in *Banerjee & Banerjee v Hindustan Steel Works Construction Ltd*.<sup>162</sup> Here the party claiming under the guarantee failed to point out the precise amount of his claim although he had the means to quantify it, his intention being to suppress vital information, the court held that his conduct being fraudulent, enforcement of the guarantee ought to be stayed.

Another example would be where the encashment of the guarantee would be contrary to law. For example, where a contractor gave a bank guarantee

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be stopped only in cases of fraud or irretrievable loss. *Rani Constructions (P) Ltd v Patibel JV*, (2006) 129 DLT 38, guaranteee revealed that bank was liable to pay on first demand with no right of objection. This also amounted to waiver of the right under S. 133. Mark Williams, *Documentary Credit & Fraud: English and Chinese Law Compared*, 2004 JBL 155; *Himadri Chemicals Industries Ltd v Coal Tar Refining Co*, (2007) 8 SCC 110: AIR 2007 SC 2798, no injunction against encashment of letter of credit, the buyer of goods was given the option to negotiate but instead he only agreed to amend the letter with the consent of the bank.

160. (1958) 2 QB 127, 129: (1958) 2 WLR 100 (CA). The House of Lords in *United City Merchants (Investments) Ltd v Royal Bank of Canada*, (1983) 1 AC 168: (1982) 2 WLR 1039 (HL) held that the principles enunciated in the cases dealing with confirmed irrevocable letters of credit were equally applicable to cases of bank guarantees in internal trade within country; *United Coconut Oil Mills v Indian Overseas Bank*, (1991) 3 Curr LJ 2345 (Singapore); *Swiss Bank Corp v Jai Hind Oil Mills Co*, (1994) 1 Bom CR 371, there is no privity of relationship between the vendor and the confirming bank. For further study see, *Agasha Mugasha, Enjoining the beneficiary's claim on a Letter of Credit or Bank Guarantee*, 2004 JBL 515.

161. 1978 QB 146: (1977) 3 WLR 752.

162. AIR 1986 Cal 374.

along with his bid as was required by the tender notice, the bidder, having the right to do so, withdrew his bid before its acceptance, the Department was restrained from encashing the guarantee. There was no contract yet about which it could be said that there was a breach.<sup>163</sup>

Where the sub-letting of a Government contract was allowed only in respect of three items and the principal contractor in fraud of his sub-lettee handed over the entire work to him and obtained from him a bank guarantee for due performance, the enforcement of the guarantee was stayed by reason of the fraud, for otherwise the sub-lettee would have suffered an irreparable loss.<sup>164</sup>

Where the bank which presented the letter of credit for encashment was a holder in due course, it was held that the bank which issued the letter would have to honour the same even if the document was tainted by fraud. The facts of the present case showed that a fraud was practised by the buyer and the supplier colluding with one and another to deprive the bank of repayment. An injunction order against the bank to restrain it from honouring the documentary credit was vacated so that the payment could follow.<sup>165</sup>

A conditional or contingent bank guarantee cannot be invoked by the creditor without the specified condition being fulfilled.<sup>166</sup>

#### *Bank guarantee and arbitration clause*

The enforcement of a bank guarantee cannot be made the subject-matter of arbitration proceeding.<sup>167</sup> But where a bank found that there was a pending arbitration under which the liability of all the parties had to be ascertained, the Karnataka High Court upheld the decision of the bank to withhold payment.<sup>168</sup> In another Karnataka case<sup>169</sup> it was held that the right of the beneficiary of the guarantee to recover the guaranteed amount could not be stayed pending arbitration and the bank could not be restrained from honouring its obligation. But the amount encashed is subject to adjustment under the final award to be passed by the arbitrator.

163. *Kirloskar Pneumatic Co Ltd v NTPC Ltd*, AIR 1987 Bom 308. Another case of stay because of special equities is *Arul Marugan Traders v Rashtriya Chemicals and Fertilisers Ltd*, AIR 1986 Mad 161. Still another is *Sztein v J. Henry Schorder Bkg Corp*, (1941) 3 HYS 2d 631 where the enforcement was stayed because the shipment was not that of real but of worthless waste material.

164. *Nagia Constructions (India) (P) Ltd v National Building Construction Corp* Ltd, AIR 1990 NOC 177 (Del). Writ jurisdiction is not a proper remedy for demanding stay, *Rayalaseema Paper Mills Ltd v A.P. State Trading Corp*, AIR 1990 NOC 124 (AP); *National Project Construction Corp Ltd v Sadhu & Co*, AIR 1990 P&H 300.

165. *State Bank of Mysore v Machado Computer Services*, (2009) 5 Mah LJ 349.

166. *Karnataka State Khadi and Village Industries Board v Punjab National Bank*, (2014) 1 SCC 625: (2013) 101 ALR 245.

167. *National Project Construction Corp Ltd v G. Ranjan*, AIR 1985 Cal 23. The court referred to *Union of India v Raman Iron Foundry*, (1974) 2 SCC 231: AIR 1974 SC 1265; *Centax (India) Ltd v Vinmar Impex Inc*, (1986) 4 SCC 136: AIR 1986 SC 1924.

168. *Kudremukh Iron Ore Co Ltd v Korula Rubber Co (P) Ltd*, AIR 1987 Kant 139.

169. *HVS Technologies Inc, USA v Aeronautical Development Agency*, (2001) 4 Kant LJ 211.

### Period of limitation (expiry of guarantee period)

The period of limitation for enforcing a guarantee is three years from the date on which the letter of guarantee was executed.<sup>170</sup> Where as against the advancement of a loan to a company, the guarantee deed was executed by its directors and subsequently a letter acknowledging the loan was issued by the same directors on behalf of the company, it was held that the letter did not have the effect of extending the period of limitation. Recovery proceedings instituted after three years from the date of the deed of guarantee were liable to be quashed.<sup>171</sup> Where an acknowledgement of liability by part payment or otherwise has the effect of extending the period of limitation, it was held that the debt remained the same as it was before. So long as the principal debtor remains liable, the surety also continues to be liable. There is no need for any separate acknowledgement from the surety.<sup>172</sup>

Where the terms of the deed of guarantee showed that the guarantee was of continuing nature, it was held that the suit would be governed by Article 55 of the Limitation Act, 1963. Hence, so long as the account was alive, i.e. neither settled nor there was refusal by guarantors to carry out the obligation, the period of limitation would not start running. On breach taking place, the bank gave notice invoking the guarantee. A suit filed within three years from that date was held to be within time.<sup>173</sup>

A guarantee has to be invoked within its validity period, i.e. before its expiry date. Once it is invoked within time actual proceedings can be commenced within the period of three years from that date. Any clause in the contract cutting short this period would be hit by Section 28.<sup>174</sup>

170. *New Bank of India v Sajitha Textiles*, AIR 1997 Ker 201, the guarantee deed was not allowed to be enforced against the guarantor under a suit filed after expiry of the period. Article 55 of the Limitation Act, 1963 is applicable.

171. *Annama Jose v Kerala Financial Corp*n, AIR 2002 Ker 396.

172. *Syndicate Bank v K. Prakash*, AIR 2007 Mad 307.

173. *Indian Bank v State of T.N.*, AIR 2002 Mad 423; *Ibrahim Abdul Latif Shaikh v Corpn Bank*, AIR 2003 Kant 98, revival letter and acknowledgement executed by the principal debtor on authorisation of guarantor. The guarantor's plea that this did not have the effect of creating a fresh period of limitation was held to be not tenable. *Punj Lioyd Ltd v India Cements Ltd*, AIR 2005 Del 389, courts cannot direct, a bank to extend a bank guarantee. *Punj Lloyd Insulations Ltd v SBI*, AIR 2006 Del 256, extended contract, bank guarantee encashed in accordance with terms and conditions. *Mula Sahakari Sakhar Karkhana Ltd v SBI*, (2005) 6 Bom CR 55, contract for erection of paper plant, clause for 10 per cent retention on the bills, replaced by bank guarantee, contract terminated invocation of bank guarantee not stayed, invocation was after breach and therefore not premature, the question whether the document was an indemnity or guarantee could be considered at the trial, the contractor was not likely to suffer any irretrievable injustice. *Syndicate Bank v Channaveerappa Beleri*, (2006) 11 SCC 506: AIR 2006 SC 1874, commencement of liability depends upon terms of the guarantee. In the case of demand guarantee, limitation begins when there is refusal to pay after due invocation. The case against the principal debtor should be a live claim.

174. *Explore Computers (P) Ltd v Cals Ltd*, (2006) 131 DLT 477; *Maharashtra State Financial Corpn v Magna Elastomeric Rollers (P) Ltd*, 2005 SCC OnLine Bom 227: (2005) 4 Bom CR 661, limitation as against the guarantor starts only from invocation of the guarantee. Followed in *SICOM Ltd v Padmashri Mahipatrali Shah*, (2005) 3 Mah LJ 125.

Where the guarantee was valid for 90 days, the court said that it could be invoked on the 91st day, if the 90th day happened to be a public holiday or sunday and the banks did not function that day.<sup>175</sup>

Where the contract between the parties had expired by efflux of time without invocation of bank guarantee, as such the defendants had no right under the contract to invoke the bank guarantee. They induced the plaintiff to renew the guarantee thus changing position to their detriment. Defendants invoked the guarantee immediately after renewal. The order of injunction passed restraining the defendants from invoking the guarantee was held to be proper.<sup>176</sup>

### Joint-debtors and suretyship [S. 132]

**S. 132. Liability of two persons, primarily liable, not affected by arrangement between them that one shall be surety in other's default.**—Where two persons contract with a third person to undertake a certain liability, and also contract with each other that one of them shall be liable only on the default of the other, the third person not being a party to such contract, the liability of each of such two persons to the third person under the first contract is not affected by the existence of the second contract, although such third person may have been aware of its existence.

#### *Illustration*

A and B make a joint and several promissory note to C. A makes it, in fact, as surety for B, and C, knows this at the time when the note is made. The fact that A, to the knowledge of C, made the note as surety for B, is no answer to a suit by C against A upon the note.

The section is based upon the principle that the liability of persons who are primarily liable as joint-debtors is not affected by any arrangement between them as to the order of their liability. A creditor is not affected by any private arrangement entered into as between his two debtors that one will be the surety of the other even if the creditor knows of this arrangement. The creditor may not be a consenting party to the arrangement.<sup>177</sup>

The principle of the section is that whatever be the arrangement between joint-debtors as to their liability to the creditor they remain joint debtors. The creditor is not concerned with their mutual agreement that one would be a principal and the other a surety. Where, however, the creditor knows of any such arrangement, he must refrain from doing anything which would have the effect of discharging the surety under Sections 133, 134 or 135.<sup>178</sup>

175. *ICICI Bank Ltd v Tata International Ltd*, (2008) 6 Mah LJ 446, S. 10 of the General Clauses Act, 1897.

176. *Videocon Industries Ltd v Coal India Ltd*, AIR 2014 Cal 113.

177. *Duncan Fox & Co v North & South Wales Bank*, (1880) LR 6 AC 1 (HL).

178. *Oakeley v Pasheller*, (1836) 4 Cl & Fin 207; 7 ER 80 and *Overend, Gurney & Co v Oriental Financial Corp*, (1874) LR 7 HL 348; *Rouse v Bradford Banking Co Ltd*, 1894 AC 586 (HL). In two Indian cases the same view has been taken. *Punchanun Ghose v Dally*, (1875) 15 BLR 331; *Harjiban Das v Bhagwan Das*, (1871) 7 BLR 535; followed in *Moolji Murarji Sunderji v M.C. Pinto*, AIR 1926 Sind 156; *Bihari Lal v Allahabad Bank Ltd*, AIR 1929 All 664 and *M. Pogose v Bank of Bengal*, ILR (1877) 3 Cal 174.

Unless there is a specific agreement between the surety and the creditor to the effect that the principal debtor alone would be liable in the first instance, the creditor can proceed against the surety to the same extent as if he were himself the principal debtor. It would not be necessary first to realise the amount from the principal debtor.<sup>179</sup>

A personal guarantee executed by the guarantor providing that the guaranteee was to remain in force till the borrower paid the full loan amount on demand was held to be a continuing guarantee. The period of limitation started running on refusal by the borrower to fulfil the demand.<sup>180</sup> After notice of revocation, any amount due from the surety in respect of pre-existing transactions, the payment for the same must be claimed within three years failing which it would become time-barred.<sup>181</sup>

### DISCHARGE OF SURETY FROM LIABILITY

A surety is said to be discharged from liability when his liability comes to an end. The Act recognises the following modes of discharge:

#### 1. By revocation [S. 130]

Ordinarily a guarantee is not revocable when once it is acted upon. But Section 130 provides for revocation of continuing guarantees.

**S. 130. Revocation of continuing guarantee.**—A continuing guarantee may at any time be revoked by the surety, as to future transactions, by notice to the creditor.

#### *Illustrations*

- (a) *A, in consideration of B's discounting, at A's request, bills of exchange for C, guarantee to B, for twelve months, the due payment of all such bills to the extent of 5000 rupees. B discounts bills for C to the extent of 2000 rupees. Afterwards, at the end of three months, A revokes the guarantee. This revocation discharges A from all liability to B for any subsequent discount. But A is liable to B for the 2000 rupees, on default of C.*
- (b) *A guarantees to B, to the extent of 10,000 rupees, that C shall pay all the bills that B shall draw upon him. B draws upon C. C accepts the bill. A gives notice of revocation. C dishonours the bill at maturity. A is liable upon his guarantee.*

Revocation becomes effective for the future transactions while the surety remains liable for transactions already entered into.<sup>182</sup> *Offord v Davies*<sup>183</sup> is a suitable illustration:

The defendants guaranteed the repayment of bills to be discounted by the plaintiffs for *Davies & Co* for twelve months not exceeding £600.

179. *Medisetti Ravi Babu v Pramida Chit Fund (P) Ltd*, (2003) 2 BC 527 (AP).

180. *C.P. Sreelal v District Collector, Thiruvananthapuram*, AIR 2007 Ker 131.

181. *Tamil Nadu Industrial Investment Corpn v Sudarsanam Industries*, AIR 2009 Mad 15 (DB).

182. *Indian Overseas Bank v Goh Teng Hoon*, (1989) 1 CLJ 554 (HC Singapore).

183. (1862) 6 LT 579: 142 ER 1336. A guarantee for money to be advanced from time to time is a continuing guarantee. *Laurie v Scholefield*, (1869) LR 4 CP 622.

The defendants revoked the guarantee before any bill was discounted. But the plaintiffs discounted the bills which remained unpaid.

The question was whether the surety had a right to revoke. The court said: "We are of opinion that they had and consequently they were not liable. In the case of a simple guarantee for a proposed loan, the right of revocation before the proposal has been acted on did not appear to be disputed." In the case of a continuing guarantee, every credit given is a separate transaction which makes the surety irrevocably liable, but he may free himself from further liability.<sup>184</sup>

The employment of a servant is one transaction. A guarantee for his good behaviour is not a continuing one and is not revocable as long as he continues in the job.<sup>185</sup> At any rate the employer is entitled to such notice as will enable him to determine the employment without liability. Nor is such a guarantee determined by the surety's death unless there is an agreement to the contrary.<sup>186</sup>

Whether a guarantee for the payment of rent can be revoked depends upon the facts of each case and the language employed by the parties to express their intention.<sup>187</sup> In a guarantee of this kind where the surety died, the court held that neither could he have revoked the guarantee during his lifetime nor was his estate released from liability.<sup>188</sup> JOYCE J said: "The right to determine or withdraw a guarantee by notice forthwith cannot possibly exist when the consideration for it is indivisible, so to speak, and moves from person to whom the guarantee is given once for all, as in the case of the consideration being the giving or conferring an office or employment upon any person whose integrity is guaranteed."

As against it when a person guaranteed the payment of rent by his servant and revoked the guarantee as soon as the servant left his employment, he was held not liable for rents which became due after the revocation.<sup>189</sup>

Where the directors of a company guaranteed the payment of the company's overdrafts and subsequently resigned their office and the bank was informed, it was held that the liability of the directors would be confined to the amount due up to the date of their resignation.<sup>190</sup> The guaranteeing directions of the company can be proceeded against even when the company has

184. *Anil Kumar v Central Bank of India*, AIR 1997 HP 5, a co-surety gave notice to the bank and cancelled his guarantee, held, no liability for anything after such notice; the liability of the other co-sureties not affected.

185. *Lloyds v Harper*, (1880) LR 16 Ch D 290.

186. *Balfour v Crace*, (1902) 1 Ch 733.

187. *Coles v Pack*, (1869) LR 5 CP 65, 70.

188. *Balfour v Crace*, (1902) 1 Ch 733.

189. *Windfield v De St Croin*, (1919) 35 TLR 432.

190. *Hargopal Agarwal v SBI*, AIR 1956 Mad 211. A yearly renewable guarantee for the conduct of a treasurer, held, continuing, *Lala Bansidhar v Govt of Bengal*, (1872) 9 Beng LR 364: 14 MIA 86.

entered into protection from liability under the Sick Industrial Companies (Special Provision) Act, 1985.<sup>191</sup>

“Notice to the creditor” means a clear and specific notice intended to terminate liability under the guarantee. A denial of liability in a previous suit was held to be not serving as a notice.<sup>192</sup>

## 2. By death of surety [S. 131]

A continuing guarantee is also determined by the death of the surety unless there is a contract to the contrary. Once again, the termination becomes effective only for the future transactions.<sup>193</sup> The surety's heirs can be sued for liability already incurred. The section clearly points this out.

**S. 131. Revocation of continuing guarantee by surety's death.**—The death of the surety operates, in the absence of any contract to the contrary, as a revocation of a continuing guarantee, so far as regards future transactions.

### *Liability of legal heirs*

The liability of the deceased surety can be imposed against his legal heirs but only to the extent of the property inherited by them.<sup>194</sup>

## 3. By variance [S. 133]

Courts of law and equity have always taken zealous care of a surety's interest. “A surety is considered a favoured debtor and his liability is in *strictissimi juris*.<sup>195</sup> Initially a contract of guarantee may not be one of utmost good faith, but once formed the duty of utmost good faith is imposed upon the creditor. The result of this concern of the courts for the surety's interest is that a surety is held discharged when, without his consent, the creditor makes any change in the nature or terms of his contract with the principal debtor.<sup>196</sup> “The surety is discharged as soon as the original contract is

191. *R.K. Dewan v State of U.P.*, 2005 All LJ 2067.

192. *Bhikabhai v Bai Bhuri*, ILR 27 Bom 418. A request for release also does not have the effect of a notice of revocation, *Perwatra Habib Bank v Sehatian Development*, (1994) 1 Curr LJ 394 (Malaysia).

193. Termination becomes effective on the creditor receiving the notice. *Coulthari v Clementson*, (1879) LR 5 QBD 42. But under the section there is automatic termination on death. A term of the guarantee that the legal heirs may terminate by notice after death would be a provision to the contrary. *Durga Priya Chowdhury v Durga Pada Roy*, AIR 1928 Cal 204: ILR (1928) 55 Cal 154.

194. *R.K. Dewan v State of U.P.*, (2005) All LJ 2067. *SBI v Jayanthi*, (2011) 2 CTC 465: AIR 2011 Mad 179 (DB), creditor can recover dues out of the estate of the deceased.

195. See judgment of KAY LJ in *Rouse v Bradford Banking Co Ltd*, 1894 AC 586 (HL), followed by the Supreme Court in *State of Maharashtra v M.N. Kaul*, AIR 1967 SC 1634, where a guarantee was not allowed to be enforced after the expiry of its term. The court cited passages from the speech of Lord WESTBURY LC in *Blest v Brown*, (1862) 4 De GF & J 367, 376: 45 ER 1225: “You bind him to the letter of his engagement. Beyond the proper interpretation of that engagement, you have no hold upon him.” *SBI v Jayanthi*, (2011) 2 CTC 465: AIR 2011 Mad 179 (DB), recovery from the estate of the deceased.

196. A variance with consent either given in advance or at the time of variance would maintain the liability of the surety intact. Thus he can agree that he would not claim the benefit of Ss. 133,

altered without his consent.”<sup>197</sup> A guarantee is not a contract in respect of a primary transaction. It is an independent transaction containing independent and reciprocal obligations. It is created on a principal to principal basis. Therefore, some relief is provided both to the creditor and the guarantor.<sup>198</sup> Section 133 of the Indian Contract Act incorporates this principle.

**S. 133. Discharge of surety by variance in terms of contract.**—Any variance, made without the surety's consent, in the terms of the contract between the principal<sup>199</sup> [debtor] and the creditor, discharges the surety as to transactions subsequent to the variance.

*Illustrations*

- (a) A becomes surety to C for B's conduct as a manager in C's bank. Afterwards, B and C contract, without A's consent, that B's salary shall be raised, and that he shall become liable for one-fourth of the losses on overdrafts. B allows a customer to overdraw, and the bank loses a sum of money. A is discharged from his suretyship by the variance made without his consent, and is not liable to make good this loss.
- (b) A guarantees C against the misconduct of B in an office to which B is appointed by C, and of which the duties are defined by an Act of the Legislature. By a subsequent Act, the nature of the office is materially altered. Afterwards, B misconducts himself. A is discharged by the change from future liability under his guarantee, though the misconduct of B is in respect of a duty not affected by the latter Act.
- (c) C agrees to appoint B as his clerk to sell goods at a yearly salary, upon A's becoming surety to C for B's duly accounting for moneys received by him as such clerk. Afterwards, without A's knowledge or consent, C and B agree that B should be paid by a commission on the goods sold by him and not by a fixed salary. A is not liable for subsequent misconduct of B.
- (d) A gives to C a continuing guarantee to the extent of 3000 rupees for any oil supplied by C to B on credit. Afterwards B becomes embarrassed, and, without the knowledge of A, B and C contract that C shall continue to supply B with oil for ready money, and that the payment shall be applied to the then existing debts between B and C. A is not liable on his guarantee for any goods supplied after this new arrangement.
- (e) C contracts to lend B 5000 rupees on the 1st March. A guarantees repayment, C pays the 5000 rupees to B on the 1st January. A is discharged from his liability, as the contract has been varied, inasmuch as C might sue B for the money before the first of March.

*Bonar v Macdonald*<sup>200</sup> is one of the early illustrations.

134, 135, 139 and 141 and such agreement would be valid. *T. Raju Setty v Bank of Baroda*, AIR 1992 Kant 108: (1991) 4 Kant LJ 475. The court did not agree with the contrary view as expressed in *Union of India v Pearl Hosiery Mills*, AIR 1961 Punj 281 to the effect that S. 133 cannot be excluded by an agreement to the contrary. The court agreed with the view expressed in *Citibank N.A. v J.K. Jute Mills Co Ltd*, AIR 1982 Del 487 and *R. Lilavati v Bank of Baroda*, AIR 1987 Kant 2: ILR 1987 Kant 964.

197. *Pratapsing Moholalbhai v Keshavlal Harilal Setalwad*, (1934–34) 62 IA 23: AIR 1935 PC 21.

198. *Industrial Finance Corp of India Ltd v Cannanore Spg & Wvg Mills Ltd*, (2002) 5 SCC 54: AIR 2002 SC 1841: (2002) 110 Comp Cas 685.

199. This word was inserted by S. 2 and Sch. 1 of the Repealing and Amending Act, 1917 (XXIV of 1917).

200. (1850) 3 HL Cas 226: 10 ER 87; *Brahmayya & Co v K. Srinivasan Thangirayar*, AIR 1959 Mad 122.

The defendant guaranteed the conduct of a manager of a bank. The bank afterwards raised his salary on the condition that he would be liable for one-fourth of the losses on discounts allowed by him. No communication of this new arrangement was made to the surety. The manager allowed a customer to overdraw his account and the bank lost a sum of money.

It was held that the surety could not be called on to make good the loss as the fresh agreement was a substitution of a new agreement for the former which discharged the surety.

Similarly, where the payment of rent was guaranteed, and the rent was increased without the consent of the surety;<sup>201</sup> where the creditor on default of payment took a promissory note from the principal debtor without reference to the surety;<sup>202</sup> where the position of a partner in a firm was guaranteed and the business of the firm was extended without knowledge of the surety, the sureties were held to be discharged.<sup>203</sup>

One of the questions that concerns the courts is that where a variation is not substantial or material, or is beneficial to the surety, will he be discharged? A problem of this kind was before the Supreme Court in *M.S. Anirudhan v Thomco's Bank Ltd.*<sup>204</sup>



The defendant guaranteed the repayment of a loan of Rs 20,000 given by the plaintiff bank to the principal debtor. The guarantee paper showed the loan to be Rs 25,000. The bank refused to accept. The principal then reduced the amount to Rs 20,000 and without intimation to the surety gave it to the bank which was then accepted. The principal debtor failed to pay and the bank sued the surety. The question was whether the alteration had discharged him.

It was held by a majority that the surety was not discharged. KAPUR J and HIDAYATULLAH J (afterwards CJ) were of this view, but SARKAR J dissented. HIDAYATULLAH J (afterwards CJ) considered the authorities.<sup>205</sup>

Lord WESTBURY LC in *Blest v Brown*<sup>206</sup> stated the liability in the following terms: "It must always be recollect in what manner the surety is bound. You bind him to the letter of his engagement. Beyond the proper interpretation of that engagement you have no hold upon him. He receives no benefit and no consideration. He is bound, therefore, merely according

201. *Khatun Bibi v Abdullah*, ILR (1880) 3 All 9.

202. *Creet v Seth & Seth*, 1887 All WN 136; *C.N. Sundaram v Chennai Finance Co Ltd*, (2005) 5 An LT 60: AIR 2006 NOC 505 (AP), loan for a period of five months. The creditor unilaterally extended time and also accepted new schedule for repayment. This was done on the asking of one of the guarantors without informing even the principal borrower. The other guarantors and the principal borrower became discharged.

203. *Jowand Singh v Tirath Ram*, AIR 1939 Lah 193.

204. AIR 1963 SC 746: (1963) 1 SCR 63: (1963) 33 Comp Cas 185.

205. *M.S. Anirudhan v Thomco's Bank Ltd*, AIR 1963 SC 746: (1963) 1 SCR 63: (1963) 33 Comp Cas 185.

206. (1862) 4 De GF & J 367: 45 ER 1225.

to the proper meanings and effect of the written engagement that he has entered into. If that written engagement is altered in a single line, no matter whether the alteration be innocently made, he has a right to say: 'The contract is no longer for that for which I engaged to be surety; you have put an end to the contract that I guaranteed, and my obligation, therefore, is at an end.'

The statement of the law in *Blest v Brown*<sup>207</sup> was considered by the Court of Appeal in *Holme v Brunskill*.<sup>208</sup> COTTON LJ stated the law in these words:

"The true rule in my opinion is that if there is any agreement between the principals with reference to the contract guaranteed, the surety ought to be consulted, and that if he has not consented to the alteration, although in cases where it is without inquiry evident that the alteration is unsubstantial, or that it cannot be otherwise than beneficial to the surety, the surety may not be discharged; yet that if it is not self-evident that the alteration is unsubstantial or one which cannot be prejudicial to the surety, the court will not in an action against the surety, go into inquiry as to the effect of the alteration."

"There is a noticeable difference between the strict rule stated by Lord WESTBURY and that stated by COTTON LJ and the law now accepts that unsubstantial alterations which are to the benefit of the surety do not discharge the surety from the liability. Of course, if the alteration is to the disadvantage of the surety, or its unsubstantial character is not self-evident the surety can claim to be discharged. The court will not then inquire whether it in fact harmed the surety. That dictum of COTTON LJ was quoted with approval by the Judicial Committee in *Ward v National Bank of New Zealand Ltd.*<sup>209</sup>"

An attempted variation which does not become effective leaves the surety bound by his guarantee.<sup>210</sup>

Another effect is that an alteration not only discharges the surety from his personal liability but also releases the property, if any, which the surety had included in the contract.<sup>211</sup> This was the situation in *Bolton v Salmon*.<sup>212</sup> The defendant was a surety for a loan and also brought in some of her own property as security. The principal debtor, without her knowledge, borrowed from the creditor further still and executed a new deed consolidating all the

207. *Ibid.*

208. (1877) LR 3 QBD 495 (CA).

209. (1883) LR 8 AC 755 (PC).

210. *Egbert v National Crown Bank*, 1918 AC 903 (PC). The acceptance of claims by a liquidator in the winding up of a company does not have the effect of discharging the surety. *Punjab National Bank v Mehra Bros (P) Ltd*, AIR 1983 Cal 335. The amount of arrears due was mentioned in a guarantee. Subsequently the amount was found to be less than that mentioned. Held, did not amount to variation. *N. Sulochana v State of A.P.*, AIR 1984 AP 173.

211. *Bolton v Salmon*, (1891) 2 Ch 48. *Kahn Singh v Tek Chand*, AIR 1968 J&K 93, compromise of decreed debt, surety discharged.

212. (1891) 2 Ch 48.

loans. The defendant was held to have been discharged and her property released from the bond.

Where a guarantee was given for the loan account of the principal debtor with a bank and the bank opened a second account in the name of the principal debtor into which considerable payments were received, the surety was held to have been discharged.<sup>213</sup> The terms of guarantee provided interest at 9 per cent and that the surety's consent would not be necessary for any grant by the creditor to the principal debtor "of time or any other indulgence or consideration". The creditor extended the time of payment by one year and increased the interest to 16 per cent. This discharged the surety. The court said that the substantial increase of interest could not be covered by the words "any indulgence or consideration".<sup>214</sup> The liability under a guarantee ceased to exist where the guarantee was substituted by another guarantee bond covering the whole amount and signed by other guarantors.<sup>215</sup>

Extension of cash-credit limit of the borrower beyond the amount which was guaranteed did not have the effect of discharging the surety because his limit of liability was to remain the same as under the guarantee.<sup>216</sup>

The liability of the guarantor would not automatically cease or come to an end merely because he had not signed revival letters. The fact that the guarantor was no longer willing to continue with the guarantee did not end the guarantee or his liability under it.<sup>217</sup>

#### *Advance authorisation of alteration*

The Madhya Pradesh High Court has been of the view that an authority given by the surety in advance enabling the creditor and the principal debtor to make any alteration in the terms and conditions of the transaction guaranteed would be contrary to the provision of Section 133 and, therefore, of no effect. The consent of the surety of which the section talks must be consent taken at the time of variance so as to be simultaneous with the proposed variance. The court also said that the provisions of Sections 134, 135, 139 and 141 cannot be nullified in advance.<sup>218</sup>

213. *National Bank of Nigeria Ltd v M. S. Awolesi*, (1964) 1 WLR 1311; *Satish Chandra Jain v National Small Industries Corpn Ltd*, AIR 2003 SC 623: (2003) 1 ICC 788, guarantee for son's proprietary business debts, business converted into company with the son and another becoming guarantors. The original guarantor was not allowed to be proceeded against.

214. *Burnes v Trade Credits Ltd*, (1981) 1 WLR 805 (PC), on appeal from Wales.

215. *Punjab National Bank v Yarlapadda Venkata Krishnaiyah*, 1998 AIHC 3052 (AP); *Industrial Finance Corpn of India Ltd v Cannanore Spg & Wvg Mills Ltd*, (2002) 5 SCC 54; AIR 2002 SC 1841: (2002) 110 Comp Cas 685, nationalisation of the borrower mill (textile) did not result in discharge of contract of guarantee on account of frustration. The guarantee had no co-relationship with the Nationalisation Act, 1974. It was an independent contract and had to be honoured to fulfil the contractual obligation between the surety and creditor.

216. *M.V. Shantanarasimhaiah v Dena Bank*, (2002) 2 Kant LJ 255: (2002) 2 ICC 260 (Kant).

217. *Male Venkateswarlu v State Bank of India*, AIR 2006 NOC 508 (AP): (2005) 5 Andh LD 62. 218. *Central Bank of India v Ali Mohd*, (1993) 2 Mah LJ 1092.

Consent may be either prior or subsequent to the alteration.<sup>219</sup> All that the above decision means to say is that there should be either a proposed alteration for prior consent or an alteration already effected for subsequent consent. There should not be consent to variation in vacuum. The High Court of Delhi has expressed the view that a term in a bank guarantee providing that variations in the underlying contract may be made without affecting the liability of the bank would be valid.<sup>220</sup>

#### *Effect of decree against surety*

In a case before the High Court of Delhi,<sup>221</sup> the creditor obtained a decree both against the principal debtor and the surety making them collectively and severally liable to pay the amount to the decree-holder. He then entered into a settlement with the principal debtor agreeing to accept from him a less amount and not to enforce the decree against him for the balance. The surety claimed a discharge on this basis. The court did not agree with him. Once the liability is converted into a decreed-debt, the earlier constraints of the underlying contract cease to be applicable. The subsequent dealing with the principal debtor does not operate to discharge the surety from a liability under which he is no longer liable as a surety, but under the decree.<sup>222</sup>

Earlier the Madras High Court<sup>223</sup> had observed in a case of this kind:

“We are not, after a joint decree has been passed against principal and surety, any longer dealing with a principal and surety but with a joint debtor.”

219. *Lloyds Steel Industries Ltd v Indian Oil Corpn Ltd*, AIR 1999 Del 248.

220. Ibid; *Indian Bank v S. Krishnaswamy*, AIR 1990 Mad 115, comparing the effect of variation under S. 62 with that under S. 133 the court cited *British Motor Trust Co Ltd v Hyams*, (1934) 50 TLR 230, normally speaking any alteration in the contract between the creditor and the debtor is sufficient to release the surety but that effect can be excluded. *SBI v Vivek Garg*, AIR 2011 Sikk 7, the guarantee stipulated that notwithstanding any variation made in the terms of the arrangement or any composition between the bank and borrower, the guarantor would not be relieved and he shall be deemed to have consented to the same. Hence, he could not plead discharge. *Kunbi Sahakari Bank Ltd v Shakti Paper Co*, (2009) 1 Mah LJ 696, guarantors who waived their rights under Ss. 133, 134, 139 and 141, could not claim discharge from liability under these sections.

221. *Charan Singh v Security Finance (P) Ltd*, AIR 1988 Del 130.

222. *Jenkins v Roberton*, (1854) 2 Drewry 351: 61 ER 755; *Union Bank of India v Manku Narayana*, (1987) 2 SCC 335. The decision in this case was overruled by the Supreme Court in *SBI v Indexport Registered*, (1992) 3 SCC 159: AIR 1992 SC 1740 by holding that the decree-holder obtaining a composite decree can proceed at his choice to execute the decree either against security or person. This was followed in *Sharad R. Khanna v Industrial Credit and Investment Corpn of India*, (1993) 1 Bom CR 546, decree against mortgage property and against surety. Enforcement of decree against surety personally not to be prevented. The decree-holder not compellable to proceed against mortgage property first, *SBI v Balak Raj Abrol*, AIR 1989 HP 41.

223. *Meenakshisundaram Chettiar v Velambal Ammal*, AIR 1944 Mad 423. Compare with *Kahn Singh v Tek Chand*, AIR 1968 J&K 93, compromise of a decreed debt operated as a discharge of the surety.

In still another Madras case,<sup>224</sup> a loan due to a co-operative society was guaranteed by a surety and an award was obtained by the society against the principal debtor as well as the surety. The principal debtor obtained a discharge from the debt. The decree-holder sought to enforce the decree against the surety, who contended that he was no more liable under the award as the liability of the principal debtor stood extinguished. But the court found no merit in this contention and said: "After a decree has been passed the characters of the principal debtor and that of the surety change into those of co-judgment-debtors. The provisions of Sections 133–139 of the Contract Act apply only where no decree has been passed. These provisions which govern the rights and liabilities of the creditor, the principal debtor and surety, cease to operate after the rights and liabilities are determined and declared by a decree. The liability as determined by the decree cannot thereafter be modified by anything which the decree-holder may do or omit to do."<sup>225</sup>

An alteration which does not disturb the basic structure of liability created by a guarantee would not render the guarantee unenforceable. Two directors of a company guaranteed the company's obligation under a leasing transaction for photocopying equipment. Later someone dropped the word "company" from the borrowing company's name and initialled the alteration in the names of the directors. It was held that though the alteration was a forgery, the guarantee remained enforceable.<sup>226</sup>

#### 4. Release or discharge of principal debtor [S. 134]

**S. 134. Discharge of surety by release or discharge of principal debtor.**—The surety is discharged by any contract between the creditor and the principal debtor, by which the principal debtor is released, or by any act or omission of the creditor, the legal consequence of which is the discharge of the principal debtor.

##### *Illustrations*

- (a) *A gives a guarantee to C for goods to be supplied by C to B. C supplies goods to B, and afterwards B becomes embarrassed and contracts with his creditors (including C's) to assign to them his property in consideration of their releasing him from their demands). Here B is released from his debt by the contract with C, and A is discharged from his suretyship.*

224. *Nellore Coop Urban Bank Ltd v Akili Mallikarjmayya*, AIR 1948 Mad 252.

225. *Debtor A (No 14 of 1913), re*, (1913) 3 KB 11. Followed by Kerala High Court in *Velappa Kumar v Kosamattom Chit Fund*, 1978 KLT 10 and dissenting from *Sardar Kahn Singh v Tek Chand Nanda*, AIR 1968 J&K 93. Enforcement against the surety of the composite decree does not have the effect of discharging the surety. The decree can be executed against him for the amount, if any, remaining unpaid. *Chittur Service Coop Bank Ltd v Pankunny*, (1988) 1 KLT 358.

226. *Lombard Finance Ltd v Brookplain Trading Ltd*, (1991) 1 WLR 271 (CA); *Mohan Jatia v Indian Bank*, AIR 2004 Cal 326, receiver appointed by bank, took over securities, the surety could not claim discharge, securities have to be valued and realised and only then consequences could be worked out.

- (b) A contracts with B to grow a crop of indigo on A's land and to deliver it to B at a fixed rate, and C guarantees A's performance of this contract. B diverts a stream of water which is necessary for irrigation of A's land and thereby prevents him from raising the indigo. C is no longer liable on his guarantee.
- (c) A contracts with B for a fixed price to build a house for B within a stipulated time, B supplying the necessary timber. C guarantees A's performance of the contract. B omits to supply the timber. C is discharged from his suretyship.

*(i) Release of principal debtor*

The section provides for two kinds of discharge from liability. In the first place, if the creditor makes any contract with the principal debtor by which the latter is released, the surety is discharged. Where, for example, the creditor accepts a compromise and releases the principal debtor, the surety is likewise released. Any release of the principal debtor is a release of the surety also.<sup>227</sup>

*Effect of Debt Relief Acts.*—Where the liability of the principal debtor is reduced under the provisions of a statute, an important question arises whether the liability of the surety is also diminished thereby. Facing this problem probably for the first time in 1938 and again in 1944 the Nagpur High Court held that the intention of the statute is to relieve the principal debtor and not the surety.<sup>228</sup> But a Full Bench of the Madras High Court, applying the provisions of the Madras Agriculturists' Debt Relief Act, 1938 held that "the surety is liable only for the reduced amount".<sup>229</sup> This view of the Madras High Court has now been supported by the Kerala High Court in *Aypunni Mani v Devassy Kochouseph*.<sup>230</sup> Explaining the purpose of the debt-relieving statutes, GOPALAN NAMBIYARE J observed as follows: "It appears to us, that to hold otherwise, would be to altogether deny the benefit of the ameliorative provisions of the Act to the agriculturist debtor. On any other view it would be open to the creditor to recover the debt as scaled down from the agriculturist debtor, and the balance from the surety, and the

227. *Kahn Singh v Tek Chand*, AIR 1968 J&K 93; and see Illustration (a) to S. 134; *Manohar Lal Beli Ram v Har Kishan Lal*, AIR 1968 Del 108; Also see *Radha Thiagarajan v South Indian Bank Ltd*, 1985 KLT 29 (SN) where it is pointed out that the discharge of the principal debtor is not discharge of the surety where it is not brought about by the voluntary act of the creditor, but by operation of law; *Bank of India Ltd v Rustom Fakirji Cowasjee*, AIR 1955 Bom 419. Similarly, the creditor, while discharging the principal debtor, may reserve his rights against the surety and in that event the surety would not be discharged. *Cutler v McPhail*, (1962) 2 QB 292: (1962) 2 WLR 1135. Accepting new promissory note in place of the old loan system which was guaranteed discharged the old loan and with that also the surety, *P.C. Ravi v Union Bank of India*, 1995 AIHC 2168 (Ker); *Balbir Sound v Indian Bank*, 1996 MPLJ 853.

228. *Balkrishna v Atmaram*, AIR 1944 Nag 277.

229. *Subramania Chettiar v M.P. Narayanaswami Gounder*, AIR 1951 Mad 48, overruling *Subramania v Batcha Rowther*, AIR 1942 Mad 145; *Narayan Singh v Chhatarsingh*, AIR 1973 Raj 347; *Aypunni Mani v Devassy Kochouseph*, AIR 1966 Ker 203; *Babu Rao Ramchandra Rao v Babu Manaklal Nehmal*, AIR 1938 Nag 413; *Gopilal J. Nachani v Trac Industries and Components Ltd*, AIR 1978 Mad 134.

230. AIR 1966 Ker 203.

latter in his turn could seek reimbursement from the principal debtor (*vide* S. 144 of the Contract Act).<sup>231</sup> Such a construction would completely nullify the benefits of the ameliorative legislation to indebted agriculturists."

This is indeed the most desirable interpretation of Section 128 which makes the liability of the surety coextensive with that of the principal debtor. In view of this decision the effect of the section is "that a statutory reduction or extinguishment of the principal debtor's liability will operate as a *pro tanto* reduction or extinguishment of surety's debt". The mere suspension of a debt for a short period and that too with a clause that the period of limitation will not run during the period of suspension, will not affect the liability of the guarantor.<sup>232</sup>

### *Application of insolvency laws*

The Supreme Court has laid down that though under Section 134 the surety is discharged by release or discharge of the principal debtor, a discharge which the principal debtor may secure by reason of winding up or insolvency does not absolve the surety of his liability. A bank guarantee for a sum of Rs 50,000 was submitted by a supplier of the Electricity Board. The bank was liable under the guarantee to pay the amount within 48 hours of demand by the Board. The Board demanded payment. The bank made it. The bank was now trying to realise the amount out of the securities deposited by the supplier for securing the guarantee. The supplier company went into liquidation. The liquidator sought to restrain the bank from realising the securities. But the court allowed the bank to go ahead. The bank was a secured creditor and was entitled to the benefit of securities. The bank had nothing to do with the state of the relations between the company and the Electricity Board.<sup>233</sup>

### *(ii) Act or omission*

The second ground of discharge provided in Section 134 is that when the creditor does "any act or omission the legal consequence of which is the discharge of the principal debtor", the surety would also be discharged from his liability. Where, for example, there is a contract for the construction of a building the performance of which is guaranteed by a surety. Under the contract, the creditor has to supply the building material. An omission on

231. This section enables the surety to recover from principal debtor the amount which he has lawfully paid to the creditor under the contract of guarantee.

232. *Gopilal J. Nachani v Trac Industries and Components Ltd*, AIR 1978 Mad 134.

233. *Maharashtra SEB v Official Liquidator*, (1982) 3 SCC 358: AIR 1982 SC 1497. Similarly, the takeover of undertakings under statutory power, such as Sick Textiles Undertakings Notification Act, 1974, does not discharge the sureties of the borrowings from such undertakings. *Bank of Madura Ltd v Bank of Baroda*, 1986 SCC OnLine Mad 95: (1986) 99 LW 721; *State of A.P. v Central Bank of India*, (1982) 1 An WR (SN) 10. Suspension of the contract between the creditor and principal on account of the latter's defaults does not have the effect of absolving the surety from his liability. *SCIL (India) Ltd v Indian Bank*, AIR 1992 Bom 131.

his part to do so would discharge the contractor and so would the surety be discharged. Similarly, where the payment of rent due under a lease is guaranteed and the creditor terminates the lease, or where the payment of instalments due under a hire-purchase is guaranteed and the creditor prematurely determines the agreement, the effect would be the release of the surety also.<sup>234</sup> The act of the creditor in terminating the agreement, e.g., in determining the agreement of hire-purchase by taking possession of the goods, discharged the surety.<sup>235</sup>

The effect of omission to sue is considered later.<sup>236</sup>

## 5. Composition, extension of time and promise not to sue [S. 135]

**S. 135. Discharge of surety when creditor compounds with, gives time to, or agrees not to sue principal debtor.**—A contract between the creditor and the principal debtor, by which the creditor makes a composition with, or promises to give time to, or not to sue the principal debtor, discharges the surety, unless the surety assents to such contract.

The section provides for three modes of discharge from liability:

- (1) Composition;
- (2) Promise to give time, and
- (3) Promise not to sue the principal debtor.

### *Composition*

If the creditor makes a composition with the principal debtor, without consulting the surety, the latter is discharged. Composition inevitably involves variation of the original contract, and, therefore, the surety is discharged.<sup>237</sup> A settlement was entered into between the principal borrower and bank for one-time settlement without reference to the guarantor. The court said that this amounted to novation of the contract between the creditor and principal debtor to the exclusion of guarantor. The liability of guarantor ceased to exist. No proceedings could be initiated against the guarantor under Section 13 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002. The guarantor was allowed to

234. See *Unity Finance Ltd v Woodcock*, (1963) 1 WLR 455 (CA).

235. *Hewison v Ricketts*, (1894) 63 LJQB 711. See also *Hastings Corp v Letton*, (1908) 1 KB 378, a lease under which payment of rent was guaranteed the lessor terminated the lease, the surety was held discharged.

236. See under S. 137. The Supreme Court laid down that a creditor is entitled to recover the debt from the surety, even though a suit on the guarantee against the principal debtor is time barred. *Bombay Dyeing & Mfg Co Ltd v State of Bombay*, AIR 1958 SC 328: 1958 SCR 1122.

237. See *Bolton v Salmon*, (1891) 2 Ch 48; *Kahn Singh v Tek Chand*, AIR 1968 J&K 93, where after decrees had been passed against the principal debtor and sureties, the principal debtor compromised without consulting the sureties. This discharged them. *Mahomedalli Ibrahimji v Lakshmibai Anant Palande*, AIR 1930 Bom 122, compromise of the suit by the principal debtor undertaking to pay the dues by instalments, discharge of surety.



challenge the action initiated against him by invoking writ jurisdiction.<sup>238</sup> A compromise in terms of a court decree is different from private composition. That does not discharge the surety,<sup>239</sup> unless the decree is collusive.

#### *Promise to give time*

When the time for the payment of the guaranteed debt comes, the surety has the right to require the principal debtor to pay off the debt. Accordingly, it is one of the duties of the creditor towards the surety not to allow the principal debtor more time for payment. "The creditor has no right, it is against the faith of his contract, to give time to the principal, even though manifestly for the benefit of the surety, without the consent of the surety."<sup>240</sup> "It is very undesirable that there should be any dispute or controversy about whether it is for his benefit or not; there shall be the broad principle that if the creditor does intentionally violate any rights the surety had when he entered into the suretyship, even though the damage be nominal only, he shall forfeit the whole remedy."<sup>241</sup>

Thus, where the principal debtor was to make payment for gas supplied within fourteen days and on one occasion he having failed to pay, the supplier took a promissory note from him, this amounted to extension of time and thereupon the surety was discharged.<sup>242</sup> Similarly, where the price of a motor car was to be paid in instalments and payment of which was guaranteed, the buyer fell into arrears and the dealer settled with the buyer that he should pay a certain sum immediately and the balance by the end of the month. This discharged the surety.<sup>243</sup> The Supreme Court of India has held that where a bank gave time to the principal debtor to make up the quantity of the goods pledged, it did not have the effect of giving time for payment within the meaning of Section 135.<sup>244</sup>

238. *N. B. Gurudeva v State Bank of Mysore*, AIR 2011 Kant 188.

239. *City Bank N.A. v Juggilal Kamlapat Jute Mills Co Ltd*, AIR 1982 Del 487.

240. See Lord ELDON in *Samuel v Howarth*, 3 Mer 272, 279.

241. BLACKBURN J in *Polak v Everett*, (1876) LR 1 QBD 669. See also *Rouse v Bradford Banking Co Ltd*, 1894 AC 586 (HL). A unilateral extension of time without any contract with the principal debtor does not discharge the surety. At best it is a forbearance to sue. *Ushadevi Malhotra v Bhagwandas Tiwari*, AIR 1967 MP 250.

242. *Croydon Commercial Gas Co v Dickinson*, (1876) 2 CPD 46 (CA). *M. Venkataramanaiyah v Margadarsi Chit Funds*, AIR 2009 NOC 940 (AP), creditor made arrangement with debtor in form of promise to give time or agreed not to sue him, this is a situation comparable to novation of contract or composition. Surety discharged.

243. *Midland Motor Showrooms Ltd v Newman*, (1929) 2 KB 256; *Permata Merchant Bank v Glove Seal*, (1994) 1 Curr LJ 389 (Malaysia), here the original guarantee executed by the parties clearly showed that the sureties were not to be discharged or released by the restructuring of the mode of repayment of the loan by instalments.

244. *Amritlal Goverdhan Lalan v State Bank of Travancore*, AIR 1968 SC 1432: (1968) 3 SCR 724. Where the principal debtor acknowledged the debt which had the effect of extending the period of limitation, it was held that the surety would continue to be liable for the extended period. *Wandoor Jupiter Chits (P) Ltd v K.P. Mathew*, AIR 1980 Ker 190. Where by an arrangement between the principal judgment-debtor and the decree-holder, the time for discharge of the debt was extended by the former, it was held that its effect upon discharge of surety depended upon the discretion of the court. *Ram Chand Diwan Chand v Sant Singh*,

**S. 136. Surety not discharged when agreement made with third person to give time to principal debtor.**—Where a contract to give time to the principal debtor is made by the creditor with a third person, and not with the principal debtor, the surety is not discharged.

*Illustration*

C, the holder of an overdue bill of exchange drawn by A as surety for B, and accepted by B, contracts with M to give time to B. A is not discharged.

*Promise not to sue*

If the creditor under an agreement with the principal debtor promises not to sue him, the surety is discharged. “The main reason is that a surety is entitled at any time to require the creditor to call upon the principal debtor to pay off the debt” when it is due and this right is positively violated when the creditor promises not to sue the principal debtor.

*Forbearance to sue*

This is, however, subject to two important qualifications. In the first place, a promise not to sue should be distinguished from a mere “forbearance to sue”. “A promise not to sue is an engagement which ties the hands of the creditor. It is not negatively refraining; not exacting the money at the time, but it is the act of the creditor depriving himself of the power of suing....”<sup>245</sup> Section 137 incorporates this principle.

**S. 137. Creditor's forbearance to sue does not discharge surety.**—Mere forbearance on the part of the creditor to sue the principal debtor or to enforce any other remedy against him does not, in the absence of any provision in the guarantee to the contrary, discharge the surety.

*Illustration*

B owes to C a debt guaranteed by A. The debt becomes payable. C does not sue B for a year after the debt has become payable. A is not discharged from his suretyship.

Thus “mere forbearance to sue” does not discharge the surety.<sup>246</sup> But suppose that the forbearance continues up to the expiry of the period of limitation and consequently the action against the principal debtor becomes time barred, will the surety be discharged? According to Section 134 if the creditor is guilty of any act or omission the legal consequence of which is the discharge of the principal debtor, the surety is also discharged. The

AIR 1930 Lah 896; *Bank of Baroda v Avdoot Bhagwant Naik*, AIR 2005 Bom 224, delay in asking for payment and in filing suit, did not mean promise to extend time, the trawler purchased was disposed of but the loan amount not paid. The principal debtor and guarantor became jointly and severally liable.

245. See Lord HANWORTH MR in *Midland Motor Showrooms Ltd v Newman*, (1929) 2 KB 256 (CA).

246. Dissolution of a company which was the principal debtor, death of one of the sureties and the creditor not proceeding against the company did not discharge the remaining sureties. *Union of India v Modern Stores India Ltd*, AIR 1988 Cal 18.

omission to sue the principal debtor within the period of limitation definitely discharges him. Thus if Section 134 stood alone the surety would be discharged. But Section 137 declares that “mere forbearance to sue” does not discharge the surety. These two provisions naturally created a conflict of decisions which was ultimately resolved by the decision of the Privy Council in *Mahanth Singh v U Ba Yi*.<sup>247</sup> Lord PORTER observed as follows: “...a failure to sue the principal debtor until recovery is barred by the statutes of limitation does not operate as a discharge of the surety in England.”<sup>248</sup> The same view prevails in most of the High Courts in India....<sup>249</sup> With these decisions of the other High Courts in India may be contrasted the case of *Ranjit Singh v Naubat*,<sup>250</sup> which decides that in spite of the provisions of Section 137, the creditor’s right against the surety is not preserved unless he sues the principal debtor within the period of limitation. Such a decision is inconsistent with the views held by the courts in England and majority of the courts in India. In this conflict, their Lordships prefer the reasoning of the majority.”<sup>251</sup>

#### *Reserving rights against surety*

The decision further points out that an agreement not to sue the principal debtor or to give time with a reservation of the right against the surety, would not discharge the surety. The *Mahanth Singh* case<sup>252</sup> was decided on this principle.

The plaintiff was engaged as a contractor by certain trustees of a pagoda for construction work. The payment by the trustees was guaranteed by the defendants. The trustees defaulted and, therefore, the plaintiff sued the trustees and the surety. The beneficiaries of the trust replaced their trustees and the plaintiff dropped his case against them and was not allowed subsequently to sue them in their personal capacity. But the suit against the surety was maintained.

It was held that the surety was not discharged. “The appellant’s act in continuing to sue the surety though he withdrew his action against the

247. (1938–39) 66 IA 198: AIR 1939 PC 410: (1939) 181 IC 1; affirmed by the Supreme Court in *Bombay Dyeing & Mfg Co Ltd v State of Bombay*, AIR 1958 SC 328: 1958 SCR 1122.

248. See *Carter v White*, (1883) LR 25 Ch D 666 (CA).

249. See *Sankara Kalana v Virupakshapa Ganesha*, ILR (1883) 7 Bom 146; *Nur Din v Allah Ditta*, AIR 1932 Lah 419; *Aziz Ahmed v Sher Ali*, AIR 1956 All 8 (FB); *Dass Bank Ltd v Kali Kumari Devi*, AIR 1958 Cal 530 DB; *Bombay Dyeing & Mfg Co Ltd v State of Bombay*, AIR 1958 SC 328: 1958 SCR 1122.

250. ILR (1901–03) 24 All 504.

251. 66 IA at pp. 206–07. See further *Ushadevi Malhotra v Bhagwandas Tiwari*, AIR 1967 MP 250; *Punjab National Bank v Surendra Prasad Sinha*, 1993 Supp (1) SCC 499: AIR 1992 SC 1815 to the effect that where the debt becomes time barred, the securities deposited by the guarantor can be used towards realisation. *Makhan Lal Harnarain v Karamchand Thaper & Bros (P) Ltd*, AIR 2004 Jhar 143, takeover of coal mine by Government, former owner’s liabilities to be paid by Government, paid less to a claimant, balance allowed to be recovered by the guarantor.

252. *Mahanth Singh v U Ba Yi*, (1938–39) 66 IA 198: AIR 1939 PC 410: (1939) 181 IC 1.

principal debtors was a clear reservation of his rights. The remedy of the surety against the principal debtor is not impaired and his liability is, therefore, not discharged.”<sup>253</sup>

*Promise to give time to debtor made with third person*

Secondly, Section 136 provides that “where a contract to give time to the principal debtor is made by the creditor with a third person, and not with the principal debtor, the surety is not discharged”.

**6. By impairing surety's remedy [S. 139]**

**S. 139. Discharge of surety by creditor's act or omission impairing surety's eventual remedy.**—If the creditor does any act which is inconsistent with the right of the surety, or omits to do any act which his duty to the surety requires him to do, and the eventual remedy of the surety himself against the principal debtor is thereby impaired, the surety is discharged.

*Illustrations*

- (a) *B contracts to build a ship for C for a given sum, to be paid by instalments as the work reaches certain stages. A becomes surety to C for B's due performance of the contract. C, without the knowledge of A, prepays to B the last two instalments. A is discharged by this prepayment.*
- (b) *C lends money to B on the security of a joint and several promissory note, made in C's favour by B, and A as surety for B, together with a bill of sale of B's furniture, which gives power to C to sell the furniture, and apply to proceeds in discharge of the note. Subsequently, C sells the furniture, but, owing to his misconduct and wilful negligence, only a small price is realized. A is discharged from liability on the note.*
- (c) *A puts M as apprentice to B, and gives a guarantee to B for M's fidelity. B promises on his part that he will, at least once a month, see M make up the cash. B omits to see this done as promised, and M embezzles. A is not liable to B on his guarantee.*

If the creditor does any act which is inconsistent with the rights of the surety, or omits to do any act which his duty to the surety requires him to do, and the eventual remedy of the surety himself against the principal debtor is impaired, the surety is discharged. It is the plain duty of the creditor not to do anything inconsistent with the rights of the surety. A surety is entitled, after paying off the creditor, to his indemnity from the principal debtor. If the creditor's act or omission deprives the surety of the benefit of this remedy, the surety is discharged.<sup>254</sup> Thus, where the integrity of a cashier is guaranteed and the employer undertakes to check his work once in a month but neglects to do so, the cashier embezzles, the surety is not liable. The same duty requires the creditor to preserve the securities, if any, which he has against the principal debtor. If he loses or parts with the securities, the surety is discharged to that extent.<sup>255</sup> Similarly, where against the

253. See further, *Orissa Agro Industries Corp Ltd v Sarbeswar Guru*, AIR 1985 Ori 270, where the suit against the principal debtor was dismissed, but it was allowed against the surety.

254. See, for example, *Unity Finance Ltd v Woodcock*, (1963) 1 WLR 455 (CA).

255. *SBI v Praveen Tanneries*, (1992) 2 An LT 5 (notes on recent cases) where the surety was

terms of the guarantee the Government allowed the contractor to remove felled trees from a forest without payment of price, the surety was held to be discharged.<sup>256</sup>

Another suitable illustration is *Darwen & Pearce, re*:<sup>257</sup>

The principal debtor was a shareholder in a company. His shares were partly paid and the payment of the unpaid balance was guaranteed by the surety. The shareholder defaulted in the payment of calls and the company forfeited his shares.

By reason of the forfeiture the shares became the property of the company. If they had not been forfeited they would have belonged to the surety on payment of the outstanding calls. Thus, the forfeiture deprived the surety of his right to the shares and he was accordingly discharged.

Failure on the part of the supplier of a lorry to seize it after an accident, particularly when it was under repairs and under lien for repair charges, is not the same thing as impairing the surety's remedy who had guaranteed payment of the remaining instalments of the price.<sup>258</sup> To the same effect is a decision of the Rajasthan High Court.<sup>259</sup> The payment of the price of a liquor shop was spread into ten instalments and these payments were guaranteed by the defendant. The principal debtor defaulted with the instalments. The State could have cancelled the licence and re-auctioned the shop, but did not do so. The guarantor contended that this inaction should put an end to his liability. But he was held liable. The State inaction had in no way impaired his ultimate remedy against the principal debtor. Similarly, where the surety repeatedly asked the bank to do something against the principal debtor who was rapidly disposing of his assets and even so the bank did nothing, the surety was not allowed to claim any discharge.<sup>260</sup>

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discharged because the bank was not able to give to the surety the securities in the same condition as they formerly stood in his hands; *State Bank of Saurashtra v Chitrangan Rangnath Raja*, (1980) 4 SCC 516: AIR 1980 SC 1528 where the security of the pledged goods was lost because the bank was found to be highly negligent in the keeping and handling of those goods.

256. *State of M.P. v Kaluram*, AIR 967 SC 1105. See also *Amritlal Goverdhan Lalan v State Bank of Travancore*, AIR 1968 SC 1432, where the creditor's negligence in allowing the goods (securities) to fall short was held sufficient to discharge the surety. *M.R. Chakrapani Iyengar v Canara Bank*, AIR 1997 Kant 216, the principal debtor disposed of the hypothesized property, the surety submitted all the particulars to the creditor but the latter took no steps to seize the property or to issue criminal process against the debtor, the surety became discharged. *Union Bank of India v Suresh Bhailal Mehta*, AIR 1997 Guj 48, security in the form of hypothecated goods, lost on account of bank's negligence and not in existence at the time of the suit against the surety, the suit liable to be dismissed.

257. (1927) 1 Ch 176.

258. *Vasireddi Seetharamaiah v Srirama Motor Finance Corp*n, AIR 1977 AP 164.

259. *Dalichand v State of Rajasthan*, AIR 1976 Raj 112. Where the creditor gets the security sold in execution of a court decree, it does not amount to parting with security so as to discharge the surety. *City Bank N.A. v Juggilal Kamlapat Jute Mills Co Ltd*, AIR 1982 Del 487.

260. *Bhabani Shankar Patra v S.B.I.*, AIR 1986 Ori 247.

The creditor also owes to the surety the duty of realising the proper value of the securities in case he exercises his power of sale.<sup>261</sup> "Any improper dealing with the collateral deposited to secure an indebtedness guaranteed by another is available to the guarantor as a defence."<sup>262</sup> In a New York case<sup>263</sup> the guarantor pleaded in defence that the collateral security (skins in this case) was sold before maturity of the debt without notice for 200 dollars although worth 12,500 dollars at the time of sale. The guarantor was allowed corresponding reduction in his liability. Where, on the other hand, the assets of a company, whose debt was secured by mortgaging the assets and also guaranteed by a director, were taken over by the receiver appointed by the mortgagee, the receiver was held to be under no duty towards the surety to realise proper value of the assets. The guarantor sued the receiver for the loss caused to him by not obtaining proper value of the assets. But the action was not allowed.<sup>264</sup> The decision proceeded on the ground that the receiver is an agent of the creditor or, at the most, of the company, but not that of the surety. But the decision has been criticised.<sup>265</sup>

In a case before the Supreme Court:

A bank granted a loan on the security of the stock in godown. The loan was also guaranteed by a surety. The goods were lost from the godown on account of the negligence of bank officials. The surety was discharged to the extent of the value of the stock so lost.<sup>266</sup>

261. *Bhumiputra Merchant Banker Berhad v Melewar Corpns*, (1990) 2 Current LJ 30 (HC Kuala Lumpur), a mortgagee has the right to choose the time to sell and when he has decided to sell, he owes a common law duty to the mortgagor to realise the true value of the property sold. The court cited *Standard Chartered Bank Ltd v Walker*, (1982) 1 WLR 1410 (CA), where Lord DENNING described this duty as only a particular application of the general duty of care to your neighbour which was stated by Lord ATKIN in *Donoghue v Stevenson*, 1932 AC 562 (HL). The mortgagor and guarantor are clearly in very close "proximity" to those who conduct sale. *Shri Mahadev Rama Bhonsle v Central Bank of India*, (1998) 2 Bom CR 244, the bank realising the value of hypothecated vehicles after a lapse of five years, the bank was liable to reduce the recovery from the surety to the extent of recoverable loss. *Chistovan Vaz v Indian Overseas Bank*, (1998) 2 Bom CR 522, sale of vehicles after four years' exposure to sun and rains, considerable diminution in value, liability of surety to be reduced to that extent.

262. *Vose v Florida Railroad Co*, 50 NY 369, (1872).

263. *New Netherlands Bank of N.Y. v Dernburg*, 200 NYS (2d) 577 (1967).

264. *Latchford v Beirne*, (1981) 3 All ER 705.

265. See P.J. Davies, *No Duty of care to a Company Guarantor*, (1982) 98 LQR 351, where it has been maintained that the decision is contrary to the present trend of expanding the professional men's, duty of care towards those who have inevitably to rely on them. See *Yianni v Edwin Evans & Co*, 1982 QB 438; (1981) 3 WLR 843. See also *Barclays Bank Ltd v Thienel & Thienel*, (1978) 122 Sol Jo 472, where also it was held that no duty was owed to a mortgagee guarantor when the mortgagee exercised the power of sale.

266. *State Bank of Saurashtra v Chitrangan Rangnath Raja*, (1980) 4 SCC 516: AIR 1980 SC 1528, following *State of M.P. v Kaluram*, AIR 1967 SC 1105 and *Amritlal Goverdhan Lalan v State Bank of Travancore*, AIR 1968 SC 1432, where the creditor's negligence in allowing the goods (securities) to fall short was held sufficient to discharge the surety. As against this where the hypothecated goods were in the possession of the borrower himself and the bank was neither exercising control over the goods nor the borrower was under a duty to give a periodic account and the bank was also not aware of any disposal of the goods otherwise

This has been further supplemented by the Supreme Court by the declaration in a subsequent case that the creditor must proceed in the first place against the security and then only against the surety for the balance.<sup>267</sup>

Where the salary of both the principal debtor and the surety was got attached, it was held that nothing could be recovered from the surety as long as the principal debtor was paying his instalments. Only an instalment in default could be recovered. The creditor caused delay of some years in executing the decree. The court said that the interest for the period of delay could not be recovered from the surety. His liability was to be confined to the original decretal amount.<sup>268</sup>

In a case before the Privy Council,<sup>269</sup> their Lordships observed that the creditor owed no duty to the surety to exercise his power of sale of the mortgaged securities and could decide in its own interest whether to sell and when to do so. The security was neither surrendered, nor lost, nor imperfect, nor altered in condition by reason of what was done by the creditor. The creditor bank had three sources of repayment. The creditor could sue the debtor, sell the mortgaged securities or sue the surety. All those remedies could be exercised at any time or times simultaneously or contemporaneously or successively or not at all. If the creditor chose to sue the surety and not pursue any other remedy, the creditor on being paid in full was bound to assign the mortgaged securities to the surety. If the creditor chose to exercise his power of sale over the mortgaged security, he must sell for the correct market value, but the creditor must decide in his own interest if and when he should sell. The creditor does not become a trustee of the mortgaged

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than in the course of business, the surety was held to be not discharged because there was no connection between the bank's negligence and the loss of security. *Union Bank of India v M.P. Sreedharan Kartha*, AIR 1993 Ker 285, distinguishing *SBI v Quality Bread Factory*, AIR 1983 P&H 244. *Indian Bank v M. Aribika*, (2001) 1 Kant LJ 478, following *State of M.P. v. Kaluram*, AIR 1967 SC 1105. H.N. TILHARI J emphasised the duty of the bank in this connection. The bank failed to prevent transfer of the hypothecated stock by the principal to a third party despite having the power under the terms of the loan to do so. The bank was under duty to inspect periodically, take account, evaluate and give directions regarding disposal of the hypothecated stock. Failure of the bank in this respect facilitated illegal alienation. The surety was discharged to the extent of such loss of the stock. *Punjab National Bank v Lakshmi Industrial & Trading Co (P) Ltd*, AIR 2001 All 28, a receiver was appointed on the application of the bank for pledged goods. The bank claimed that the goods were damaged or destroyed due to natural decay while in the custody of the bank. No evidence was offered to show the quantity or quality of the goods at the initial stage. The bank's suit against the sureties was decreed after adjusting the value of the goods lost.

267. *Union Bank of India v Manku Narayana*, (1987) 2 SCC 335: AIR 1987 SC 1078.

268. *H.P. Jalajakshi v Karnataka Bank*, AIR 2003 Kant 280.

269. *China and South Sea Bank Ltd v Tan Soon Gin*, (1990) 1 AC 536: (1990) 2 WLR 56 (PC) on appeal from the Court of Appeal of Hong Kong. *J&K Bank Ltd v Choudhary Prakash Chand*, AIR 2006 J&K 11, vehicle loan guaranteed by a surety. Default by borrow, bank did nothing to cause sale of the hypothecated vehicle, surety not discharged. *Appanna Pullam Raju v Central Bank of India*, AIR 2006 NOC 1413 (AP): (2006) 1 CCC 262, allegation by the bank that the debtor tampered with the goods lying in the godowns which was mortgaged with the bank, Guarantor pleaded that the loss was caused by the conduct of the bank officials. Guarantor's liability not affected because of such negligence.

securities and the power of sale for the surety unless and until the creditor is paid in full and the surety, having paid the whole of the debt, is entitled to a transfer of the mortgaged securities to procure recovery of the whole or part of the sums he has paid to the creditor.

### *Waiver of rights*

There are contradictory rulings on the point whether a surety can give up the benefit of provisions designed to relieve him from liability. The Karnataka High Court<sup>270</sup> has been of the view that the rights under Sections 133, 134, 135, 139 and 141 are of variable nature and, therefore, a surety can waive the benefit of these provisions by a clause in the guarantee. There is, however, a ruling to the effect that the operation of Section 133 relating to discharge by variance cannot be ousted.<sup>271</sup>

## RIGHTS OF SURETY

A surety has certain rights against the debtor, creditor and co-sureties.

### **Rights against principal debtor**

Following are the rights of the surety against the principal debtor:

1. Right of Subrogation [S. 140]
2. Right to Indemnity [S. 145]

#### *1. Right of subrogation [S. 140]*

Section 140 provides for the right of subrogation:

**S. 140. Rights of surety on payment or performance.**—Where a guaranteed debt has become due, or default of the principal debtor to perform a guaranteed duty has taken place, the surety, upon payment or performance of all that he is liable for, is invested with all the rights which the creditor had against the principal debtor.

When the surety has paid all that he is liable for he is invested with all the rights which the creditor had against the principal debtor. The surety steps into the shoes of the creditor. The creditor had the right to sue the principal debtor. "If the liability of the surety is coextensive with that of the principal debtor, his right is not less coextensive with that of the creditor after he satisfies the creditor's debt."<sup>272</sup> The surety may, therefore, sue the principal debtor in the rights of the creditor. For example in *Lamplugh Iron Ore Co, re*:<sup>273</sup>

270. *T. Raju Setty v Bank of Baroda*, AIR 1992 Kant 108. This ruling was followed in *Central Bank of India v Multi Block (P) Ltd*, AIR 1997 Bom 109 and *Corporation Bank v B. Mohandas Baliga*, (1993) 1 Kant LJ 308 (DB).

271. *Union of India v Pearl Hosiery Mills*, AIR 1961 Punj 281.

272. *Babu Rao Ramchandra Rao v Babu Manaklal Nehmal*, AIR 1938 Nag 413.

273. (1927) 1 Ch 308.

A director of a company in liquidation guaranteed and paid the rents due from the company before the date of the liquidation. It was held that he was entitled to stand in the place of the creditor, and to use all remedies; if need be, in the name of the creditor in any action to obtain indemnification from the principal debtor for the loss sustained.

The Supreme Court has laid down that “the surety will be entitled to every remedy which the creditor had against the principal debtor; to enforce every security and all means of payment; to stand in the place of the creditor; to have the securities transferred to him, though there was no stipulation for that; and to avail himself of all those securities against the debtor. This right of a surety stands not merely upon contract, but also upon natural justice. The language of Section 140 which employs the words “is invested with all the rights which the creditor had against the principal debtor” makes it plain that even “without the necessity of a transfer, the law vests those rights in the surety”.<sup>274</sup>

This may not always be to the advantage of the surety. Where the principal debtor becomes insolvent, the surety cannot ask the creditor first to pursue his remedy against the principal debtor. The Supreme Court has pointed out that even then the surety should pay. He will be subrogated to the rights of the creditor against the principal debtor, though such rights against an insolvent debtor may not be of much use. “The very object of guarantee is defeated if the creditor is asked to postpone his remedies against the surety.”<sup>275</sup>

#### *Rights before payment*

Under the right of subrogation the surety may get certain rights even before payment. The Calcutta High Court examined this possibility in a case where the surety found, that the amount having become due, the principal debtor was disposing of his personal properties one after the other lest the surety, after paying, may seize them and sought a temporary injunction to prevent the principal debtor from doing so. The court granted the injunction. Relying upon an authoritative work, SUKUMAR CHAKRAVARTY J said<sup>276</sup> that if in any suit it is proved by affidavit or otherwise that the defendant threatens, or is about to remove or dispose of his property with intent to defraud his creditors, the court may grant a temporary injunction to restrain such act or to give such other order for the purpose of staying or preventing the removal or disposition of the property.

274. *Amritlal Goverdhan Lalan v State Bank of Travancore*, AIR 1968 SC 1432.

275. *Bank of Bihar Ltd v Damodar Prasad*, AIR 1969 SC 297: (1969) 1 SCR 620, 623; *Jugalkishore Rampratapji Rathi v Brijmohan*, (1994) 2 Bom CR 537, the surety's application is maintainable, the court must consider it on merits, it should not be rejected mechanically. See also *Aboobacker v Ayishu*, (1999) 3 KLT 530: AIR 2000 NOC 29 (Ker), the principal had paid to a very large extent, only the balance allowed to be recovered from the surety, for which he was entitled to indemnity from the principal debtor.

276. *Mamata Ghose v United Industrial Bank Ltd*, AIR 1987 Cal 280, 283.

Listing the other rights of the surety which arise in his favour before payment, the court cited the following passage from **STORY ON EQUITY**:<sup>277</sup> "Sureties, also, are entitled to come into a court of equity, after a debt has become due, to compel the debtor to exonerate them from their liability by paying the debt; or sue in the creditor's name, and collect the debt from the principal, if he will indemnify the creditor against the risk, delay and expense of the suit."

The court brought out from **SNELL'S PRINCIPLES OF EQUITY**<sup>278</sup> a passage which discusses the remedies of the surety under two heads, viz., before payment and after payment: "It has been stated there that the surety has an equitable right to compel the principal debtor to pay the debt and so relieve the surety from the necessity of paying it out of his pocket. It is in the nature of *quia timet*, and is based on the principle that it is unreasonable that a man should always have a cloud hang over him, so that he ought to be entitled to remove it. It is, therefore, immaterial that the creditor has refused to sue or that he has made no demand. A *fortiori*, the action lies where the principal debtor threatens to commit a breach of the obligations which the surety has guaranteed and an order may be made even though the principal debtor is without funds. But an action will not lie where the debt is not an actual, accrued or definite debt or, if on its true construction, the guarantee precludes action before the creditor demands payment."<sup>279</sup>

In a suit against the principal debtor and sureties for recovery of the mortgage money the sureties paid the amount on passing of preliminary decree. The court said that this amounted to payment during the pendency of the suit. The court further said that, by operation of law, the suit became assigned in their favour and they could continue it against the principal debtor by virtue of the subrogation.<sup>280</sup>

## 2. Right to indemnity [S. 145]

**S. 145. Implied promise to indemnify surety.**—In every contract of guarantee there is an implied promise by the principal debtor to indemnify the surety; and the surety is entitled to recover from the principal debtor whatever sum he has rightfully paid under the guarantee, but no sums which he has paid wrongfully.

### *Illustrations*

- (a) *B* indebted to *C*, and *A* is surety for the debt. *C* demands payment from *A*, and on his refusal sues him for the amount. *A* defends the suit, having reasonable grounds for

277. (3rd Edn) 138, para 327. See, AIR 1987 Cal 280 at 283.

278. (28th Edn by P.V. Baker and P. St. J. Langan) 467.

279. The court also cited a passage from **CHITTY ON CONTRACTS** (24th Edn) Vol 11, para 4855 to the effect that there are certain potential and inchoate rights of surety before payment. See at p. 283, AIR 1987 Cal. See *Jagdish Chandra Sahani v Prakash Kaur*, (1997) 2 MPLJ 320, the rights under S. 140 are available only against the principal debtor and not co-sureties. Against co-sureties there is only the right to contribution under Ss. 146 and 147.

280. *Kadamba Sugar Industries (P) Ltd v Devru Ganapathi Hedge Bhairi*, AIR 1993 Kant 288.

doing so, but is compelled to pay the amount of the debt with costs. He can recover from *B* the amount paid by him for costs, as well as the principal debt.

- (b) *C* lends *B* a sum of money, and *A*, at the request of *B*, accepts a bill of exchange drawn by *B* upon *A* to secure the amount. *C*, the holder of the bill, demands payment of it from *A*, and, on *A*'s refusal to pay, sues him upon the bill. *A*, not having reasonable grounds for so doing, defends the suit, and has to pay the amount of the bill and costs. He can recover from *B* the amount of the bill, but not the sum paid for costs, as there was no real ground for defending the action.
- (c) *A* guarantees to *C*, to the extent of 2000 rupees, payment for rice to be supplied by *C* to *B*. *C* supplies to *B* rice to a less amount than 2000 rupees, but obtains from *A* payment of the sum of 2000 rupees in respect of the rice supplied. *A* cannot recover from *B* more than the price of the rice actually supplied.

Thus in every contract of guarantee there is an implied promise by the principal debtor to indemnify the surety. The right enables the surety to recover from the principal debtor whatever sum he has rightfully paid under the guarantee,<sup>281</sup> but not sums which he paid wrongfully. An example of wrongful payment is a case where a surety had guaranteed the payment of four motor vehicles delivered on hire-purchase. The surety contended that he had paid Rs 4000 in discharge of his liability, but he failed to give an account of the price which the motor vehicles might have realised on resale. He was not allowed to recover his indemnity.<sup>282</sup>

### Rights against creditor

The surety enjoys the following rights against the creditor:

1. Right to securities [S. 141]
2. Right to share reduction
3. Right of set off

#### 1. Right to securities [S. 141]

**S. 141. Surety's right to benefit of creditor's securities.**—A surety is entitled to the benefit of every security which the creditor has against the principal debtor at the time when the contract of suretyship is entered into, whether the surety knows of the existence of such security or not; and, if the creditor loses, or, without the consent of the surety, parts, with such security, the surety is discharged to the extent of the value of the security.

#### Illustrations

- (a) *C* advances to *B*, his tenant, 2000 rupees on the guarantee of *A*. *C* has also a further security for the 2000 rupees by a mortgage of *B*'s furniture. *C* cancels the mortgage. *B*

281. *Supreme Leasing v Low Chuan Henry*, 1989 Current LJ 809 (Kuala Lumpur). *Shri Bishwakarma Furniture Workshop v Santanu Sarkar*, (2006) 5 AIR Kant (NOC) 762 (Jha): AIR 2006 Jhar 89, surety paid off the creditor, allowed to recover his indemnity from the principal. The principal's plea that he had agreed to pay without any such claim was not proved by him. *Karnail Singh Randhawa v Jagir Kaur*, (2008) 66 AIC 539 (P&H), entitled to recover the same amount from the principal, can also recover interest on it.

282. *Chekka Ponnamma v A.S. Thammayya*, AIR 1983 Kant 124.

becomes insolvent, and *C* sues *A* on his guarantee. *A* is discharged from liability to the amount of the value of the furniture.

- (b) *C*, a creditor, whose advance to *B* is secured by a decree, receives also a guarantee for that advance from *A*. *C* afterwards takes *B*'s goods in execution under the decree, and then, without the knowledge of *A*, withdraws the execution. *A* is discharged.
- (c) *A*, as surety for *B*, makes a bond jointly with *B* to *C*, to secure a loan from *C* to *B*. Afterwards, *C* obtains from *B* a further security for the same debt. Subsequently *C* gives up the further security. *A* is not discharged.

The section recognises and incorporates the general rule of equity as expounded in *Craythorne v Swinburne*<sup>283</sup> that the surety is entitled to every remedy which the creditor has against the principal debtor, including enforcement of every security.<sup>284</sup>

On paying off the creditor the surety steps into his shoes and gets the right to have the securities, if any, which the creditor has against the principal debtor.<sup>285</sup> The right exists irrespective of the fact whether the surety knows of the existence of such security or not. "It is the duty of the creditor to keep the securities intact; not to give them up or to burden with further advances."<sup>286</sup>

The plaintiffs lent to *B* and *P*, who were traders, £300 for the payment of which the defendant became surety. At the time of the loan *B* and *P* assigned by deed as security for the debt, the lease of their business premises and plant, fixtures and things thereon. The plaintiff had the right to sell on default by giving a month's notice. The default took place, but the defendant did not enter into possession. He received notice of the debtors' insolvency but allowed them to continue in possession. Consequently the assets were seized and sold by the receiver. It was held that the plaintiffs, by their omission to seize the property assigned on default, had deprived themselves of the power to assign the security to the surety. He was, therefore, discharged to the amount that the goods were worth.<sup>287</sup>

283. (1807) 14 Ves Jun 160: 33 ER 482.

284. *Industrial Finance Corp of India Ltd v Cannanore Spg & Wvg Mills Ltd*, (2002) 5 SCC 54: AIR 2002 SC 1841: (2002) 110 Comp Cas 685.

285. The term "security" is not used in any technical sense but as including all rights which the creditor has against the property of the principal. *State of M.P. v Kaluram*, AIR 1967 SC 1105: (1967) 1 SCR 266.

286. *Forbes v Jackson*, (1882) LR 19 Ch D 615, 621. See also *Amritlal Goverdhan Lalan v State Bank of Travancore*, AIR 1968 SC 1432. Where a car was delivered on hire-purchase, the payment of instalments of hire guaranteed by the surety and the car was seized because of the hirer's default but returned to him on his paying a small amount and under no information to the surety, the surety was held to be absolved from liability. *Kunjuvareeth v Union of India*, (1991) 1 KLT 49 (SN); *Ibrahim Abdul Latif Shaikh v Corpn Bank*, AIR 2003 Kant 98: (2003) 1 ICC 726, in the absence of an agreement to that effect, the surety cannot ask the creditor to proceed against security at a particular time. It is a discretion of the creditor. Forfearance on his part in that respect does not absolve the surety of his liability. *Mukesh Gupta v SIMCOM Ltd*, AIR 2004 Bom 104: (2004) 2 BC 470: (2004) 2 Bom CR 290: (2004) 1 Mah LJ 159 the surety had waived the benefits under Ss. 140, 141, not permissible for him to contend that he stood discharged because of the failure of the principal debtor to take timely steps to preserve the security or to call for additional security.

287. *Wuff & Billing v Jay*, (1872) LR 7 QB 756.



Where certain bills of exchange were given by way of collateral security and they being dishonoured, the creditor made them useless by not doing anything within the period of limitation, the surety was discharged to the extent of their value.<sup>288</sup>

If the securities are burdened with further advances it will not affect the rights of the surety. For example, in *Forbes v Jackson*:<sup>289</sup>

The principal debtor borrowed £200 on mortgaging his leasehold premises and a policy of life insurance, the defendant joining as a surety. The principal debtor borrowed further sums from the creditor on the same securities, the surety knowing nothing about it. The principal debtor failed to pay. The surety paid off £200 and interest and claimed both the securities. The creditor demanded payment of the further advances also. But it was held that the surety's right to the securities was not affected by the further advances and, therefore, he was entitled to both the securities.

According to English law, the surety has a right to securities which the creditor in fact has against the principal debtor, whether the surety knew of them or not and whether they were received before or after the guarantee.

"The expression 'security' in Section 141 is not used in any technical sense; it includes all rights which the creditor had against the property at the date of contract." This statement occurs in the judgment of SHAH J (afterwards CJ) of the Supreme Court in *State of M.P. v Kaluram*.<sup>290</sup>

The State sold a lot of felled timber to a person for a fixed price payable in four equal instalments, the payment of which was guaranteed by the defendant. The contract further provided that if a default was made in the payment of an instalment, the State would get the right to prevent further removal of the timber and to sell the remaining timber for the realisation of the price. The buyer defaulted but even so the State allowed him to remove the timber.

The surety was then sued for the loss. But he was held not liable. "The State had a charge over the goods sold as well as to remain in possession till payment of the instalments. When the goods were removed by the buyer that

288. *M. Rammairain (P) Ltd v State Trading Corp of India*, AIR 1988 Bom 45.

289. (1882) LR 19 Ch D 615. *Padamakar K. Bhagwathar v State Bank of India*, (2006) 2 AIR Kant (NOC) 228 (Bom) contract provision that the surety would not be discharged by reason of the failure of the bank to take any further security, valid and effective.

290. AIR 1967 SC 1105; (1967) 1 SCR 266; reaffirmed, *Amritlal Goverdhan Lalan v State Bank of Travancore*, AIR 1968 SC 1432: (1968) 3 SCR 724. In ignorance of this decision the Karnataka High Court held in *Karnataka Bank Ltd v Gajanan Shankararao Kulkarni*, AIR 1977 Kant 14 and again in *R. Lilavati v Bank of Baroda*, AIR 1987 Kant 2 that a mere passive activity or passive negligence on the part of the creditor by failing to realise the debt from the collateral security is not sufficient in itself to discharge the surety. If this view is correct, the effect would be that the creditor can passively permit the securities to be lost, but should not do something active to destroy them. The court proceeded on the logic that the surety can himself take steps to seize the security by paying out the creditor.



security was lost and to the extent of the value of the security lost, the surety stood discharged." The court also pointed out that it was immaterial that the loss of securities was due to a mere inaction and not to a positive action.

The difference between the English law and the principle laid down in Section 141 was explained by the Supreme Court in *Amritlal Goverdhan Lalan v State Bank of Travancore*:<sup>291</sup> "It is true that Section 141 has limited the surety's right to securities held by the creditor at the date of his becoming surety and has modified the English rule that the surety is entitled to the securities given to the creditor both before and after the contract of guarantee. But subject to this variation, Section 141 incorporates the rule of English law relating to discharge from liability of a surety when the creditor parts with or loses the security held by him."



CASE PILOT

**WHEN RIGHT TO SECURITIES ACCRUES.**—When is the surety entitled to the securities? Obviously, only on paying the debt. Difficulty, however, arises when the surety has guaranteed only a part of the debt and consequently even when he has paid all that he was liable for, the creditor's claim against the principal debtor is not yet fully satisfied. The Bombay High Court considered the question in *Goverdhandas Goculdas Tejpal v Bank of Bengal*.<sup>292</sup>



CASE PILOT

Certain mortgages were given to a bank as security for debts amounting to Rs 3,15,000. The plaintiff, who was a surety in part, paid Rs 1,25,000 and claimed that he was entitled to that extent to stand in the place of the Bank and to receive a share of the proceeds of the said securities proportioned to the sum which he had paid.

FARRAN J considered the English authorities and following them, said: "A surety who has paid the debt, which he has guaranteed, has a right to the securities held by the creditors, because as between the principal debtor and surety the principal is under an obligation to indemnify the surety. The equity between the creditor and the surety is that the creditor shall not do anything to deprive the surety of that right. But the creditor's right to hold his securities is paramount to the surety's claim upon such securities, which only arises when the creditor's claim against such securities has been satisfied."

The Madras High Court has differed not only from this opinion but also from the fact whether this is the effect of the English decisions.<sup>293</sup> The case before it was *Parvateneni Bhushayya v Potluri Suryanarayana*.<sup>294</sup>

The Imperial Bank advanced three different loans to a person with three different sureties for each loan. The principal debtor did not repay the loans in time and, therefore, the bank obtained mortgage of his property. Ultimately the bank had to file suits and three different decrees were

291. AIR 1968 SC 1432: (1968) 3 SCR 724, 733.

292. ILR (1891-92) 15 Bom 48.

293. For a contrary decision, see *Goodwin v Gray*, (1874) 22 WR 312.

294. AIR 1944 Mad 195: ILR 1944 Mad 340.

obtained against the principal debtor and the surety on each loan. The first two sureties paid off the decrees for which they were sureties but the third did not.

The question on these facts was whether the first two sureties who had paid off their obligations were entitled to a proportionate share in the mortgage, while a part of the bank's claim against the principal was still unsatisfied. KRISHNASWAMI AYYANGER J held that they were so entitled. He said: "Section 140 ... expressly says that the surety upon payment of all that he is liable for is invested, that is, immediately invested, with all the rights which the creditor had against the principal debtor. The condition laid down by the section for this right to arise is the payment by the surety of all that he is liable for, and not the payment of all that may be due to the creditor who holds the securities. Where the guaranteed debt is fraction only of the debt, the surety's right comes into existence immediately on payment of that fraction, for that fraction is, so far as he is concerned, the whole."<sup>295</sup> The learned Judge then considered Indian and English authorities and came to the conclusion that "the result of the discussion on a careful consideration of the decided cases is that a surety for a part only of a debt is on payment of that part entitled *pro tanto* to the security held by the creditor as a cover for the debt as a whole".<sup>296</sup>

Where the evidence did not disclose that the creditor had anything to do with the loss of the hypothecated properties, the surety was not permitted to claim any reduction of liability in that respect. The act of losing or parting with a security has to be a voluntary act on the part of the creditor. The loss has to be due to an act which is attributable to the creditor.<sup>297</sup> The decision of the Karnataka High Court<sup>298</sup> was on the basis of a surety bond which provided that the surety would not claim the benefit of Section 141. The section does not carry the words "not notwithstanding anything contained to the contrary, etc.", but even so the court held that by reason of the provision in Section 128, which permits liability to be regulated by agreement, a surety can waive the benefit of any of the provisions touching his liability.<sup>299</sup>

295. See *Sass, re, National Provincial Bank of England Ltd, ex p*, (1896) 2 QB 12. *Ibid* at p. 204.

296. *Parvateneni Bhushayya v Potluri Suryanarayana*, AIR 1944 Mad 195: ILR 1944 Mad 340 at p. 206. The learned Judge considered the decision of the Privy Council on appeal from the Calcutta High Court in *Carr Lazarus Phillips v Alfred Ernest Mitchell*, AIR 1930 Cal 17: ILR (1930) 57 Cal 764. On appeal, *A.E. Mitchell v C.L. Phillips*, (1930–31) 58 IA 306: AIR 1931 PC 224.

297. *Industrial Finance Corp of India Ltd v Cannanore Spg & Wvg Mills Ltd*, (2002) 5 SCC 54: AIR 2002 SC 1841: (2002) 110 Comp Cas 685.

298. *R. Lilavati v Bank of Baroda*, AIR 1987 Kant 2.

299. See also *Perwatra Habib Bank v Sehatian Development*, (1994) 1 Curr LJ 394 (Malaysia) where a clause in the contract of guarantee enabled the creditor to vary the terms of the agreement without any need for reference to the guarantors.

### *Hypothecation is only equitable charge*

The section is not applicable to hypothecation, it being only an equitable charge. The goods remain with the borrower and normally the question of their being lost by the creditor does not arise.<sup>300</sup>

### *2. Right to share reduction*

This right may be illustrated by the case of *Hobson v Bass*:<sup>301</sup>

*J* gave a guarantee to *B* in the following words: "I hereby guarantee to you the payment of all goods you may supply to *E.H.*, but so as my liability to you under this or any other guarantee shall not at any time exceed the sum of £250." *E* gave a similar guarantee. *B* supplied goods to *E.H.*, to the amount of £657. *E.H.* became bankrupt. *B* proved the whole sum in the insolvency of *E.H.* and then called on the guarantors who paid him £250 each. Subsequently *B* received from the receiver a sum of 2s, and, 1d... in the pound on £657. It was held that each of the guarantors was entitled to a part of the dividend bearing to the whole the same proportion as £250 to 657.<sup>302</sup>

### *3. Right of set-off*

If the creditor sues the surety, the surety may have the benefit of the set-off, if any, that the principal debtor had against the creditor. He is entitled to use the defences of the debtor against the creditor. If, for example, the creditor owes him something, or the creditor has in his hand something belonging to the debtor for which the creditor could have counter-claimed, the surety can also put up that counter-claim.<sup>303</sup>

He can claim such a right not only against the creditor, but also against third parties who have derived their title from the creditor. Thus where a mercantile agent sold the goods of his principal and, being a surety for payment of the price to the principal, had to pay it, he was held to have become entitled to the unpaid seller's lien against the buyer and those deriving title from him.<sup>304</sup>

## **Rights against co-sureties**

Where a debt has been guaranteed by more than one person, they are called co-sureties. Some of their rights against each other are:

1. Effect of releasing a surety;
2. Right to contribution.

300. *Bank of India v Yogeshwar Kant Wadhera*, AIR 1987 P&H 176.

301. (1871) LR 6 Ch App 792.

302. See also *Bardwell v Lydall*, (1831) 7 Bing 489: 131 ER 189.

303. *Bechervaise v Lewis*, (1872) LR 7 CP 372.

304. *Wolmershausen v Gullick*, (1893) 2 Ch 514.

1. *Effect of releasing a surety [S. 138]*

**S. 138. Release of one co-surety does not discharge others.**—Where there are co-sureties, a release by the creditor of one of them does not discharge the others; neither does it free the surety so released from his responsibility to the other sureties.

The creditor may at his will release any of the co-sureties from his liability. But that will not operate as a discharge of his co-sureties. However, the released co-surety will remain liable to the others for contribution in the event of default.<sup>305</sup>

2. *Right to contribution [Ss. 146–147]*

**S. 146. Co-sureties liable to contribute equally.**—Where two or more persons are co-sureties for the same debt or duty, either jointly or severally, and whether under the same or different contracts, and whether with or without the knowledge of each other, the co-sureties, in the absence of any contract to the contrary, are liable, as between themselves, to pay each an equal share of the whole debt, or of that part of it which remains unpaid by the principal debtor.

*Illustrations*

- (a) *A, B and C as sureties to D, for the sum of 3000 rupees lent to E. E makes default in payment. A, B and C are liable, as between themselves, to pay 1000 rupees each.*
- (b) *A, B and C are sureties to D for the sum of 1000 rupees lent to E, and there is a contract between A, B and C that A is to be responsible to the extent of one-quarter, B to the extent of one-quarter, and C to the extent of one-half. E makes default in payment. As between the sureties, A is liable to pay 250 rupees, B 250 rupees and C 500 rupees.*

**S. 147. Liability of co-sureties bound in different sums.**—Co-sureties who are bound in different sums are liable to pay equally as far as the limits of their respective obligations permit.

*Illustrations*

- (a) *A, B and C as sureties for D, enter into three several bonds each in a different penalty, namely, A in the penalty of 10,000 rupees, B in that of 20,000 rupees, C in that of 40,000 rupees, conditioned for D's duly accounting to E. D makes default to the extent of 30,000 rupees. A, B and C are liable to pay 10,000 rupees.*
- (b) *A, B and C, as sureties for D, enter into three several bonds, each in a different penalty, namely, A in the penalty of 10,000 rupees, B in that of 20,000 rupees, C in that of 40,000 rupees conditioned for D's duly accounting to E. D makes default to the extent of 40,000 rupees. A is liable to pay 10,000 rupees, and B and C 15,000 rupees each.*
- (c) *A, B and C, as sureties for D, enter into three several bonds, each in a different penalty, namely, A in the penalty of 10,000 rupees, B in that of 20,000 rupees, C in that of 40,000 rupees, conditioned for D's duly accounting to E. D makes default to the extent of 70,000 rupees. A, B and C have to pay each the full penalty of his bond.*

Where there are several sureties for the same debt and the principal debtor has committed a default, each surety is liable to contribute equally to the

305. *Sri Chand v Jagdish Parshad Kishan Chand*, AIR 1966 SC 1427: (1966) 3 SCR 451, 456–57; *Rajamma v C. Puttachari*, (2005) AIR Kant 1542.

extent of the default.<sup>306</sup> If one of them has been compelled to pay more than his share, he can recover contribution from his co-sureties so as to equalise the loss as between all of them.<sup>307</sup> Thus, if there are three sureties and a default of three thousand rupees has taken place, each surety must contribute one thousand rupees. The principle will apply whether their liability is joint or several, under the same or different contracts, and whether with or without the knowledge of each other.

The principle was applied by the English Court of Appeal even to a case in which payment was made by one of the co-sureties even before there was any formal demand by the creditor as required by the guarantee. The court said that it was necessary for this purpose that the co-surety must not have acted officiously or voluntarily. A demand is not a precondition for liability under a guarantee. It is rather a procedural and evidentiary requirement. It is there for the benefit of the surety alone. He could waive it. Where the creditor is entitled to proceed against either co-surety without notifying the other, such waiver by one co-surety would not deprive him of his entitlement to contribution from the other who has not been specially disadvantaged.<sup>308</sup> PETER GIBSON LJ summarised the law thus:<sup>309</sup> "Let me start by setting out certain uncontroversial principles applicable in this area of the law:

(1) Where more than one person guarantee to the creditor the payment of the same debt, an equity arises such that if one of them pays more than his due proportion of the debt, he is entitled to a contribution from his co-guarantor or co-guarantors.

(2) It is immaterial whether the co-guarantors are bound jointly or severally or jointly and severally, or by the same instrument or by separate instruments, or in the same sum, or different sums, or at the same time or different times, or whether the co-guarantor making payment knows of the existence of the other co-guarantor or co-guarantors, as the right of contribution is not dependent upon agreement, express or implied.

(3) Normally an action for contribution cannot be brought until payment has been made by a co-guarantor of more than his share of the common liability.

(4) In particular circumstances an action for contribution will lie even before payment is made; thus when judgment has been entered by the creditor against one guarantor, who has paid nothing in respect of the judgment, he can maintain an action in equity against his co-guarantor and obtain an order requiring payment of the co-guarantor's due share to the creditor (if a party to the action) or (if the creditor is not a party) an order that the co-guarantor indemnify the judgment-debtor, on payment of his own share, against further liability."

306. *SBI v Prem Dass*, AIR 1998 Del 49, a bank loan was guaranteed by more than one guarantors, they were held jointly and severally liable to pay the principal debt.

307. *Shirley v Burdett*, (1911) 2 Ch 418; *Wolmershausen v Gullick*, (1893) 2 Ch 514.

308. *Stimpson v Smith*, 1999 Ch 340: (1999) 2 WLR 1292 (CA).

309. *Ibid* at p. 837.

These principles are all subject to any contractual terms which may limit or extend the entitlement of an interested person.

Is the service of a demand in writing in accordance with the guarantee, a precondition of liability under the guarantee? It would be surprising if an evidentiary or procedural requirement of service of a written demand in the guarantee was a precondition.

The only textbook which deals with the specific point is Andrews and Millett, *LAW OF GUARANTEES*.<sup>310</sup> The editors say:<sup>311</sup>

“It is submitted that strictly speaking there is no restriction upon the time at which a surety can apply for relief against his co-sureties, provided that the account between the principal (debtor) and the creditor is closed and there is an immediate liability due and payable under the guarantee such that the amount of the contribution can be properly ascertained. It is immaterial that the creditor has not yet demanded payment, or even that the creditor is obliged under the terms of the guarantee to make a demand before the surety is liable. It is enough that the creditor could enforce the guarantee, either forthwith or after making a demand for more than the surety’s rateable share. This is certainly the case with *qua times* relief against the principal debtor for an indemnity, and there is no reason why the same should not apply against the co-surety for contribution.”

The principle of equal contribution is subject to the maximum limit, if any, fixed by a surety to his liability. This is so because Section 147 lays down that “co-sureties who are bound in different sums are liable to pay equally as far as the limits of their respective obligations permit”. Suppose that A, B and C are three sureties for a debt. A undertakes to be liable up to Rs 200, B up to Rs 400 and C for Rs 600. The principal debtor makes a default of Rs 600. Each surety must contribute Rs 200. But if the default is of Rs 900, then according to the principle of equal contribution, each would be liable for Rs 300; this being more than the limit of A’s obligation, he can be required to contribute only Rs 200. The remaining seven hundred will be apportioned between B and C equally.

### Indemnity and guarantee distinguished

Indemnity and guarantee have this common feature that both are devices for providing protection against a probable loss. In either case the loss may arise due to human conduct. However, the technique of providing protection, the need and occasion for protection and the number of parties involved mark some differences between them. “Guarantees and indemnities, which are also described as securities, are distinct arrangements under which a third party, the surety, agrees to assume liability if the debtor defaults or

310. (2nd Edn, 1994).

311. At p. 360.

causes loss to the creditor. The former arrangement is a guarantee, the latter involves an indemnity.”<sup>312</sup>

1. The liability under a contract of indemnity is contingent in the sense that it may or may not arise.<sup>313</sup> Under a guarantee, on the other hand, the liability is subsisting in the sense that once a guarantee has been acted upon, the liability of the surety automatically arises, though it remains in suspended animation till the principal debtor commits default.

2. The undertaking in a guarantee is collateral, in an indemnity it is original. The purpose of a guarantee is to support the primary liability of a third person. In an indemnity, there being no third person, the indemnifier’s liability is in itself “primary”.<sup>314</sup>

3. In a contract of indemnity there are only two parties, namely, the indemnifier and the indemnity-holder. But there are three parties to a guarantee, the creditor, the principal debtor and the surety. It is a tripartite arrangement.

4. In an indemnity there is only one contract, that is, the contract of indemnity against loss between the indemnity-holder and the indemnifier. But in a guarantee there are three contracts, namely, a contract of loan between the principal debtor and the creditor; a contract of guarantee between the creditor and the surety and finally an implied contract of indemnity between the principal debtor and the surety.

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312. Ellinger, MODERN BANKING LAW, 259 (1987). See *Jayakrishna Trading Co v Kandasamy Wvg Factory & Co*, 1994 SCC OnLine Mad 502: (1995) 1 LW 230. In this case guarantee was given not at the request of the principal debtor, no liability for the default of the principal debtor in such a case.

313. *Unity Finance Ltd v Woodcock*, (1963) 1 WLR 455 (CA).

314. See Cheshire and Fifoot, LAW OF CONTRACT (9th Edn by Furmston, 1976) 181.

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- *Allahabad Bank v S.M. Engg Industries*, (1992) 1 Cal LJ 448
- *Amritlal Goverdhan Lalan v State Bank of Travancore*, AIR 1968 SC 1432: (1968) 3 SCR 724
- *Bank of Bihar Ltd v Damodar Prasad*, AIR 1969 SC 297: (1969) 1 SCR 620
- *Bombay Dyeing & Mfg Co Ltd v State of Bombay*, AIR 1958 SC 328: 1958 SCR 1122
- *Centax (India) Ltd v Vinmar Impex Inc*, (1986) 4 SCC 136
- *Goverdhandas Goculdas Tejpal v Bank of Bengal*, ILR (1891–92) 15 Bom 48
- *Industrial Finance Corp of India Ltd v Cannanore Spg & Wvg Mills Ltd*, (2002) 5 SCC 54
- *London General Omnibus Co v Holloway*, (1912) 2 KB 72 (CA)
- *M.S. Anirudhan v Thomco's Bank Ltd*, AIR 1963 SC 746: (1963) 1 SCR 63: (1963) 33 Comp Cas 185
- *Maharashtra SEB v Official Liquidator*, (1982) 3 SCC 358
- *State of M.P. v Kaluram*, AIR 1967 SC 1105: (1967) 1 SCR 266
- *U.P. Coop Federation Ltd v Singh Consultants and Engineers (P) Ltd*, (1988) 1 SCC 174
- *Union Bank of India v Avinash P. Bhonsle*, 1991 Mah LJ 1004



13

## Bailment

Bailment implies a sort of relationship in which the personal property of one person temporarily goes into the possession of another. The ownership of the articles or goods is in one person and the possession in another. The circumstances in which this happens are numerous. Delivering a cycle, watch or any other article for repair, or leaving a cycle or car, etc., at a stand, depositing luggage or books in a cloakroom, delivering gold to a goldsmith for making ornaments, delivering garments to a dry-cleaner, delivering goods for carriage, warehousing or storage and so forth, are all familiar situations which create the relationship of bailment. Thus bailment is a subject of considerable public importance.<sup>1</sup>

### DEFINITION

“Bailment” is defined in Section 148 of the Indian Contract Act in the following words:

**S. 148. “Bailment”, “bailor” and “bailee” defined.**—A “bailment” is the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them. The person delivering the goods is called the “bailor”. The person to whom they are delivered is called the “bailee”.

*Explanation.*—If a person already in possession of the goods of another contracts to hold them as a bailee, he thereby becomes the bailee, and the owner becomes the bailor of such goods, although they may not have been delivered by way of bailment.

### ESSENTIAL FEATURES

The following essential features of “bailment” are emphasised by this definition.

#### 1. Delivery of possession

The first important characteristic of bailment is “the delivery of possession” by one person to another.<sup>2</sup> “Delivery of possession” for this purpose

1. See, for example, C.V. Davidge, *Bailment*, (1925) 41 LQR 433.

2. *New India Assurance Co Ltd v DDA*, (1991) 2 PLR (Del) 82, the essence of bailment is possession. Delivery of truck to the parking centre, receipt issued for charges, safe keeping

should be distinguished from a mere "custody". "One who has custody without possession, like a servant, or a guest using his host's goods is not a bailee."<sup>3</sup> The goods must be handed over to the bailee for whatever is the purpose of bailment. Once this is done, a bailment arises, irrespective of the manner in which this happens.

An old customer went into a restaurant for the purpose of dining there. When he entered the room a waiter took his coat, without being asked, and hung it on a hook behind him. When the customer rose to leave the coat was gone.<sup>4</sup>

What the waiter did might be no more than an act of voluntary courtesy towards the customer, yet the restaurant-keeper was held liable as a bailee. The waiter by taking the coat into his possession had relieved the plaintiff of its care and had thus assumed the responsibility of a bailee. It was he who selected the place where the coat should be put.

If the customer had instructed the servant where and how the coat should be put, the result, perhaps, would have been otherwise. To take, for instance, a decision of the Madras High Court.<sup>5</sup>

A lady handed over to a goldsmith certain jewels for the purpose of being melted and utilized for making new jewels. Every evening as soon as the goldsmith's work for the day was over, the lady used to receive half-made jewels from the goldsmith and put them into a box in the goldsmith's room and keep the key in her possession. The jewels were lost one night.

But the lady's action against the goldsmith failed, the court saying: "Any bailment that could be gathered from the facts must be taken to have come to an end as soon as the plaintiff was put in possession of the melted gold. Delivery is necessary to constitute bailment. The mere leaving of box in a room in the defendant's house, when the plaintiff herself took away the key, cannot certainly amount to delivery within the meaning of the provision in Section 149."

#### *Bank locker*

On the same principle, the hiring of a bank's locker and storing things in it would not constitute a bailment. Things kept there are in a way put in a hired portion of the premises and not entrusted to the bank. The court also found that there was no proof of the fact that at the time when bank locker was robbed the customer had some items of jewellery in the locker. The

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for 24 hours. The owner of the centre could not return the vehicle nor he gave any plausible explanation for its absence, held liable for the loss.

3. Pollock and Mulla, INDIAN CONTRACT AND SPECIFIC RELIEF ACTS (1957) 560. See also *Reeves v Capper*, (1838) 5 Bing NC 136: 132 ER 1057, where the custody of a servant is distinguished from delivery of possession to a bailee.

4. *Ultzen v Nicols*, (1894) 1 QB 92.

5. *Kaliaperumal Pillai v Visalakshmi*, AIR 1938 Mad 32.



court further said that it could not be inferred without proof that the strong room and lockers were not built according to specifications. The customer was not allowed to claim any damages.<sup>6</sup> The court said<sup>7</sup> that in order to constitute bailment within the meaning of Section 148 it is necessary to show that actual and exclusive possession of the property was given by the hirer of the locker to the bank. It is only then that the question of reasonable care and damages would arise. As it was, it was impossible to know the quantity, quality or the value of the jewellery that was there in the locker. It is also not a relationship of landlord and tenant. The locker-holder has no direct access to his locker, nor he can operate it of his own. He can do so only with the assistance of the bank.

#### *Actual or constructive delivery*

Section 149 explains the meaning of delivery of possession.

**S. 149. Delivery to bailee how made.**—The delivery to the bailee may be made by doing anything which has the effect of putting the goods in the possession of the intended bailee or of any person authorised to hold them on his behalf.

An explanation to Section 148 provides that “if a person already in possession of the goods of another contracts to hold them as a bailee, he thereby becomes the bailee and the owner becomes the bailor although they may not have been delivered by way of bailment”.

Delivery of possession is thus of two kinds, namely:

- (1) actual delivery, and
- (2) constructive delivery.

When the bailor hands over to the bailee physical possession of the goods, that is called “actual delivery”. “Constructive delivery” takes place when there is no change of physical possession, goods remaining where they are, but something is done which has the effect of putting them in the possession of the bailee. For example, delivery of a railway receipt amounts to delivery of the goods.<sup>8</sup> Similarly, where a person pledged the projector machinery of his cinema under an agreement which allowed him to retain the machinery for the use of the cinema, the Andhra Pradesh High Court<sup>9</sup> observed:

“It must be held that there was a constructive delivery, or delivery by attornment to the bank. Since then there was a change in the legal character of the possession of goods, though not in the actual and physical

6. *Atul Mehra v Bank of Maharashtra*, AIR 2003 P&H 11: (2003) 2 BC 570: (2002) 3 ICC 138.

7. *Ibid* at p. 17. Citing at p. 16 *Port Swettenham Authority v T.W. Wu & Co (M) Sdn Bhd*, 1979 AC 580: (1978) 3 WLR 530 statement to the effect that a banker is under no obligation to accept a parcel for safe custody and where he is asked to do so, he could ask to know the contents and value in order to gauge the nature and extent of any possible liability.

8. See *Morvi Mercantile Bank Ltd v Union of India*, AIR 1965 SC 1954: (1965) 3 SCR 254.

9. *Bank of Chittoor v Narasimbulu*, AIR 1966 AP 163.

custody. Even though the bailor continued to remain in possession, it was the possession of the bailee.”<sup>10</sup>

Another illustration of constructive delivery is *Fazal v Salamat Rai*.<sup>11</sup>

The defendant was holding the plaintiff’s mare under the execution of a decree. The plaintiff satisfied the decree and the court ordered redelivery of the mare to the plaintiff. The defendant, however, refused to do so unless his maintenance charges were also paid. The mare was stolen from his custody.

Holding him liable, the court said that after the delivery order had been passed, the relation of bailor and bailee was established by virtue of the Explanation to Section 148.

In a case before the Supreme Court the owner of a car involved in an accident delivered it under the policy on behalf of the insurer to the nearest garage for repairs. This delivery was regarded as sufficient to constitute the insurance company as a bailee and the garage as a sub-bailee. They became responsible for the loss of the car in a fire on the premises.<sup>12</sup>

## 2. Delivery should be upon contract

Delivery of goods should be made for some purpose and upon a contract that when the purpose is accomplished the goods shall be returned to the bailor. When a person’s goods go into the possession of another without any contract, there is no bailment within the meaning of its definition in Section 148. A well-known illustration is the decision of the Allahabad High Court in *Ram Gulam v Govt of U.P.*<sup>13</sup>

The plaintiff’s ornaments, having been stolen, were recovered by the police and, while in police custody, were stolen again. The plaintiff’s action against the State for the loss was dismissed.

SETH J said: “...the obligation of a bailee is a contractual obligation and springs only from the contract of bailment. It cannot arise independently of a contract. In this case the ornaments were not made over to the Government under any contract whatsoever.... The Government, therefore, never occupied the position of bailee and is not liable as such to indemnify the plaintiffs.”<sup>14</sup>

10. Per VENKATASWAMI J at p. 166, *ibid*.

11. (1928) 120 IC 421. Goods which cannot be delivered, like a film not yet produced, cannot be pledged. *Chief Controlling Revenue Authority v Sudarsanam Picture*, AIR 1968 Mad 319.

12. *N.R. Srinivasa Iyer v New India Assurance Co Ltd*, (1983) 3 SCC 458: AIR 1983 SC 899.

13. AIR 1950 All 206. See also *Oma Prasad v Secy of State*, AIR 1937 Lah 572; (1937) 172 IC 567; *Surendra Nath Koley v Kali Kumar Sen*, AIR 1956 Ass 55, hiring of elephants is not bailment unless so agreed. *Anamalai Timber Trust Ltd v Trippunitchura Devaswom*, AIR 1954 TC 305.

14. To the same effect is *Mohd Murad Ibrahim Khan v Govt of U.P.*, AIR 1956 All 75, property deposited in court under orders, no bailment because there was no contract. In Pollock and Mulla, INDIAN CONTRACT AND SPECIFIC RELIEF ACTS (8th Edn, 1957) 562, this assumption has been described as unjustifiable.



### *Non-contractual bailments*

English law recognises bailment without contract. In the words of Cheshire and Fifoot: "At the present day, no doubt, in most instances where goods are lent or hired or deposited for safe custody, or as security for a debt, the delivery will be the result of a contract. But this ingredient, though usual, is not essential."<sup>15</sup>

The Bombay High Court in its decision in *Lasalgaoon Merchants Coop Bank Ltd v Prabhudas Hathibhai*<sup>16</sup> has taken the lead in imposing the obligation of a bailee without a contract. In the opinion of the court, as expressed through NAIK J, where certain goods belonging to an individual are seized by the Government the latter becomes the bailee thereof even if there is no suggestion of a contract between the Government and the individual. The facts stated briefly were as follows:

Certain packages of tobacco lying in the godown of a partnership firm were pledged to the plaintiff bank. Some of the partners, having failed to clear their income tax dues, the Income Tax Officer ordered seizure of the goods. The officials of the Collectorate accordingly locked the godown and handed over the key to the police. Then came heavy rains. The roof of the godown leaked and the tobacco was damaged.

The court said: "Heavy rains do not (necessarily) amount to an act of God. It was the duty of Government officers to take such care as every prudent manager would take of his own goods. The Government stood in the position of bailees and it was for them to prove that they had taken as much care as was (reasonably) possible for them and that the damage was due to reasons beyond their control."<sup>17</sup>

This view was accepted by the Supreme Court in *State of Gujarat v Memon Mahomed Haji Hasan*.<sup>18</sup>

Certain motor vehicles and other goods belonging to the plaintiffs were seized by the State in exercise of its powers under a Sea Customs Act. The goods while in the custody of the State remained totally uncared for.

It was contended on behalf of the State that as the State were not bailees, there was no obligation to take care. Referring to this SHELAT J observed as follows:<sup>19</sup> "That contention is not sustainable. Bailment is dealt with by the Contract Act only in cases where it arises from a contract, but it is not correct to say that there cannot be a bailment without an enforceable contract....

15. LAW OF CONTRACT (6th Edn, 1964) 73. See also the speech of Lord COLERIDGE CJ in *R. v Macdonald*, (1885) LR 15 QBD 323, 326 and CAVE J at p. 327. For an illustration of non-contractual bailment see *Gilchrist Watt & Sanderson Pty Ltd v York Products Pty Ltd*, (1970) 1 WLR 1262 (PC), where a party who unloaded goods became bailee for their safe custody.

16. AIR 1966 Bom 134.

17. *Ibid.* NAIK J at p. 140.

18. AIR 1967 SC 1885, 1888: (1967) 3 SCR 938.

19. *Ibid* at p. 1888.

Nor is consent indispensable for such a relationship to arise. A finder of goods of another has been held to be a bailee in certain circumstances.”

The court also cited the following passage from Pollock and Wright:<sup>20</sup> “Bailment is a relationship *sui generis* and unless it is sought to increase or diminish the burdens imposed upon the bailee by the very act of bailment, it is not necessary to incorporate it into the law of contract and to prove a consideration.”<sup>21</sup>

The trend set by these cases has been affirmed by the Supreme Court though without reference to them.<sup>22</sup> The facts involved a repetition of the *Ram Gulam*<sup>23</sup> story, namely, theft, recovery of the ornaments by the police and their final disappearance from police custody. The State was held liable to pay the value of the ornaments to the victim of the theft.

When the Port Trust is required to store imported goods, the relationship of bailor and bailee comes into existence. Under Section 42(6) of the Major Port Trusts Act, 1963, the Port Trust of a Major Port would be regarded as the bailee of the goods coming into its possession. The provisions of Sections 151, 152 and 161 of the Contract Act become applicable (duty of care and duty to return).<sup>24</sup>

### *Contract, express or implied*

The contract may be express or implied. Thus, where with the consent of the station-master goods were stored on a railway company's platform, wagons being not available, the company was held liable when they were damaged by fire caused by a spark emitted by a passing engine.<sup>25</sup>

### **3. Delivery should be upon some purpose**

Bailment of goods is always made for some purpose and is subject to the condition that when the purpose is accomplished the goods will be returned to the bailor or disposed of according to his mandate.<sup>26</sup> If the person to whom the goods are delivered is not bound to restore them to the person

20. POSSESSION IN THE COMMON LAW, 143.

21. *State of Gujarat v Memon Mahomed Haji Hasan*, AIR 1967 SC 1885, 1888: (1967) 3 SCR 938, 943.

22. *Basavu Kom Dyamangouda Patil v State of Mysore*, (1977) 4 SCC 358: 1977 SCC (Cri) 598: AIR 1977 SC 1749. B.B. Pandey welcomes this decision in his article, *Government Liability for the Goods Lost in Custody: A Step in the Direction of Reasonable Accountability*, (1977) 4 SCC 13 (Journal section).

23. *Ram Gulam v Govt of U.P.*, AIR 1950 All 206.

24. *Port of Bombay v Sriyanesh Knitters*, (1999) 7 SCC 359: AIR 1999 SC 2947.

25. *Governor General of India in Council v Jubilee Mills Ltd*, AIR 1953 Bom 46. Where, however, the goods were left after they were marked by the loading clerk and neither any railway receipt was obtained, nor the railway company made incharge of the goods, no bailment arose. *Lachmi Narain v Bombay, Baroda & Central India Rly Co*, ILR (1923) 45 All 235; *Dhanraj Agarwalla v Union of India*, AIR 1958 Ass 5.

26. *Gangaram v Crown*, AIR 1943 Nag 436, no bailment where the thing is not to be specifically accounted for.

delivering them or to deal with them according to his directions, their relationship will not be that of bailor and bailee.

The plaintiff delivered to the Treasury Officer at Meerut nine Government promissory notes for cancellation and consolidation into a single note of Rs 48,000. The defendant's servants misappropriated the notes. The plaintiff sued the State to hold them responsible as bailees.<sup>27</sup>

But his action failed. There can be no bailment unless there is a delivery of goods and a promise to return. The Government was not bound to return the same notes, nor was it bound to dispose of the surrendered notes in accordance with the plaintiff's directions.

#### *Bailment compared with other similar relations*

It is this feature of bailment which distinguishes it from many other transactions of the same kind. A deposit of money with a banker is not a bailment as he is not bound to return the same notes and coins.<sup>28</sup> Accordingly, a bank was not allowed to exercise the right of lien as a bailee on money held under a fixed deposit.<sup>29</sup> An agent who has collected money on his principal's behalf is not a bailee of the money for the same reason.<sup>30</sup> In the words of SHETTY J of the Supreme Court:<sup>31</sup> "One important distinguishing feature between agency and bailment is that the bailee does not represent the bailor. He merely exercises, with the leave of the bailor (under contract or otherwise), certain power of the bailor in respect of his property. Secondly, the bailee has no power to make contracts on bailor's behalf, nor can he make the bailor liable, simply as bailee, for any acts he does."<sup>32</sup> Applying this principle to the position of a banker who was holding the goods on behalf of its account-holder for the purpose of delivering them to his customers against payment, the court held that the bank was not thereby constituted into an agent and remained a bailee only.

A bailment is also distinguishable from sale, exchange or barter. In these transactions what is transferred is not mere possession, but also ownership and, therefore, the person buying is under no obligation to return. In a sale of beer bottles, one of the terms was that the price of the bottles would be refunded on the buyer returning the bottles. The transaction was held to be a sale of the bottles and not a bailment.<sup>33</sup> But hire-purchase contract is a

27. *Secy of State v Sheo Singh Rai*, (1875–80) 2 All 756.

28. *Ichha Dhanji v Natha*, ILR (1888) 13 Bom 338; *Devendrakumar v Gulabsingh*, AIR 1946 Nag 114; ILR 1946 Nag 210.

29. *Union Bank of India v K.V. Venugopalan*, AIR 1990 Ker 223.

30. *Shanker Lal v Bhura Lal*, AIR 1951 Ajm 24; *Bridges v Garrett*, (1870) LR 5 CP 451.

31. *UCO Bank v Hem Chandra Sarkar*, (1990) 3 SCC 389, 395; AIR 1990 SC 1329.

32. Citing Friedman's LAW OF AGENCY, 23 (5th Edn).

33. *Kalyani Breweries Ltd v State of W.B.*, (1997) 7 SCC 738; AIR 1998 SC 70, under the W.B. Sales Tax Act, 1954; distinguishing it from *United Breweries Ltd v State of A.P.*, (1997) 3 SCC 530; AIR 1997 SC 1316, where recovery of bottles was under a well-laid out system. *Raj Sheel v State of A.P.*, (1989) 3 SCC 262; AIR 1989 SC 1696; *State of Maharashtra v Britannia Biscuits Co Ltd*, 1995 Supp (2) SCC 72; (1995) 96 STC 642, deposit taken for tins, refundable



bailment, though of course, not merely a bailment. It has two aspects, bailment *plus* an element of sale.<sup>34</sup>

### *Post office, bailee*

Post Office is a bailee of the articles of the sender.<sup>35</sup>

### DUTY OF BAILOR

According to Section 150 which deals with the duty of bailor, bailors are of two kinds, namely:

- (1) gratuitous bailor, and
- (2) bailor for reward.

A person who lends his articles or goods without any charge, is called a "gratuitous bailor". His duty is naturally much less than that of a bailor for hire or consideration.

#### Duty of gratuitous bailor

Speaking of the duty of a gratuitous bailor, Section 150 says:

**S. 150. Bailor's duty to disclose faults in goods bailed.**—The bailor is bound to disclose to the bailee faults in the goods bailed, of which the bailor is aware, and which materially interfere with the use of them, or expose the bailee to extraordinary risks; and if he does not make such disclosure, he is responsible for damage arising to the bailee directly from such faults.

If the goods are bailed for hire, the bailor is responsible for such damage, whether he was or was not aware of the existence of such faults in the goods bailed.

#### *Illustrations*

- (a) A lends a horse, which he knows to be vicious, to B. He does not disclose the fact that the horse is vicious. The horse runs away. B is thrown and injured. A is responsible to B for damage sustained.
- (b) A hires a carriage of B. The carriage is unsafe, though B is not aware of it, and A is injured. B is responsible to A for the injury.

A person, for example, who lends his cycle or horse to a friend, and if he knows that the cycle is without brakes or that the horse is unsound, he should disclose this fact and his duty ends there. "Would it not be monstrous

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on return of tins. The court held that the tins would be deemed to be sold on the expiry of the time for return.

34. So held by the Supreme Court in a number of cases: *Instalment Supply (P) Ltd v Union of India*, AIR 1962 SC 53: (1962) 2 SCR 644; *K.L. Johar & Co v CTO*, AIR 1965 SC 1082: (1965) 2 SCR 112; *Damodar Valley Corpn v State of Bihar*, AIR 1961 SC 440: (1961) 2 SCR 522; *Sundaram Finance Ltd v State of Kerala*, AIR 1966 SC 1178: (1966) 2 SCR 828; *South Australian Insurance Co v Randell*, (1869) LR 3 PC 101, delivery of goods with a right to claim equivalent value in some other goods.
35. *CIT v P.M. Rathod & Co*, AIR 1959 SC 1394: (1960) 1 SCR 401. The position of post office in reference to VPP articles.



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to hold that if the owner of a horse, knowing it to be vicious and unmanageable, should lend it to one who is ignorant of its bad qualities and conceal them from him, and the rider, using ordinary care and skill, is thrown from it and injured, he should not be responsible? By the necessarily implied purpose of the loan a duty is contracted towards the borrower not to conceal from him those defects known to the lender which may make the loan perilous or unprofitable to him.”<sup>36</sup> The conditions of his liability are:

- (1) He should have knowledge of the defect and the bailee should not be aware.<sup>37</sup>
- (2) The defect in the goods must be such as exposes the bailee to extraordinary risks or materially interferes in the use of the goods.

### Duty of bailor for reward

The duty of a bailor for consideration is much greater. He is making profit from his profession and, therefore, it is his duty to see that the goods which he delivers are reasonably safe for the purpose of the bailment. It is no defence for him to say that he was not aware of the defect. Section 150 clearly says that “if the goods are bailed for hire, the bailor is responsible for such damage, whether he was or was not aware of such faults in the goods bailed”. He has to examine the goods and remove such defects as reasonable examination would have disclosed. In *Hyman & Wife v Nye & Sons*:<sup>38</sup>

The plaintiff hired from the defendant for a specific journey a carriage, a pair of horses and a driver. During the journey a bolt in the underpart of the carriage broke, the splinter bar became displaced, the carriage was upset and the plaintiff injured.

Holding the defendant liable LINDLEY J said: “A person who lets out carriages is not responsible for all defects discoverable or not; he is not an insurer against all defects. But he is an insurer against all the defects which care and skill can guard against. His duty is to supply a carriage as fit for the purpose for which it is hired as care and skill can render it.” Similarly in *Reed v Dean*:<sup>39</sup>

The plaintiffs hired a motor launch from the defendant for a holiday on the river Thames. The launch caught fire, and the plaintiffs were unable to extinguish it, the fire-fighting equipment being out of order. They were injured and suffered loss.

The court held that there was an implied undertaking that the launch was as fit for the purpose for which it was hired as reasonable care and skill could make it. The defendant was accordingly held liable.

36. *Blakemore v Bristol and Exeter Rly Co*, (1858) 8 El&Bl 1035, 1051: 120 ER 385.

37. Gratuitous bailor not liable for defects not known to him.

38. (1881) LR 6 QBD 685.

39. (1949) 1 KB 188.

Where a bailor delivers goods to another for carriage or for some other purpose, and if the goods are of dangerous nature, the fact should be disclosed to the bailee.<sup>40</sup>

### DUTIES OF BAILEE

The following are the duties of every bailee:

#### 1. Duty of reasonable care [Ss. 151–152]

Section 151 lays down this duty in the following terms:

**S. 151. Care to be taken by bailee.**—In all cases of bailment the bailee is bound to take as much care of the goods bailed to him as a man of ordinary prudence would, under similar circumstances take, of his own goods of the same bulk, quality and value as the goods bailed.

#### *Uniform standard of care*

The section lays down a uniform standard of care for “all cases of bailment”.<sup>41</sup> Originally in English law “liability in bailment was absolute. It was no excuse for the bailee to say that the damage or failure to return was due to no fault of his own; he was liable in any case”.<sup>42</sup> Thus, where goods were delivered to a bailee for safe custody and he was robbed of them, the court held him liable, saying, “it is a delivery which chargeth him to keep at his peril”.<sup>43</sup> The first concession was given to a gratuitous bailee. It was laid down in *R. v Viscount Hertford*<sup>44</sup> that “if money be given to one to keep generally without consideration and if the person be robbed, he is discharged”. Lord HOLT in *Coggs v Bernard*<sup>45</sup> further reduced the scope of absolute liability by confining it only to bailees “who exercised a public calling”, namely, public carriers and innkeepers.<sup>46</sup> Subsequently still by a judgment of Lord MANSFIELD absolute liability was confined to carriers only.<sup>47</sup> The rest of the bailees owe only the duty of reasonable care.<sup>48</sup>

40. *Lyell v Ganga Dai*, ILR (1875–80) 1 All 60, goods consigned without disclosing that they were combustible; *Great Northern Rly Co v L.E.P. Transport & Depository Ltd*, (1922) 2 KB 742 (CA); *Dwarkanath Raimohan Choudhuri v River Steam Navigation Co Ltd*, AIR 1917 PC 173.

41. Thus even a gratuitous or involuntary bailee is bound to bring into his duty the same amount of care as is prescribed by the section. *Wilson v Brett*, (1843) 11 M&W 113.

42. C.V. Davidge, *Bailment*, (1925) 41 LQR 433, 436.

43. *Southcot v Bennet*, 1601 Cro Eliz 815: 78 ER 1041.

44. (1681) Shower 172: 39 ER 870.

45. (1704) 2 Ld Raym 909.

46. About innkeepers (hotels, lodges and guest-houses) the general trend of decisions is that they are bailees liable only if the requisite standard of care is not observed. See *Rampal Singh v Murray & Co*, ILR (1897–1900) 22 All 164; before the Contract Act there were some decisions to the contrary effect. See *Whateley v Palanji*, (1866) 3 BHC (OC) 137. But now the opinion is different. *Jan and Son v A. Cameron*, ILR (1922) 44 All 735.

47. *Forward v Pittard*, (1785) 1 TR 27: 1 RR 142.

48. A carrier is permitted by the Carriers Act, 1865 to reduce his liability from an insurer to that of a bailee by a special contract with each consignee, but he cannot exclude his liability for negligence. *Irrawaddy Flotilla & Co Ltd v Bugwandass*, (1890–91) 18 IA 121: ILR (1891–92)

For the purpose of duty of care modern English law divides bailees into two kinds only, namely, gratuitous bailee and bailee for reward. A gratuitous bailee is liable for loss of, or damage to, goods only if he is guilty of gross negligence. "There is a certain degree of negligence to which everyone attaches great blame", and that may be called "gross negligence".<sup>49</sup> But the modern trend is towards a simple principle of liability for negligence in all cases.<sup>50</sup> *Blount v War Office*<sup>51</sup> shows this trend.

A house belonging to the plaintiff was requisitioned by the War Office. The plaintiff was allowed to store certain articles in a strong-room in the house, which he locked. Of the troops stationed there, who were not kept under proper control, some broke into the room and stole a quantity of silver plates.

The War Office was held liable. The court said: "There was a voluntary bailment of the goods to the defendants in the way of deposit and the standard of care required of them was reasonable care which a man would take of his own property. It is hard to believe that any reasonable man, who had valuable property of his own stored in those circumstances, would leave it to the tender mercies of seventy or eighty displaced persons of that type without taking any precaution. The Ministry was negligent."

This trend has been further confirmed by the Court of Appeal in *Houghland v R.R. Low (Luxury Coaches) Ltd.*<sup>52</sup>

The plaintiff was a passenger in one of the defendant's coaches. She had her suitcase put in the boot of the coach from where it was lost. The trial Judge found that this was technically a gratuitous bailment.

Even so it was held that the standard of care was that of reasonable care and was the same whether the bailment was gratuitous or for reward. ORMEROD LJ said: "The question that we have to consider in a case of this kind, if it is necessary to consider negligence; is whether in the circumstances of this particular case a sufficient standard of care has been observed by the defendants or their servants."

The standard of care expected of a paid bailee has been expressed in almost similar terms. This appears from *Martin v London County Council*.<sup>53</sup>

18 Cal 620 (PC); S. 93 of the Railways Act, 1989 charges the Railways with the responsibility of an insurer subject only to some defences and variations permitted by the Act. Carriers by Sea and Air are under similar responsibility. See, for further details, Avtar Singh, *LAW OF CARRIAGE* (3rd Edn, 1993); *Parasram v Air-India Ltd*, 1952 SCC OnLine Bom 144; *National Tobacco Co of India Ltd v Indian Airlines Corp*n, AIR 1961 Cal 383; *Rukmanand Ajitsaria v Airways India Ltd*, AIR 1960 Ass 71; *Indian Airlines Corp v Madhuri Chowdhuri*, AIR 1965 Cal 252; *Bombay Steam Navigation Co Ltd v Vasudev Baburao Kamat*, AIR 1928 Bom 5: ILR (1928) 52 Bom 37, *CARRIAGE OF GOODS BY SEA ACT*, 1925.

49. *Thomas Giblin v John Franklin McMullen*, (1869) LR 2 PC 317.

50. The Supreme Court of India has also pointed out that liability under Ss. 151–152 is one for negligence only. *Union of India v Amar Singh*, AIR 1960 SC 233: (1960) 2 SCR 75.

51. (1953) 1 WLR 736.

52. (1962) 1 QB 694 (CA).

53. 1947 KB 628.

The plaintiff was brought to a paid hospital as a patient. On her entry, the hospital officials took charge of two pieces of jewellery and a gold cigarette-case. They were subsequently stolen by a thief who broke into the room in which they were kept.

It was held that the defendants were bailees for reward and were liable for the loss as they had failed to exercise care which the nature and quality of the articles required.

In India, however, Section 151 prescribes a uniform standard of care in all cases of bailment, that is, a degree of care which a man of ordinary prudence would take of his own goods of the same type and under similar circumstances. If the care devoted by the bailee falls below this standard, he will be liable for loss of or damage to the goods:

**S. 152. Bailee when not liable for loss, etc, of thing bailed.**—The bailee, in the absence of any special contract, is not responsible for the loss, destruction or deterioration of the thing bailed, if he has taken the amount of care of it described in Section 151.

“No cast-iron standard can be laid down for the measure of care due from a bailee and the nature and amount of care must vary with the posture of each case.”<sup>54</sup> Nature, quality and bulk of the goods bailed, the purpose of bailment, facilities reasonably available for safe custody and the like, will be taken into account for determining whether proper care has been taken. Thus, where a part of the foodgrains stored at a bailee’s godown were damaged by floods unprecedented in the history of the place;<sup>55</sup> where a man hired a wooden shop and it was burnt by mobs during communal riots in the city,<sup>56</sup> the bailee in each case was held not liable as the loss was due to events beyond his control. Where on account of partition of the country a bank had to flee along with mass exodus from Pakistan to India, the bank was held to be not liable for goods bailed to it in Pakistan and which were thus lost there.<sup>57</sup>

#### *Loss by theft*

Where the bailor’s goods are stolen from the custody of the bailee, he will be liable if there has been negligence on his part. Where the plaintiff stayed at a hotel and his articles were stolen while he was away, the hotelier was held liable as the room was, to his knowledge, in an insecure condition.<sup>58</sup> Similarly, in another case, a bailee kept the bailor’s ornaments locked in a

54. *Shanti Lal v Tara Chand Madañ Gopal*, AIR 1933 All 158. As to the effect of circumstances see *Shiv Nath Rai Ram Dhari v Union of India*, AIR 1965 SC 1666.

55. *Union of India v Udhā Ram & Sons*, AIR 1963 SC 422: (1963) 2 SCR 702.

56. *Sunder Lal v Ram Swarup*, AIR 1952 All 205.

57. *Gopal Singh Hira Singh v Punjab National Bank*, AIR 1976 Del 115; *Pyramid Finance Ltd v Ramkrishna Iyer*, 2007 SCC OnLine Bom 1227: 2007 Cri LJ 1767, bailee held not liable for destruction of goods in an accidental fire.

58. *Jan and Son v A. Cameron*, ILR (1922) 44 All 735.

safe and kept the key in a cash-box in the same room. The room was situated on the ground floor and, being locked from outside, was easily accessible to burglars by removing the latch. The ornaments having been stolen, the bailee was held liable.<sup>59</sup> Where a banker was rendering the service of receiving goods on behalf of its account-holder and to hold them for the purpose of delivering them to the customers of the account-holder against payment, it was held by the Supreme Court that the position of the banker was that of the bailee and he was liable for the account-holder's loss inasmuch as the banker did not deliver goods to the customers from whom payment had been received. The court said:<sup>60</sup> "The banker-bailee, gratuitous or for reward, is bound to take the same care of the property entrusted to him as a reasonably prudent person and careful man may fairly be expected to take of his own property of the like description. In fact, a paid bailee must use the greatest possible care and is expected to employ all precautions in respect of the goods deposited with him. If the property is not delivered to the true owner, the banker cannot avoid his liability in conversion."

Applying these principles the court held that "the bank could not avoid the liability to return the goods as agreed upon or to pay an equivalent amount to the plaintiff. Even if we assume that the goods were delivered to a wrong person, the bank had to own up the liability to the plaintiff. The liability of banker to a customer in such a case is absolute even if no negligence is proved". In HALSBURY'S LAWS OF ENGLAND it is stated: "Where the bank delivers the goods to the wrong person, whereby they are lost to the owner, the liability of the bank is absolute, though there is no element of negligence, as where delivery is obtained by means of an artfully forged order. In law the banker could contract out of this liability, but he would be unlikely to do so in practice."<sup>61</sup>

#### *Burden of proof*

The burden of proof is on the bailee to show that he was exercising reasonable care and if he can prove this he will not be liable. If the bailee places before the court evidence to show that he had taken reasonable care to avoid damage which was reasonably foreseeable or had taken all reasonable precautions to obviate risks which were reasonably apprehended, he would be absolved of his liability.<sup>62</sup> Thus, where the railway administration was not

59. *Rampal Ramchand Agarwal v Gourishankar Hanuman Prasad*, AIR 1952 Nag 8. See *Lakhaji v Mahadeo*, AIR 1938 Bom 101. Failure to insure would not have made the bailee liable because ordinarily an owner also does not insure. *Bosech & Co v Maudlestan*, 1906 Punj Rec No 70.

60. *UCO Bank v Hem Chandra Sarkar*, (1990) 3 SCC 389, 396: AIR 1990 SC 1329.

61. Para 94, Vol 3, 4th Edn: *Lakshmi Narain Baijnath v Secy of State for India*, (1922-23) 27 CWN 1017, carrying goods in a boat with holes, obvious negligence.

62. *Kuttappa v State of Kerala*, (1988) 2 KLT 54. A Port Authority was held liable in the absence of proof that they took as much care of the goods landed at their port as satisfied the requirement of S. 151. They neither informed the consignee of the arrival of the goods nor made any serious effort to find out what had happened to the goods. *Chittagong Port Authority*

able to explain how the barge carrying the plaintiff's goods sank and was lost, negligence was presumed making the railway liable.<sup>63</sup> Where a jewellery box with declared contents was handed over to a bank under the clause which provided, "The articles in safe custody will be kept in the strong-room under joint custody of the manager or an officer duly authorised by the Head Office and the cashier", it was held that the bank was liable to account for the missing articles of jewellery and became liable because it failed to give any sufficient explanation for the loss. The depositor having died the recovery was sought by legal heirs through open delivery in court.<sup>64</sup> Where the bank took over possession of the hypothecated truck because of the borrower's default in repayment and neither disposed of it in accordance with the terms of the agreement nor took proper care of it leaving it in an open place, the extent to which the truck suffered loss of value because of the passage of time, the loan amount had to be reduced to that extent.<sup>65</sup> Where the plaintiff's car was lost in a fire occurring in a garage where it was delivered for repairs and the bailees did not lead any evidence to show as to how the incident took place, the Supreme Court held the bailees liable.<sup>66</sup> Where the goods were removed by the carrier's driver and attendant, it was held that the onus was on the carriers, as bailee, to prove that the loss was not caused by any fault of his or his agents. In the case before the court the carrier had failed to discharge the onus of proof and as such the court found

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v *Mohd. Ishaque*, (1983) 35 DLR (AD) 364 (Bangladesh SC). *Milap Carriers v National Insurance Co Ltd*, AIR 1994 AP 24, loss due to circumstances beyond control of carrier, there was also special contract exempting certain risks, the insurer who had to pay the claim was not allowed to recover indemnity from the carrier. *Hunt & Winterbotham (West of England) Ltd v B.R.S. (Parcels) Ltd*, (1962) 1 QB 617: (1962) 2 WLR 172, there is the following statement in this case: If an owner of goods leaves them with another person, who undertakes to mend them for reward, and then fails to produce them when they are wanted, it is a reasonable inference, in the absence of any explanation, that he was negligent.

63. *Union of India v Sugauli Sugar Works (P) Ltd*, (1976) 3 SCC 32. See also *Orient Paper Mills Ltd v Union of India*, AIR 1984 Ori 156 for responsibility of railways as bailees and the question of burden of proof. Loading was done in the private siding of the plaintiff and so burden upon him to prove the fact of loading; *Cochin Port Trust v Associated Cotton Traders*, AIR 1983 Ker 154, Port Trust not able to explain how fire commenced and destroyed bairl's goods, held, presumption of negligence. *SBI v Quality Bread Factory*, AIR 1983 P&H 244, goods lost from hypothecated godown on account of the negligence of bank officials, held, borrower's liability reduced to that extent. *Raman & Co v Union of India*, AIR 1985 Bom 37, since the liability of the Railways is that of bailee under Ss. 151–152, burden was on them to show how loss occurred and that it occurred after the first 7 days after the completion of the transit; *M. Veerabhadra Rao v Union of India*, (1985) 1 ATC 207 (AP), goods lost after seven days, the plaintiff came to receive the goods four months after their arrival, no liability. *Wilkinson v. Shields*, ILR (1887) 9 All 398, horse dying in the bailee's custody, burden on him to account for circumstances. *Trustees of Harbour, Madras v Best & Co*, ILR (1899) 22 Mad 524, goods lost from safe-custody, accountability.
64. *Jagdish Chandra Trikha v Punjab National Bank*, AIR 1998 Del 266. The suit filed within three years after obtaining letters of administration was held to be within time. Recovery of the value of the missing articles was allowed at the market price on the date of the suit with 12 per cent simple interest.
65. *Central Bank of India v Abdul Mujeeb Khan*, 1997 AIHC 299 (MP).
66. *N.R. Srinivasa Iyer v New India Assurance Co Ltd*, (1983) 3 SCC 458: AIR 1983 SC 899.

as a fact that the carrier was negligent in appointing a particular driver in the circumstances.<sup>67</sup> As against it, where certain engraving plates were gratuitously left with a bailee and they were lost and though he was not able to account for the manner of loss, he proved that the plates were kept in a proper place under the care of proper persons and in a proper arrangement. He was accordingly held not liable.<sup>68</sup>

#### *Loss due to act of bailee's servant*

Where the loss has been due to the act of the bailee's servant, he would be liable if the servant's act is within the scope of his employment. Explaining the principle in *Cheshire v Bailey*<sup>69</sup> COLLINS MR said: "The bailee is bound to bring reasonable care to the execution of every part of the duty accepted. He may perform that duty by servant or personally, and if he employs servants he is as much responsible for all acts done by them within the scope of their employment."

Thus in, *Sanderson v Collins*:<sup>70</sup>

The defendant sent his carriage to the plaintiff for repairs and the latter lent his own carriage to the defendant while the repairs were going on. The defendant's coachman, without his knowledge, took away the carriage for his own purpose and damaged it.

The defendant was held not liable as the coachman at the time when the injury was done to the carriage was not acting within the course of his employment. "If a burglar broke into the coach house and took away the carriage and caused damage to it and brought it back, no liability would attach to the bailee. The act of the servant was not different."<sup>71</sup>

Where, on the other hand, the bailee's driver left the vehicle in which he was carrying the plaintiff's goods unattended and half the goods were stolen, the bailee was held liable. The court also rejected the argument that the bailee had contracted with a forwarding agent and not with the plaintiffs, as the bailee knew that the goods belonged to the plaintiff.<sup>72</sup> The same result followed where the goods were stolen by the driver and attendant of the carrier's motor lorry.<sup>73</sup>

When the goods have been stolen from the bailee's custody, he should take reasonable steps to recover them.

67. *Rothmans of Pall Mall v Neo Kim*, (1989) 1 Curr LJ 59 (Kuala Lumpur).

68. *Bullen v Swan Electric Graving Co*, (1907) 23 TLR 258 (CA).

69. (1905) 1 KB 237 (CA).

70. (1904) 1 KB 628 (CA). *Bilaspur Central Coop Bank Ltd v State of M.P.*, AIR 1959 MP 77.

71. *Cheshire v Bailey*, (1905) 1 KB 237 (CA); *Thomas Giblin v John Franklin McMullen*, (1869) LR 2 PC 317; *Searle v Laverick*, (1874) LR 9 QB 122, damage caused by collapse of a roof owing to high winds, bailee not liable. *South Eastern Carriers (P) Ltd v Mohd Sarvar*, 1996 AIHC 2988 (AP), the driver of the lorry along with his employer held liable for short delivery for which the driver was responsible.

72. *Lee Cooper Ltd v C.H. Jeakins & Sons Ltd*, (1967) 2 QB 1; (1965) 3 WLR 753.

73. *Rothmans of Pall Mall v Neo Kim*, (1989) 1 Curr LJ 59 (Kuala Lumpur)..

A farmer accepted certain cattle for adjustment. Some of them were stolen without his default, but he made no efforts whether by informing the owner or the police to recover them.<sup>74</sup>

He was held liable. He should have used reasonable diligence to recover them and he could discharge himself only by showing that such diligence would have been unavailing.

#### *Bailee's own goods lost with those of bailor*

Where the bailee's own goods are lost along with those of the bailor, the bailee would naturally contend that he was taking as much care of the bailor's goods as he did of his own.<sup>75</sup> But this would not be the deciding factor. The fact that the bailee is generally negligent with his own goods is no justification for his negligence towards the bailor's goods,<sup>76</sup> unless the bailor is aware of his habits and, therefore, knew what to expect. Even in such cases the proper inquiry is whether reasonable care has been taken. Thus, where a general merchant going to consign his parcel for export, took, out of voluntary courtesy, his friend's parcel for similar consignment and entered both the parcels under a wrong heading, and, consequently, both were seized and lost. He was held not liable as he had in good faith taken equal care of both the parcels.<sup>77</sup>

#### **Misdelivery by Railway**

Goods were delivered to an unauthorised person on production of an indemnity bond which turned out to be bogus. Railway administration was not able to show what was the date of arrival of goods and of termination of transit for the purpose of showing that neither the consignor nor the consignee had claimed the goods within a week of their arrival. Thus there was nothing to exonerate the railway administration of its liability.<sup>78</sup>

#### *Goods carried at owner's risk*

The goods carried by a road carrier were insured and were also being carried at "owner's risk". They were damaged by rash and negligent driving causing accident. It was held that "owner's risk" cannot protect a carrier from the consequences of his own negligence or negligence of his agents.

74. *Coldman v Hill*, (1919) 1 KB 443 (CA).

75. *Calcutta Credit Corpn v Prince Peter*, AIR 1964 Cal 374.

76. *Lakshmidas v Megh Raj*, 1900 Punj Rec No 90, p. 371.

77. *Sheills v Blackburne*, (1789) 1 HBL 158.

78. *P.M.S Traders v Jaitex Lungi Co*, AIR 2007 NOC 1564 (Mad), S. 77(2) of the Railways Act, 1890. *Union of India v Halasidharth Sahakari Sakhar Karkhana Ltd*, AIR 2011 Gau 78, original railway receipt was lying with the bank, railways requested not to deliver the consignment except on production of the original R/R or indemnity bond, liability incurred to the consignor for loss of the consignment because delivery happened to be made without complying with the request.

“Owner’s risk” cannot be regarded as a licence or liberty clause from the duty of reasonable care.<sup>79</sup>

### Involuntary bailee

“A person who has come into possession of a chattel through no act of his own and without his consent” is called an involuntary bailee. An early illustration is to be found in the facts of *Howard v Harris*:<sup>80</sup>

The author of a play, without being asked, sent his manuscript to a theatre operator, who lost it.

The court held “that no duty of any kind was cast on the defendant by receipt of something he had not asked for”. Subsequent decisions, however, do not support this view of the situation. And this is amply shown by *Newman v Bourne & Hollingsworth*.<sup>81</sup>

The plaintiff went to the defendant’s shop to buy a coat. She was wearing a coat fastened with a diamond brooch, and she took the coat off, and put it on a glass case with the brooch by the side of it. When leaving she forgot the brooch and it was handed by an assistant to the shopwalker who put it in his desk, from where it was lost.

The defendant was held liable. “He had not exercised that degree of care which was due from one who had found an article and had assumed possession of it. The degree of negligence must be measured by the apparent value of the article.”

But if an involuntary bailee, without negligence, does something which results in the loss of the property, he will not be liable for conversion. This has been laid down in *Elwin & Powell Ltd v Plummer Raddis Ltd*.<sup>82</sup>

A man came to the plaintiff’s warehouse, and ordered to buy £350 worth of coats. He said he wanted them to be sent to the Brighton Branch of P&E Ltd, which was done. Subsequently he sent a telegram to P&E saying: “Goods sent to your branch by error. Sending van to collect.” The defendants, believing in good faith in the error theory, allowed him to have the goods.

The plaintiff’s action against them for conversion failed.

### Contract to the contrary

It is still debatable whether a bailee can contract himself out of the duty prescribed by Section 151, or whether a contract of bailment can exempt the bailee from his liability for negligence? The argument is built chiefly on

79. *Sirmour Truck Operators Union v National Insurance Co Ltd*, AIR 2011 NOC 389 (HP).

80. (1884) 1 C&E 253, any such report being not available, the facts have been collected from CHITTY ON CONTRACTS (22nd Edn, 1961), Vol 2, 161.

81. (1951) 31 TLR 209.

82. (1933) 50 TLR 158. See H.W. Burnett, *Conversion by Involuntary Bailee*, (1960) 75 LQR 364.

the ground that Section 152 opens with the remark: "in the absence of any special contract". This may show that the legislative intent was to permit him to reduce the scope of his liability. Judicial thinking on this line is in evidence in a Punjab and Haryana decision.<sup>83</sup> The court said that the words "in the absence of special contract" as used in Section 152 show that a bailee can contract himself out of the obligation under Section 151. The court cited the following observation from a Bombay decision: "This court in *Bombay Steam Navigation Co Ltd v Vasudev Baburao Kamat*<sup>84</sup> held that it was open to a bailee to contract himself out of the obligation imposed by Section 151. The Act does not expressly prohibit contracting out of Section 151 and it could be a startling thing to say that persons *sui juris* are not at liberty to enter into such a contract of bailment as they may think fit. Contracts of bailment are very common although they are not always called by their technical name. There is no reason why a man should not be at liberty to agree to keep property belonging to a friend on the terms that such property is to be entirely at the risk of the consumer and that the man who keeps it is to be under no liability for the negligence of his servants in failing to look after it."

It is submitted with respect that this seems to be an unnatural reading of the two sections. Section 151 prescribes the minimum standard of care expected of a bailee and Section 152 has the effect of saying that unless the standard of care is enhanced by special contract, the bailee will be liable only when he fails to observe the requirement of Section 151. The words in Section 152 "in the absence of any special contract" would permit the standard of duty to be revised upwards and not to be diluted. Apart from this, it has always been held that it is unfair and unreasonable for any person to say that he would not be liable for negligence. No one can get a licence to be negligent. Thus in a Gujarat case bales of cloth were lost from bank custody under circumstances showing negligence. The banker was held liable irrespective of a clause which absolved him of all liability.<sup>85</sup> The clause in question was that the bank will be absolved from all liability for shortage of goods by way of pilferage, stealth or removal from the godown in any manner. Even this could not protect the bank because it was against the meaning and intent of the minimum standard prescribed by Section 151. The Kerala High Court also adopted this line of reasoning.<sup>86</sup> The court held: "Where the goods are entrusted with the Port Trust, their duty is certainly

83. *SBI v Quality Bread Factory*, AIR 1983 P&H 244.

84. AIR 1928 Bom 5: ILR (1928) 52 Bom 37.

85. *Mahendra Kumar Chandulal v C.B.I.*, AIR 1984 Guj (NOC) 53: (1984) 1 Guj LR 237. See further *Chittagong Port Authority v Mohd Ishaque*, (1983) 35 DLR (AD) 364, where the Chittagong Port Act was under consideration and that Act had dropped the words "in the special contract" and retained only the rest of the contents of S. 152. It was held that the goods delivered by a ship to the port constitutes the port into a bailee of the consignee; *Sheikh Mahamed v British Indian Steam Navigation Co*, (1908) 32 Mad 95; *Raipur Transport Co v Ghanshyam*, AIR 1956 Nag 145.

86. *United India Insurance Co Ltd v Pooppally Coir Mills*, (1994) 2 Ker LT 473.

in the nature of a bailee's duty and they are expected to take reasonable care. [They] cannot claim a total exemption from the standard of care to be taken by a bailee by taking recourse to the provision contained in Section 121 of the Major Ports Trust Act, 1963 (protection from liability for acts done in good faith). A Division Bench of this court had occasion to consider in *Cochin Port Trust v Associated Cotton Traders Ltd*<sup>87</sup> the nature of the duty of the Cochin Port Trust towards the owner of the goods. In this case also the goods were destroyed in a fire which broke out in the godown of the Port Trust. The court held that the Port Trust which is in the position of a bailee has a duty to take all proper measures for protection of the goods. When goods entrusted to a bailee are lost or damaged, there is initial presumption of negligence (failure to take care) on the part of the bailee. Onus of proof is on the bailee to show that he had taken necessary precautions and care required under law. The bailee alone will be in a position to explain the cause of fire. It is a fact specially within his knowledge and, therefore, under Section 106 of the Evidence Act, 1872, the burden of proving that fact will be upon him.”<sup>88</sup>

Delivery of goods to Railways for purpose of carriage is under a special contract because, in addition to it being an ordinary contract of bailment, the provisions of the Railways Act<sup>89</sup> also apply. The Bombay High Court faced a problem on this point in a case<sup>90</sup> involving consignment of certain bales of cloth to be carried in brake van and on arrival at the destination one of the bales being tampered with resulting in short delivery to the extent of 33 kg. The Railways escaped liability because the value of the goods was not declared as required by the relevant section of the Railways Act.<sup>91</sup>

As ordinary bailees Railways too are bound by the duty imposed by Section 151. The Railways were held liable where, instead of keeping the goods in their own godown, they left them at the jetty of a port and they were destroyed by fire.<sup>92</sup> Liability came to railways when the goods they were carrying in a wagon were damaged due to percolation of rain water into the wagon.<sup>93</sup>

A contract of bailment provided that the bailee would not be liable for loss or damage due to causes beyond his control. It was held that this would

87. 1983 Ker LT 562.

88. See also *R.S. Deboo v M.V. Hindlekar*, AIR 1995 Bom 68, laundry receipt carried printed term of liability up to 20 per cent of charges or half the value of the garment, whichever was less, held, unreasonable. The court said that liability under S. 151 could not be diluted.

89. No 1 of 1890, S. 77-B(1) in this case. Now S. 93 of the new Railways Act of 1989.

90. *Jugalkishore Pannalal Darak v Union of India*, AIR 1988 Bom 377.

91. S. 77-B(1) of the old Railways Act. The new Act of 1989 does not carry any list of articles of special value.

92. *Union of India v Hafiz Bashir*, 1987 Supp SCC 174. The liability of a carrier is regulated by the Carriers Act, 1865 and that of the Railways by the Railways Act, 1989. There are similar provisions in these Acts and, therefore, barring a few exceptions stated therein, the liability is absolute, see *Shah Jugaldas Amritlal v Shah Hiralal Talakchand*, AIR 1986 Guj 88.

93. *Union of India v Hari Shanker Gauri Shanker*, 2005 All LJ 2200 (All), S. 77 of the Railways Act, 1890.

not include shortage in the weight of the goods.<sup>94</sup> The court said that the words “any other cause whatsoever” would also not cover shortage of which no cause is shown. The bank officers were negligent in taking count and weight of the handles and cotton strips. Such irresponsibility could not be described as a cause. The word “cause” had to be interpreted as other causes akin to those mentioned in the clause.

## 2. Duty not to make unauthorised use [S. 154]

**S. 154. Liability of bailee making unauthorised use of goods bailed.**—If the bailee makes any use of the goods bailed which is not according to the conditions of the bailment, he is liable to make compensation to the bailor for any damage arising to the goods from or during such use of them.

### *Illustrations*

- (a) *A* lends a horse to *B* for his own riding only. *B* allows *C*, a member of his family, to ride the horse, *C* rides with care, but the horse accidentally falls and is injured. *B* is liable to make compensation to *A* for the injury done to the horse.
- (b) *A* hires a horse in Calcutta from *B* expressly to march to Benares. *A* rides with due care, but marches to Cuttack instead. The horse accidentally falls and is injured. *A* is liable to make compensation to *B* for the injury to the horse.

Goods must be used by the bailee strictly for the purpose for which they have been bailed to him. Any unauthorised use of the goods would make the bailee absolutely liable for any loss of or damage to the goods. Even an act of God or inevitable accident would be no defence. A horse lent for riding should not be used for any other purpose and if it is used outside the scope of the bailment, the bailee would be liable for any damage to the horse howsoever happening. Apart from this, the bailor may terminate the contract at once and insist on the goods being returned to him. This is so provided in Section 153.

Where a vehicle was delivered to a workshop for repair and the owner of the workshop allowed an unlicensed employee to drive the vehicle and he caused an accident resulting in the death of a person, it was held that the bailee was liable to compensate the deceased as also the owner of the vehicle because it was an unauthorised use of the vehicle and the liability was absolute. The insurer was also liable to pay compensation to the deceased and recover indemnity from the vehicle owner.<sup>95</sup>

**S. 153. Termination of bailment by bailee's act inconsistent with conditions.**—A contract of bailment is avoidable at the option of the bailor, if the bailee does any act with regard to the goods bailed, inconsistent with the conditions of the bailment.

### *Illustration*

*A* lets to *B*, for hire, a horse for his own riding. *B* drives the horse in his carriage. This is, at the option of *A*, a termination of the bailment.

94. *Balwantlal Chhabildas Mehta v State Bank of Saurashtra*, (1998) 4 GCD 3112.

95. *Alias v E.M. Patil*, AIR 2004 Ker 214.

### 3. Duty not to mix [Ss. 155–157]

The bailee should maintain the separate identity of the bailor's goods. He should not mix his own goods with those of the bailor and without his consent. If the goods are mixed with the consent of the bailor, both will have a proportionate interest in the mixture thus produced. [S. 155] If the mixture is made without bailor's consent, and if the goods can be separated, or divided, the bailee is bound to bear the expenses of separation as well as any damage arising from the mixture. [S. 156] But if the mixture is beyond separation, the bailee must compensate the bailor for his loss. Sections 155 to 157 run as follows:

**S. 155. Effect of mixture, with bailor's consent, of his goods with bailee's.**—If the bailee, with the consent of the bailor, mixes the goods of the bailor with his own goods, the bailor and the bailee shall have an interest, in proportion to their respective shares, in the mixture thus produced.

**S. 156. Effect of mixture, without bailor's consent when the goods can be separated.**—If the bailee, without the consent of the bailor, mixes the goods of the bailor with his own goods, and the goods can be separated or divided, the property in the goods remains in the parties respectively; but the bailee is bound to bear the expense of separation or division, and any damage arising from the mixture.

#### *Illustration*

A bails 100 bales of cotton marked with a particular mark to B. B without A's consent, mixes the 100 bales with other bales of his own, bearing a different mark; A is entitled to have his 100 bales returned, and B is bound to bear all the expenses incurred in the separation of the bales, and any other incidental damage.

**S. 157. Effect of mixture, without bailor's consent, when the goods cannot be separated.**—If the bailee, without the consent of the bailor, mixes the goods of the bailor with his own goods, in such a manner that it is impossible to separate the goods bailed from the other goods, and deliver them back, the bailor is entitled to be compensated by the bailee for the loss of the goods.

#### *Illustration*

A bails a barrel of Cape flour worth Rs 45 to B. B, without A's consent, mixes the flour with country flour of his own, worth only Rs 25 a barrel. B must compensate A for the loss of his flour.

### 4. Duty to return [Ss. 160–161]

Section 160 provides for the duty to return.

**S. 160. Return of goods bailed, on expiration of time or accomplishment of purpose.**—It is the duty of the bailee to return, or deliver according to the bailor's directions, the goods bailed, without demand, as soon as the time for which they were bailed has expired, or the purpose for which they were bailed has been accomplished.

**S. 161. Bailee's responsibility when goods are not duly returned.**—If, by the default of the bailee, the goods are not returned, delivered or tendered at the proper time, he is responsible to the bailor for any loss, destruction or deterioration of the goods from that time.

When the purpose of bailment is accomplished or the time for which the goods were bailed has expired, the bailee should return the goods to the bailor without demand.<sup>96</sup> If he fails to do so, he will keep the goods at his risk and will be responsible for any loss of or damage to the goods arising howsoever. For example, in *Shaw & Co v Symmons & Sons*:<sup>97</sup>



CASE PILOT

The plaintiff entrusted books to the defendant, a bookbinder, to be bound, the latter promising to return them within a reasonable time. The plaintiff having required the defendant to deliver the whole of the books then bound, the defendant failed to deliver them within a reasonable time and they were subsequently burnt in an accidental fire on his premises.

The defendant was held liable in damages for the loss of the books. When the loss takes place while the bailee's wrongful act is in operation, there is no question of any defence like "act of God" or "inevitable accident" being set up. He is liable in any case.<sup>98</sup>

Similarly, where a pawnee refused to return the goods even after the tender of the debt by the pawnner, and the goods, having been subsequently stolen, he was held liable.<sup>99</sup>

### *Termination of gratuitous bailment*

Where the lending of the goods is gratuitous, the bailor may at any time require return of the goods even though he lent them for a specified time or purpose. But if the bailee has acted on the faith of the loan made for a specified time or purpose in such manner that if the goods are demanded back before the agreed time, the bailee's loss would be greater than the benefits derived, the bailor must, if he compels the return, indemnify the bailee

96. He can be sued for detinue. *Dhian Singh Sobha Singh v Union of India*, AIR 1958 SC 274: 1958 SCR 781; *Bhatinda Chemicals Ltd v M V "X Press Nuptse"*, AIR 2006 Bom 311, no privity of contract between the claimant and the person who was alleged to have defaulted in returning the goods.

97. (1917) 1 KB 799.

98. But see *Prakash Road Lines (P) Ltd v Oriental Fire and General Insurance Co*, (1988) 1 TAC 263: (1988) 1 Kant LJ 118, failure to perform the obligation of a bailee makes the bailee liable except when the loss is due to act of God or *force majeure*. Where the goods are not fit for the purposes of bailment, the bailee has only to inform the bailor and not actually to return them. *Isuffalli v Ibrahim*, 1920 SCC OnLine Bom 93: AIR 1921 Bom 191 (1).

99. *Rampal Ramchand Agarwal v Gourishankar Hanuman Prasad*, AIR 1952 Nag 8. See also *Dhian Singh Sobha Singh v Union of India*, AIR 1958 SC 274: 1958 SCR 781. Failure to account for the goods amounts to failure to deliver and, therefore, attracts the absolute liability of the section. *Chittagong Port Authority v Mohd. Ishaque*, (1983) 35 DLR (AD) 364 (Bangladesh SC). *Dinesh V. Pai v Naval Academy, Kochi*, AIR 2003 Ker 280, excavator taken on hire for site work. There could be no justification for not returning the machine to the owner.

for the amount in which the loss occasioned exceeds the benefits derived. Section 159 is as follows:

**S. 159. Restoration of goods lent gratuitously.**—The lender of a thing for use may at any time require its return, if the loan was gratuitous, even though he lent it for a specified time or purpose. But, if, on the faith of such loan made for a specified time or purpose, the borrower has acted in such a manner that the return of the thing lent before the time agreed upon would cause him loss exceeding the benefit actually derived by him from the loan, the lender must, if he compels the return, indemnify the borrower for the amount in which the loss so occasioned exceeds the benefit so derived.

A gratuitous bailment is also terminated by the death either of the bailor or of the bailee. Section 162 is as follows:

**S. 162. Termination of gratuitous bailment by death.**—A gratuitous bailment is terminated by the death either of the bailor or of the bailee.

#### Bailment by joint owners [S. 165]

**S. 165. Bailment by several joint owners.**—If several joint owners of goods bail them the bailee may deliver them back to, or according to the directions of, one joint owner without the consent of all, in the absence of any agreement to the contrary.

#### 5. Duty not to set up “jus tertii”

A bailee is not entitled to set up, as against the bailor's demand, the defence of *jus tertii*, that is to say, that the goods belong to a third person.<sup>100</sup> The bailee is estopped from denying the right of the bailor to bail the goods and to receive them back.<sup>101</sup> Where the goods were returned to the warehouse keeper who had pledged them without the authority of the owner and the pledgee did not know this fact, the pledgee was held to be not liable to the true owner.<sup>102</sup> Even if there is a person who has a better title to the goods than that of the bailor or who claims ownership of the goods, the bailee may safely return the goods to the bailor and he will not be liable to the owner for conversion.

**S. 166. Bailee not responsible on re-delivery to bailor without title.**—If the bailor has no title to the goods, and the bailee, in good faith, delivers them back to, or according to the directions of the bailor, the bailee is not responsible to the owner in respect of such delivery.

100. This is called the estoppel of bailee. He can return the goods to the person bailing them even against the demands of the true owner unless he is under legal pressure. *Rogers Sons & Co v Lambert & Co*, (1891) 1 QB 318, 325 (CA).

101. S. 117 of the Indian Evidence Act (Act 1 of 1872). Where the goods have been seized by the Government, liability under this section does not arise. *Juggilal Kamlapat Oil Mills v Union of India*, (1976) 1 SCC 893: AIR 1976 SC 227.

102. *Bank of Bombay v Nandlal Thackerseydass*, ILR (1912–13) 40 IA 1: ILR (1913) 37 Bom 122.

But the person who claims the ownership may apply to the court to prevent the bailee from returning the goods to the bailor and to have the question of title decided.<sup>103</sup>

**S. 167. Right of third person claiming goods bailed.**—If a person, other than the bailor, claims goods bailed, he may apply to the Court to stop the delivery of the goods to the bailor, and to decide the title to the goods.

Further, if the bailee has already delivered the goods to the person having a better title, and yet the bailor sues him, he may prove that such person had a better right to receive the goods as against the bailor.<sup>104</sup> In a case before the Supreme Court:<sup>105</sup>

Oil was consigned with the Railways from Kanpur to Calcutta. It reached Calcutta intact. The sender, however, instructed the Railways to bring it back to Kanpur. Before the formalities for the same could be complied with, the oil was seized by a food inspector, who found it adulterated and had it destroyed under the order of the High Court.

Holding the Railways not liable, the court said that a bailee is excused from returning the subject-matter of the bailment to the bailor where it was taken away from him by an authority of law.

Where goods have been bailed by several joint owners, the bailee may deliver them back to one joint owner without the consent of all, in the absence of any agreement to the contrary. [S. 165]

### Transfer of shipping documents

Where the bill of lading, under which delivery of the cargo was effected to the carrier, was transferred by the shipper, it was held that the right to file a suit under the contract of carriage became transferred to the bank when it became the holder of the bill of lading under a transfer by the shipper. Even if the transfer was by the principal to its agent, the principal could not claim the right to sue. But even so the original contract of bailment would continue to exist subject only to the rights created under the transfer and subject also to the terms and conditions of the bill of lading. To that extent the original shipper could sue the carriers for their failure to deliver goods to the party entitled to them at the destination.<sup>106</sup>

### 6. Duty to return increase [S. 163]

In the absence of any agreement to the contrary, the bailee is bound to return to the bailor natural increases or profits accruing to the goods during

103. *Rogers Sons & Co v Lambert & Co*, (1891) 1 QB 318 (CA).

104. Explanation (2) to S. 117 of the Indian Evidence Act, 1872.

105. *Juggilal Kamlapat Oil Mills v Union of India*, (1976) 1 SCC 893: AIR 1976 SC 227.

106. *East West Corpn v DKBS AF* 1912 A/S, 2003 QB 1509 (CA).

the period of bailment.<sup>107</sup> This is so provided in Section 163, which is as follows:

**S. 163. Bailor entitled to increase or profit from goods bailed.**—In the absence of any contract to the contrary, the bailee is bound to deliver to the bailor, or according to his directions, any increase or profit which may have accrued from the goods bailed.

*Illustration*

A leaves a cow in the custody of B to be taken care of. The cow has a calf. B is bound to deliver the calf as well as the cow to A.

Where shares and securities were pledged with a bank and the bank received bonus shares and dividends and interest in respect thereof, it was held that the bank could not be compelled to handover such increment unless the pledged securities were redeemed.<sup>108</sup>

**FINDER [SS. 168–169]**

**S. 168. Right of finder of goods: May sue for specific reward offered.**—The finder of goods has no right to sue the owner for compensation for trouble and expense voluntarily incurred by him to preserve the goods and to find out the owner; but he may retain the goods against the owner until he receives such compensation; and where the owner has offered a specific reward for the return of goods lost, the finder may sue for such reward, and may retain the goods until he receives it.

**S. 169. When finder of thing commonly on sale may sell it.**—When a thing which is commonly the subject of sale is lost, if the owner cannot with reasonable diligence be found, or if he refuses, upon demand, to pay the lawful charges of the finder, the finder may sell it—

- (1) when the thing is in danger of perishing or of losing the greater part of its value, or
- (2) when the lawful charges of the finder, in respect of the thing found, amount to two-thirds of its value.

**Finders are bailees**

A finder of goods is a bailee thereof and as such bound by the duty of reasonable care.<sup>109</sup> He does not have the right to sue the owner for compensation for trouble and expense voluntarily incurred by him to preserve the goods and to find out the owner. [S. 168] Early English cases disallowed not only any compensation, but also right to lien for expenses. Thus where:

A finder fed a dog for 20 weeks and claimed 20s. for the same.<sup>110</sup>

107. Where, for example, bonus shares are allotted in respect of the shares during the period of their pledge, the increment has to be returned on redemption of the pledge. *Motilal Hirabhai v Bai Mani*, (1924–25) 52 IA 137.

108. *Standard Chartered Bank v Custodian*, (2000) 6 SCC 427: AIR 2000 SC 1488.

109. He is under no higher duty than that. *Isaack v Clark*, (1615) 2 Bulstr 306.

110. *Binstead v Buck*, (1776) 2 Wm Bl 117: 96 ER 660.

The court said he would be guilty of trover if he refused to deliver unless paid for his keeping. Similarly, in another case:<sup>111</sup>

A quantity of timber, placed in a dock on the bank of a navigable river, being accidentally loosened, was carried by the tide to a considerable distance. The defendant, finding it in that situation, voluntarily conveyed it to a place of safety.

He was held not entitled to lien on the timber for the trouble or expense, but was liable in trover for refusing to deliver.

### Finder's rights

Sections 168 and 169, however, protect the interest of a finder in two ways. Section 168 allows the finder to retain the goods against the owner until he receives compensation for trouble and expense. Further, where the owner has offered a specific reward for the return of the goods lost, the finder may sue for such reward, and may retain the goods until he receives it.

Section 169 allows the finder to sell the goods in certain circumstances. Where the thing found is commonly the subject of sale and if the owner cannot be found with reasonable diligence, or if he refuses to pay the lawful charges of the finder, the finder may sell the goods in the following cases:

- (1) when the thing is in danger of perishing or of losing greater part of its value, or
- (2) when the lawful charges of the finder, in respect of the thing found, amount to two-thirds of its value.

## RIGHTS OF BAILEE

### 1. Right to compensation [S. 164]

**S. 164. Bailor's responsibility to bailee.**—The bailor is responsible to the bailee for any loss which the bailee may sustain by reason that the bailor was not entitled to make the bailment, or to receive back the goods, or to give directions respecting them.

If the bailor has no right to bail the goods, or to receive them back or to give directions respecting them and consequently the bailee is exposed to some loss, the bailor is responsible for the same.

### 2. Right to expenses or remuneration [S. 158]

**S. 158. Repayment by bailor of necessary expenses.**—Where, by the conditions of the bailment, the goods are to be kept or to be carried, or to have work done upon them by the bailee for the bailor, and the bailee is to receive no remuneration, the bailor shall repay to the bailee the necessary expenses incurred by him for the purpose of the bailment.

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111. *Nicholson v Chapman*, (1793) 2 Hy Bl 254.

A bailee is entitled to recover his agreed charges. But where there is no such agreement at all, Section 158 comes into play. The section says that where the bailee is required by the terms of bailment to keep or carry the goods or to do some work upon them for the benefit of the bailor, and the contract provides for no reward, the bailee has a right to ask the bailor for payment of necessary expenses incurred by him for the purpose of the bailment. The American law is also the same.

Where the bailment is gratuitous and the bailee is in no way benefited, the bailor has to bear the expenses, if any, of the bailee for keeping the chattel. It is akin to the lien of a warehouseman for claiming charges for the preservation of the goods.<sup>112</sup>

The Calcutta High Court has laid down that this right is not linked with the right of lien. Lien can be exercised only as long as possession is retained whereas the right to charges remains alive even when possession has been parted with. In this case the State Trading Corporation had hired the plaintiff's storage tank for storing its oil. On account of a dispute, the STC appointed a special officer who took charge of the tank and delivered its contents to others as directed. The plaintiff thus lost possession of the oil and with it his lien, but his right to charges for protection and storage of the oil survived. The court said that the bailor had enjoyed the benefit of the bailee's services.<sup>113</sup>

Where the bailment is for the benefit of the bailee, there, in reference to expenses, the following two propositions apply:

If in using the thing, the borrower is put to any expense, this must be borne by himself. Thus, for example, if a horse is lent to a friend for a journey, he must bear expenses of his food during that journey, and to getting him shod, if he should chance to require it, for it is a burden which is naturally attendant upon the use of the horse.

"The borrower is compellable to bear the ordinary expenses; for the loan being for his benefit he must be presumed to engage to bear the burden as an incident to the use."<sup>114</sup>

### 3. Right of lien [Ss. 170-171]

If the bailee's lawful charges are not paid he may retain the goods. The right to retain any property until the charges due in respect of the property are paid, is called the right of lien. The Supreme Court<sup>115</sup> cited the following

112. WILLINGTON ON CONTRACTS as cited in Ramachandran, THE LAW OF CONTRACT IN INDIA (Vol III) 2266.

113. *Surya Investment Co v State Trading Corp of India (P) Ltd*, AIR 1987 Cal 46; *Forbes Forbes Campbell & Co Ltd v Port of Bombay*, AIR 2006 Bom 162, consignee of goods did not turn up, the steamer agent did not arrange for taking delivery. Port Trust was allowed to recover demurrage charges and other charges from the steamer agent.

114. STORY ON BAILEMENTS, Ss. 256 and 273.

115. *Syndicate Bank v Vijay Kumar*, (1992) 2 SCC 330: AIR 1992 SC 1066, 1068. See also *V.S. Prabhu v R.D. Mujumdar*, (1993) 2 Kant LJ 1, the bailee cannot be deprived of his possession

passage from HALSBURY'S LAWS OF ENGLAND<sup>116</sup> as to the nature of this right:

"Lien is in its primary sense a right in one man to retain that which is in his possession belonging to another until certain demands of the person in possession are satisfied. In this primary sense it is given by law and not by contract."

Liens are of two kinds; namely: (1) particular lien, and (2) general lien.

### Particular lien [S. 170]

As a general rule a bailee is entitled only to particular lien, which means the right to retain only that particular property in respect of which the charge is due. This right is provided for in Section 170 of the Act.

**S. 170. Bailee's particular lien.**—Where the bailee has, in accordance with the purpose of the bailment, rendered any service involving the exercise of labour or skill in respect of the goods bailed, he has, in the absence of a contract to the contrary, a right to retain such goods until he receives due remuneration for the services he has rendered in respect of them.

#### *Illustrations*

- (a) A delivers a rough diamond to B, a jeweller, to be cut and polished, which is accordingly done. B is entitled to retain the stone till he is paid for the services he has rendered.
- (b) A gives cloth to B, a tailor, to make into a coat. B promises A to deliver the coat as soon as it is finished, and to give a three months' credit for the price. B is not entitled to retain the coat until he is paid.

#### *Exercise of labour or skill*

Thus the right is available subject to certain important conditions. The foremost among them is that the bailee must have rendered some service involving the exercise of labour or skill in respect of the goods bailed.<sup>117</sup> Further, it has been frequently pointed out that the labour or skill exercised by the bailee must be such as improves the goods. "There is no authority for the proposition that if what the contractor does is not to improve the article, but merely to maintain it in its former condition, he gets a lien for the amount spent upon it for that maintenance. A job master has no lien at all for the amount of his bill in respect of feeding and keeping a horse at his stable, whereas a trainer does get a lien upon a horse for the improvements which he effects to the horse."<sup>118</sup>

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for any superior claim. He has to be paid first. Where goods were taken away from bailee under court order, his lien survived and applied to the sale proceeds of the goods for his payment.

116. Vol 20 (2nd Edn) 552, para 695.

117. It was observed by BEST CJ in *Bevan v Waters*, (1828) 3 C & P 520 that if a man has an article delivered to him, on the improvement of which he has to bestow trouble and expense, he has a right to detain it until his demand is paid.

118. *Hutton v Car Maintenance Co*, (1915) 1 Ch 21.

Similarly, it has been observed in another case that “where a bailee has expended his labour and skill in the improvement of a chattel delivered to him, he has lien for his charge in that respect. Thus, the artificer to whom the goods are delivered for the purpose of being worked up into form, or the farrier by whose skill the animal is cured of a disease, or the horse-breaker by whose skill he is rendered manageable, have liens on the chattels in respect of their charges”.<sup>119</sup> In *Hutton v Car Maintenance Co.*<sup>120</sup>

The owner of a motor car gave it to a company to maintain it for three years on a fixed annual payment. An amount having become due for maintenance charges, the company claimed lien on the car.



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It was held that inasmuch as what the company did was not to improve the car, but only to maintain it in its former condition, the company had no lien on the car. Similarly, where a bailee claimed lien for storage of sugar, it was held that such custody, not being a service involving the exercise of labour or skill within the meaning of Section 170, the bailee was not entitled to lien.<sup>121</sup> On the same reasoning, a person to whom cattle are given for grazing does not have the right of lien on them for his charges.<sup>122</sup>

#### *In accordance with contract*

Secondly, the labour or skill must have been exercised in accordance with the purpose of the bailment and the terms of the contract.<sup>123</sup>

#### *Goods on which labour or skill bestowed*

Thirdly, only such goods can be retained on which the bailee has bestowed trouble and expense. He cannot retain any other goods belonging to the bailor which are in his custody.<sup>124</sup> It is this element of “particular lien” which distinguishes it from “general lien”.

**POSSESSORY RIGHT.**—Lastly, the right depends on possession and is lost as soon as possession of the goods is lost. In a case before the Nagpur High Court:<sup>125</sup>

The plaintiff purchased an old refrigerator, the vendor agreeing to repair it for a fixed charge. When the repair was over and the condition of the machine was found satisfactory, it was delivered to the plaintiff but a part of the repair money was still unpaid. The machine broke down again and the vendor carried its engine and another part for further repairs and

119. PARKE B in *Scarfe v Morgan*, (1838) 4 M&C 270, 283: 150 ER 1430: 51 RR 568, 578.

120. (1915) 1 Ch 21.

121. *Chand Mal v Ganda Singh*, 1885 Rec No 60, p. 126; *Kalloomal Tapeshwari Prasad & Co v RC&F Ltd*, AIR 1990 All 214, lien not allowed for mere storage of fertilizers.

122. *Vithoba Laxman Kalar v Maroti Ukandsa Kalar*, AIR 1940 Nag 273.

123. *Skinner v Jager*, ILR (1883) 6 All 139.

124. *Chase v Westmore*, (1816) 15 M&S 180: 105 ER 1016, piecemeal delivery of goods under one contract, lien on the whole lot arises; *Miller v Nasmyths Patent Press Co*, ILR (1882) 8 Cal 312, jute delivered from time to time for pressing.

125. *Eduljee v Cafe John Bros*, ILR 1944 Nag 37.

claimed lien on these parts until the outstanding charges of repair were paid.

The court held that delivery of possession after repairs are effected puts an end to the lien which the repairer has for the charges of repairs and cannot be revived because the repairer undertakes further repairs merely out of grace and not as a matter of fresh contract. The court cited Lord ELLENBOROUGH as saying:<sup>126</sup> "...the defendant, after the repairs were completed, relinquished his possession, and could not afterwards detain for the amount of the repairs."

Thus, "lien is a possessory right which continues only so long as the possessor holds the goods".<sup>127</sup>

The right of lien may also be defeated or excluded by an agreement to the contrary. By an agreement to that effect, a particular lien may be converted into a general lien. For, Section 171 says in the end that no other persons have the right to general lien unless there is an express contract to that effect. The right of lien also became affected when the carrier was directed to deliver the goods to the consignor Warehousing Corporation because they were in the danger of perishing. The order required the furnishing of a bank guarantee.<sup>128</sup>

### General lien [S. 171]

The right of "general lien", as provided for in Section 171, means the right to hold the goods bailed as security for a general balance of account. The right of particular lien entitles a bailee to detain only that particular property in respect of which charges are due. But general lien entitled the bailee to detain any goods bailed to him for any amount due to him whether in respect of those goods or any other goods. If, for example, two securities are given to a banker but a loan has been taken only against one of them, the banker may detain both securities until his dues are paid. Where a quantity of imported meat was stored with a warehouse keeper who by a general term of the trade had a general lien, it was held that he could retain the meat for his charges due in respect of other goods.<sup>129</sup>

**S. 171. General lien of bankers, factors, wharfingers, attorneys and policy brokers.**—Bankers, factors, wharfingers, attorneys of a High Court and policy brokers may, in the absence of a contract to the contrary, retain as a security

126. In *Hartley v Hitchcock*, (1816) 171 ER 512.

127. See *Legg v Evans*, (1840) 151 ER 311; *Jacobs v Latour*, (1828) 5 Bing 130: 130 ER 1010, cited in the above-noted Nagpur decision. See also *Surya Investment Co v State Trading Corpn of India (P) Ltd*, AIR 1987 Cal 46, where the bailee lost his lien because the goods in his cold store were claimed by a special officer, the bailee was allowed by personal action to recover under S. 158 his expenses of storage; *Pennington v Reliance Motor Works Ltd*, (1923) 1 KB 127, non-transferable right.

128. *Central Warehousing Corpn v Prabhu Narain Singh*, AIR 2003 All 223: 2003 AIHC 3392 (All).

129. *Jowitt & Sons v Union Cold Storage Co*, (1913) 3 KB 1.

for a general balance of account, any goods bailed to them; but no other persons have a right to retain, as a security for such balance, goods bailed to them, unless there is an express contract to that effect.

### Parties entitled to general lien

The right of general lien is a privilege and is specially conferred by Section 171 on certain kinds of bailees only. They are: (1) Bankers, (2) Factors, (3) Wharfingers, (4) Attorneys of a High Court, and (5) Policy-brokers.

#### 1. Bankers

“The general lien of bankers, as judicially recognised and dealt with in Section 171, attaches to all goods and securities deposited with them as bankers by a customer or by a third person on a customer’s account, provided there is no contract, express or implied, inconsistent with such lien.”<sup>130</sup> The Supreme Court<sup>131</sup> cited the following passage from CHALMERS ON BILLS OF EXCHANGE<sup>132</sup> as to the concept of banker’s lien: “A banker’s lien on negotiable securities has been judicially defined as an ‘implied pledge’. A banker has, in the absence of agreement to the contrary, a lien on all bills received from a customer in the ordinary course of banking business in respect of any balance that may be due from such customer.”

The court also cited the following passage from CHITTY ON CONTRACTS:<sup>133</sup> “By mercantile custom the banker has a general lien over all forms of commercial paper deposited by or on behalf of a customer in the ordinary course of banking business. The custom does not extend to valuables lodged for the purpose of safe custody and may in any event be displaced by an express agreement or circumstances which show an implied agreement inconsistent with the lien.

... The lien is applicable to negotiable instruments which are remitted to a banker from the customer for the purpose of collection. When collection has been made the proceeds may be used by the banker in reduction of the customer’s debt balance unless otherwise earmarked.”<sup>134</sup>

Acting on these authorities the court came to the conclusion that fixed deposit receipts deposited by way of security for cash-credit facility were usable as security against the customer’s other debts also.<sup>135</sup>

130. *Mercantile Bank of India Ltd v Rochaldas Gidumal & Co*, AIR 1926 Sind 225. *SBI v Deepak Malviya*, AIR 1996 All 165, banker entitled to retain goods bailed for satisfaction of any other debt or promise.

131. *Syndicate Bank v Vijay Kumar*, (1992) 2 SCC 330: AIR 1992 SC 1066, 1069.

132. (13th Edn) 91.

133. (26th Edn) 389, para 3032.

134. The court also cited similar passages from Paget’s LAW OF BANKING (8th Edn) 408.

135. See also *J&K Bank Ltd v Abdul Samad Chaloo*, AIR 2008 J&K 1, the lending bank can recover from any partner of the firm and can also look to general lien as a protection against loss on the loan. Deposits or securities have been held to be species of goods over which lien can be exercised.

Certain gold ornaments were pledged with a bank for raising a loan. The borrower paid back the loan. The bank retained the security because of another loan subsequently taken by the borrower. The bank was held to be entitled to do so till the satisfaction of the other loan also.<sup>136</sup>

It is necessary that the goods should have been given to the banker as a bailee, because the lien extends only to goods which have been bailed to the banker.<sup>137</sup> "And there is a distinction between bailment and deposit. It has been held,<sup>138</sup> that money paid into a bank to be credited into the current account of the person making the payment does not constitute a bailment."<sup>139</sup> Following these authorities, it has been held that Section 171 does not apply to cases of deposit of money in a bank. The bank cannot claim lien on such money.<sup>140</sup> The court said: "Section 171 of the Contract Act in terms does not apply to cases of deposit of money. In such cases, the relationship of bailor and bailee is not established within the meaning of Section 148. Money deposited with a bank does not maintain its identity unless set apart or earmarked for some special purpose. Since the relationship of creditor and debtor is established, the money in customers' accounts legitimately belongs to the bank. The bank has the right of ownership over the money. The bank cannot claim lien on money which belongs to it. Therefore, the application of Section 171 should be properly confined to cases where the papers, securities and other goods of the debtor are lying with the bank under bailment. Similarly, where goods are deposited for safe custody or some other special purpose, they will not be under the spell of general lien as the acceptance of the goods for a special purpose impliedly excludes general lien."<sup>141</sup> Thus where securities were given to a bank to get them exchanged for fresh bills,

136. *K. Sita v Corporation Bank*, (1999) 3 An WR 393 (AP).

137. Title deeds casually left at a banker's table after refusal by him to advance a loan were not within the spell of banker's general lien. *Lucas v Dorrein*, (1817) 7 Taunt 278: 129 ER 112. Things deposited with him in his character as a banker are within the spell. *Allahabad Bank v MECON, Doranda*, AIR 2005 Jhar 54, bank promised to issue bank guarantee on deposit of 10 per cent of the guarantee amount which was paid and guarantee issued. Subsequently, the bank exercised lien on the party's fixed deposit for payment of guarantee commission. The court did not allow it. The only requirement was that of deposit. There was no talk of guarantee commission.

138. *Foley v Hill*, (1840) 9 ER 1002; *Official Assignee v Smith*, ILR (1908) Mad 68.

139. PURANIK J in *Devendrakumar v Gulabsingh*, AIR 1946 Nag 114: ILR 1946 Nag 210, 212.

140. *SBI v M.P. Iron and Steel Works (P) Ltd*, AIR 1998 MP 93.

141. *Cuthbert v Robarts, Lubboek & Co*, (1909) 2 Ch 226 (CA). Where the goods were seized by a banker under a particular hypothecation, the terms of which did not permit such seizure, the loanee paid the amount, the banker was not permitted to detain the goods for its other claims. *C.R. Narasimha Setty v Canara Bank*, (1990) 1 Kant LJ 81. Citing, *George Henry Chambers v Patrick Davidson*, (1866) LR 1 PC 296. Acceptance on special purpose impliedly excludes the right of general lien. *Lloyds Bank Ltd v Administrator-General of Burma*, (1934) 12 Rang 25: AIR 1934 Rang 66, the right does not extend to a trust account unless it is the property of the customer. *Agra Bank's Claim, re*, (1872) LR 8 HL 41; *Official Assignee v SRMMR Ramaswamy Chetty*, ILR (1920) 43 Mad 747, the special purpose must be clearly inconsistent with general lien. *SBI v Javed Akhtar Hussain*, AIR 1993 Bom 87, money deposited in fixed deposit by the debtor in joint account with his wife in another branch than the lending branch, not allowed to be held under lien.

the banker could not exercise lien on the new securities which, as Lord CAMPBELL said, “were delivered to them for a special purpose inconsistent with the existence of the lien claimed”.<sup>142</sup> The securities were brought to the bank by a customer but they belonged to another person. The customer instructed the bank to have them renewed and to transfer the interest to his personal account. On the interest so credited the bank was allowed to exercise lien.

Another illustration of a deposit for a special purpose is the case of *Mercantile Bank of India Ltd v Rochaldas Gidumal & Co.*<sup>143</sup>

A customer gave his banker a sum of money for transmission by telegraphic transfer to his own firm at another place. The bank purported to hold the money for their balance of account against the firm.

The first question raised was whether “money” would be covered by the words “goods bailed” as used in Section 171. The word “goods” is not defined in the Indian Contract Act. The Indian Sale of Goods Act defines “goods” as excluding money. Thus the matter was open and following English authorities it was held that “money is a species of goods which may be the subject-matter of bailment and over which lien may be exercised”.<sup>144</sup> But the court held that money given for telegraphic transfer is given for a special purpose inconsistent with the exercise of the right of lien. “It would be most unbusiness like and unreasonable for a banker to expect that a remitter who is in urgent need of money at the place of payment would agree to transmit money through the banker if he is told or has reason to believe that the money is likely to be withheld in the exercise of this alleged lien.”<sup>145</sup>

Where a customer has two accounts, a deposit account and a loan account, the banker may in the exercise of its lien, transfer the money in the deposit account to the loan account without any specific instructions of the depositor to that effect.<sup>146</sup> The Karnataka High Court has held that

142. *Branda v Barnett*, (1846) 12 Cl & Fin 787: 136 ER 207.

143. AIR 1926 Sind 225, citing the above statement.

144. *Misa v Currie*, (1876) LR 1 AC 554 (HL); *Nagalinda Chettiar v Kayarohana Chettiar*, AIR 1915 Mad 80 (2).

145. *Per RUPCHAND BILARAM AJC, Mercantile Bank of India Ltd v Rochaldas Gidumal & Co*, AIR 1926 Sind 225, 227. See *Krishna Kishore Kar v United Commercial Bank*, AIR 1982 Cal 62, where there was special arrangement for reimbursement between the parties and that excluded particular lien. In reference to the contents of an account the court held that they could be withheld for debit balance in another account of the same customer. *Port of Bombay v Sriyanesh Knitters*, AIR 1983 Bom 88, special statutory rights excluding general lien; *Port of Bombay v Premier Automobiles*, (1974) 4 SCC 710. The Supreme Court did not allow a bank to detain goods belonging to the firm against partners’ individual accounts. *Gurbax Rai v Punjab National Bank*, (1984) 3 SCC 96: AIR 1984 SC 1012.

146. *Devendrakumar v Gulabsingh*, AIR 1946 Nag 114: ILR 1946 Nag 210. Money held under a fixed deposit scheme has been held to be not a subject-matter of general lien. *Union Bank of India v Venugopalan*, (1990) 1 KLT 262. Such money does not create the relationship of bailor and bailee. It creates the relationship of creditor and debtor. *SBQ Steels Ltd v Indian Bank*, AIR 2014 NOC 452 (Mad), the bank freezed the customer’s account because of his failure to pay back the loan. Valid.

the right would extend to the fixed deposits of the customer including those of his/her spouse. The bank was entitled to adjust the amounts towards the loan account.<sup>147</sup> The court relied upon the decision of the Supreme Court in *Syndicate Bank v Vijay Kumar*,<sup>148</sup> which was to the effect that the banker's lien could be exercised in respect of a joint account also<sup>149</sup> and also fixed deposits. "The banker's lien is not prejudiced by any defect in the title of the customer or equities of third parties, provided the banker acts honestly and without notice of any defect of title."<sup>150</sup> Thus where a banker knows that the securities deposited by a customer belong to some other person he cannot hold them in the exercise of his lien against the customer.<sup>151</sup> But where two firms have separate accounts in a bank and agree to give the bank a general lien over all monies of the two firms, the bank may hold the money in one account against a loan on the other account. This has been so held by the Punjab High Court in *Firm Jai Kishan Das Jinda Ram v Central Bank of India Ltd.*<sup>152</sup>

One of the above two firms gave a sum of money to the bank to remit the same to a sugar mill. The mill refused to accept the amount when offered. The amount thus came back to the bank and it claimed lien on it for a balance due against the other firm.

The court held that the specific object for which the money was given having failed, the money was no longer bound by any incident of trust and, therefore, the bank had a good lien in the terms of the firms' agreement.

147. *K.S. Nagalambika v Corporation Bank*, AIR 2000 Kant 201.

148. (1992) 2 SCC 330; AIR 1992 SC 1066; *City Union Bank Ltd v C. Thangarajan*, (2003) 3 BC 528 (Mad), right of lien allowed to be exercised against dues under fixed deposit receipts. *SBI v Goutmi Devi Gupta*, AIR 2002 MP 61: (2003) 1 BC 165, the surety is equally liable as a debtor and, therefore, the lender bank would have lien on the surety's fixed deposits and other amounts lying with the bank. The Gauhati High Court has held to the contrary. In *Tilendra Nath Mahanta v United Bank of India*, AIR 2002 Gau 1, it was held that a fixed deposit is basically a loan in the hands of the bank. It has no connection with a loan in a different account. An amount in another account could not be adjusted against the claim in any suit. *Mahajan Chit Fund and Finance (P) Ltd v Punjab and Sind Bank*, (2003) 5 ALD 75, FDs deposited as security against cash credit facility, allowed to be adjusted against dues. *Alekh Sahoo v Puri Urban Coop Bank Ltd*, AIR 2004 Ori 142: (2004) 97 CLT 769 (Ori), gold pledged with bank was not allowed to be retained after payment of the gold loan just only because the borrower was a guarantor in some other transaction. The pledgor was entitled to take back his security. *Narendra Singh v State of Bihar*, (2002) 1 ICC 468 (Pat), a banker can retain security for a general balance account any goods bailed to him and has a general lien over all forms of security deposited with him in the ordinary course of banking business, but has no legal justification to withhold payments from the customer's saving bank account.

149. To this extent the decision of the Lahore High Court in *Simla Banking & Industrial Co Ltd v Bhagwan Kaur*, AIR 1928 Lah 316 becomes affected because in that the opinion expressed was that a joint account would not come within the coverage of the right of lien.

150. *Firm Jai Kishan Das Jinda Ram v Central Bank of India Ltd*, AIR 1955 Punj 250; *Bank of New South Wales v Valley Butter*, 1902 AC 543.

151. *Cuthbert v Robarts, Lubboek & Co*, (1909) 2 Ch 226 (CA); *Punjab National Bank Ltd v Satyapal Virmani*, AIR 1956 Punj 118; *Vijaya Bank v Naveen Mechanised Construction (P) Ltd*, AIR 2004 Kant 199, securities furnished under a bank guarantee became free because the obligation was discharged.

152. AIR 1955 Punj 250.

Where an equitable mortgage is created by deposit of title deeds for a particular loan, whether the same can be withheld for a subsequent debt is a question to be answered on facts. The Karnataka High Court held that they would not be the subject-matter of a general lien unless there was intention on the part of the depositor to that effect.<sup>153</sup>

The property mortgaged by the customer for the loan in question was attached and sold in execution of a decree. The purchaser paid back the loan and asked for return of the title deeds. The bank sought to retain the deeds as against another loan for which the customer was a surety. The purchaser paid the surety money also under protest, got the title deeds released, and then sued the bank for refund of the surety money as having been paid under coercion.

He was allowed refund. The bank was not entitled to general lien. Its withholding was wrongful and wrongful withholding of property is coercion.<sup>154</sup> The deeds were deposited to secure one particular loan and no more. The court cited Lord KINDERSLEY remark that conveyance of land was not subject to general lien.<sup>155</sup> The court also cited a remark from PAGET'S LAW OF BANKING<sup>156</sup> to the effect that "it must be assumed that the general lien extends only to the customer's own securities".

Similarly, where a person obtained a loan on a pledge of gold ornaments to the lending bank and subsequently became a guarantor for another person's loan, he was allowed to claim his ornaments on paying off his personal loan though the loan of another person guaranteed by him still subsisted.<sup>157</sup> The principle of general lien does not extend to a loan taken by the customer from another branch of the bank.<sup>158</sup> A guarantor was allowed to take back his securities from the bank when the bank guarantee in respect of which

153. *Mangalore Catholic Coop Bank Ltd v M. Sundara Shetty*, (1987) 3 Kant LJ 21. *SBI v Jayanthi*, (2011) 2 CTC 465: AIR 2011 Mad 179 (DB), equitable mortgage by deposit of title deeds created for a special purpose to secure a particular loan. It could not be held under general lien for any other loan or dues, etc. *Mohd Nayabuddin v Union of India*, AIR 2016 Cal 172, title deeds of flat pledged with bank by borrower and co-borrower for home loan. Co-borrower had obtained cash-credit facility from the same bank under which amounts were due. Loan did not exclude general lien. Bank allowed lien over title deeds also for the amount due under co-borrower's cash-credit account.

154. The court referred to *Watts v Christie*, (1849) 11 Beav 546: 50 ER 928, where a customer's lease-deed was not allowed to be retained for dues against the firm of which he was a partner. Lord ESHER MR remarked that a general lien-holder has no right to take a security given for one purpose and apply it to another. *Wolstenholm v Sheffield Union Banking Co Ltd*, (1886) 54 LT 746 (CA), lease-deed deposited to secure a particular advance not allowed to be used for other dues.

155. *Wyld v Radford*, (1863) 33 LJ Ch 51, 53.

156. (8th Edn) 500.

157. *K. Jagdishwar Reddy v Andhra Bank*, (1988) 1 An LT 605. *Nakulan v Canara Bank*, AIR 2014 Ker 64, gold loan repaid by borrower, bank allowed to retain gold ornaments because the borrower had not discharged liability under another personal loan availed by him.

158. *Syndicate Bank v Devendra Karkera*, AIR 1994 Kant 1. The court referred to *Sree Yellamma Cotton Mills Co Ltd, re; Yellamma Cotton Wollen and Silk Mills Co Ltd, re*, AIR 1969 Mys 280, where the court said hypothecation is only an extended idea of pledge.

they were deposited came to an end. The bank was not allowed to retain them for the loan of another company in which also the guarantor was a director.<sup>159</sup>

A bank provided financial assistance to a sugar factory against pledge of its entire stock of sugar stored in its seven godowns as security. Subsequently, the stock was seized under statutory provisions for payment of other claims. It was held that the right of the Commissioner of sugar could not prevail over the rights of the bank. The bank was entitled to retain the sale proceeds of the stock of sugar in two godowns ordered by the court to be sold by public auction.<sup>160</sup>

#### *Pre-deposit for entertaining appeal under the SARFAESI Act*

Under Section 18 of the SARFAESI Act, 2002 a pre-deposit of money is required for entertaining an appeal. Such deposit has been held to be not a deposit with the lender bank. The bank had no lien on such deposit. After disposal of appeal the pre-deposit has to be refunded to the borrower unless already appropriated by the bank with the consent of the depositor or any attachment in any proceedings under Section 13 or Rules.<sup>161</sup>

#### *2. Factors*

The word “factor” in India, as in England, means an agent entrusted with possession of goods for the purpose of selling them for his principal.<sup>162</sup> He is given the possession of the goods in the ordinary course of his business for the purpose of sale. He has a general lien on the goods of his principal for his balance of account against the principal. Thus where a motor car was delivered to an agent for sale, he was held entitled to retain the car until his charges were paid.<sup>163</sup> It is necessary for the lien to arise that the goods should have been delivered to the factor in the course of business and in his capacity as a “factor”.

A factor who used to have various dealings with his principal was instructed by the principal to effect a policy of insurance on a ship. The principal sent the premium and the policy remained in the possession of the agent, who claimed lien for the money which was owing to him in his capacity as a factor.

His claim was not allowed, as the policy of insurance had not come to his possession in his capacity as a factor.<sup>164</sup>

159. *Vijaya Bank v Naveen Mechanised Construction (P) Ltd*, AIR 2004 Kant 199.

160. *Central Coop Bank Ltd v State of Maharashtra*, (2011) 3 Mah LJ 634; *Devi Ispat Ltd v Central Bank of India*, (2010) 3 ICC 123 (Cal), as long as the banker shows something due from the constituent by way of general balance of account, the banker may retain the goods bailed to it as a security.

161. *Axis Bank v SBS Organics (P) Ltd*, 2016 SCC OnLine SC 353: (2016) 196 Comp Cas 236.

162. STUART CJ in *E.H. Parakh v King Emperor*, AIR 1926 Oudh 202.

163. *E.H. Parakh v King Emperor*, AIR 1926 Oudh 202.

164. *Dixon v Stansfield*, (1850) 10 CB 398: 16 LT 150.

A factor, like a banker, will not have the right of lien on such goods as have come to his possession for a specific purpose which impliedly excludes the right to lien.<sup>165</sup>

### 3. Wharfingers

“Wharf means a place contiguous to water, used for the purpose of loading and unloading goods, and over which the goods pass in loading and unloading. It is essential to a wharf that goods should be in transit over it. The primary idea is that, it is a place used, not for storing goods, but in the process of their transit to or from water.”<sup>166</sup> Wharfinger “is he that owns or keeps a wharf, or hath the oversight or the management of it”.<sup>167</sup> A wharfinger has general lien on the goods bailed to him until his wharfage, which means, charges due for the use of his wharf, are paid.

“The fact that a manufacturer has a wharf upon which he receives goods brought to him by customers, does not entitle him to claim lien as a wharfinger upon such goods.”<sup>168</sup> He is not a wharfinger in the real sense of the word.

### 4. Attorney of High Court

An attorney or a solicitor who is engaged by a client is entitled to general lien until the fee for his professional service and other costs incurred by him are paid.<sup>169</sup> The right extends to the proceeds of the action that come to the hands of the attorney.<sup>170</sup> He has a right of lien over funds which are deposited with the court.<sup>171</sup> The Bombay High Court held in a case that a solicitor who is discharged by his client, has the right to hold the papers entrusted to him subject to his lien for costs.<sup>172</sup> The court cited the following passage from a judgment of Lord JAMES J:<sup>173</sup> “A man has a right to change his solicitor if he likes; but then the law imposes certain terms in favour of the solicitor, that is to say, that the papers in the suit cannot be taken out of his hands without having his costs paid.”

But if the attorney himself decides not to act for the client, he forfeits his lien and, therefore, must hand over the papers to the client, whether his costs

165. See *Spalding v Ruding*, (1843) 6 Beav 376: 49 ER 871: 63 RR 120; *Frith v Forbes*, (1862) 135 RR 217.

166. *Per Collins LJ in Haddock v Humphrey*, (1900) 1 QB 609 (CA).

167. *Chatock v Bellamy*, (1895) 64 LJ QB 250; *Tredgar Iron & Coal Co Ltd v Steamship Colliope*, 1891 AC 11 (HL).

168. *Miller v Nasmyths Patent Press Co*, ILR (1882) 8 Cal 312.

169. *General Share Trust Co v Chapman*, (1876) 1 CPD 771, lien on client's cheques. It is necessary that documents should come into his possession as an attorney. *Sheffield v Eden*, (1878) LR 10 Ch D 291 (CA).

170. *Devkabai v Jefferson, Bhaishankar and Dinsha*, ILR (1886) 10 Bom 248; *Mangal Chand Maloo v Purna Chandra Basu*, AIR 1949 Cal 505: ILR (1945) 1 Cal 430.

171. *Tyabji Dayabhai & Co v Jetha Devji & Co*, AIR 1927 Bom 542; *Ved and Sopher v R.P. Wagle & Co*, AIR 1925 Bom 351.

172. *Balkesserbai v Naranji Walji*, ILR (1880) 4 Bom 352.

173. *Yalden, ex p*, (1876) LR 4 Ch D 129, 131; *ibid*, 355 (ILR Bom).

are paid or not. Thus where an attorney refused to act unless his previous costs were paid<sup>174</sup>, and where a firm of attorneys was dissolved and, therefore, they ceased to act for their client<sup>175</sup>, it was held in either case that the lien was lost.

The law on this point has been summarised by the Andhra Pradesh High Court in terms of the following propositions:<sup>176</sup>

(1) The common law right of passive and retaining lien available to a solicitor in England is accepted by courts in India as part of the law of this country.

(2) The said common law right is not abrogated by Section 171, Contract Act.

(3) Section 171, Contract Act, enacts a special rule of lien applicable exclusively to attorneys who are also known as solicitors.

(4) The other practitioners, who discharge the functions of solicitors, are entitled to invoke the common law rights applicable to solicitors though Section 171 is inapplicable to them.

(5) The practitioner forfeits the right of retaining lien the moment he discharges himself or by his client for misconduct.

**Advocates.**—The Supreme Court has laid down in *R.D. Saxena v Balram Prasad Sharma*<sup>177</sup> that advocates have no right of lien over clients' papers for their unpaid fee. The Court said that files containing copies of the records (perhaps some original documents also) could not be equated with the word "goods" referred in Section 171. It could not be said that files and papers of a client lying with the advocate were in the category of "goods bailed". In the case of litigation papers in the hands of the advocate there is neither delivery of goods nor any contract that they shall be returned or otherwise disposed of. That apart, the word "goods" mentioned in Section 171 is to be understood in the sense in which that word is defined in the Sale of Goods

174. *Basanta Kumar Mitter v Kusum Kumar Mitter*, (1899–1900) 4 CWN 767. It is not a professional misconduct for a lawyer to retain the papers until payment of his fee. *Damordardass Agarwal v R. Badrilal*, AIR 1987 AP 254; *A. K. Bijili Sahib v Dadhamia Bhalambai*, AIR 1936 Mad 48; *An Advocate, re, Tuticorin*, AIR 1943 Mad 493. S. 171 is not exhaustive of the relationship of a lawyer with his client. These decisions should now be taken in the light of the Supreme Court decision in *R.D. Saxena v Balram Prasad Sharma*, (2000) 7 SCC 264: AIR 2000 SC 2912 because the Supreme Court has held that refusal of an advocate to return files to his client amounts to professional misconduct irrespective of the fact whether his fee has been paid or not.

175. *McCorkindale, re*, ILR (1880) 6 Cal 1. See also *Atool Chandra Mukerjee v Shoshee Bhusan Mookerjee*, (1901–02) 6 CWN 215, a vakil may be changed if he is not proceeding with due diligence in prosecuting the case; *Rajah V. Muthu Krishna Yachendra v W.H. Nurse*, AIR 1921 Mad 320, a vakil cannot refuse to work in the case accepted by him because his fee has not been paid; *Basanta Kumar Mitter v Kusum Kumar Mitter*, (1899–1900) 4 CWN 767. There is no lien when the removal is for misconduct. 'M' an Advocate, re, AIR 1957 SC 149: 1956 SCR 811, the courts can examine professional conduct, *An Advocate, re, Tuticorin*, AIR 1943 Mad 493.

176. *Damordardass Agarwal v R. Badrilal*, AIR 1987 AP 254.

177. (2000) 7 SCC 264: AIR 2000 SC 2912 at p. 2914.

Act. Thus they have to be saleable goods. There is no scope for converting the case-files into money, nor they can be sold to any buyer. Hence, an advocate cannot place reliance upon Section 171.

### 5. Policy brokers

An insurance agent who is employed to effect a policy of marine insurance is called a policy broker. His lien extends to any balance on any insurance account due to him from the person who employed him to effect the policy.

### Lien against time-barred debt

One of the great advantages of the right of lien is that it can be exercised for the realisation of a debt even when an action for recovery of the debt would be time barred.<sup>178</sup>

### Maritime lien

The Supreme Court explained the concept in *M.V. Al Quamar v Tsaviliris Salvage (International) Ltd*:<sup>179</sup> "Be it noted that there are two attributes to maritime lien: (a) a right to a part of the property in the *res*; and (b) a privileged claim upon a ship, aircraft or other maritime property in respect of services rendered to or injury caused by that property. Maritime lien thus attaches to the property in the event of the cause of action arising and remains attached. It is, however, inchoate and very little positive in value unless it is enforced by an action. It is a right which stems from general maritime law and is based on the concept as if the ship itself caused the harm, loss or damage to others or to their property and the ship itself must make good that loss."<sup>180</sup>

### Carrier's lien

A carrier has the right to retain goods until his dues are paid. A carrier cannot be forced to deliver goods without payment of demurrage even if the detention order was issued by the Customs Authorities. The detention order turned out to be illegal. Therefore, the Customs Authorities became liable to pay the demurrage.<sup>181</sup>

178. *Bombay Dyeing & Mfg Co Ltd v State of Bombay*, AIR 1958 SC 328: 1958 SCR 1122, 1135. *S. Vasupalaiah v Vysya Bank*, (2002) 1 ICC 327 (Kant), the court said that even if the remedy of recovering debt from the principal debtor was barred by limitation, the liability subsisted and the bank was entitled to appropriate the debt due from the amounts which were in its possession either belonging to the principal debtor or to the surety. In the absence of a special contract, there is general lien in favour of the bank over securities and amounts in its possession.

179. (2000) 8 SCC 278: AIR 2000 SC 2826 at p. 2848.

180. *Citing MARITIME LAW* by Christopher Hill (2nd Edn).

181. *Shipping Corpn of India Ltd v C.L. Jain Woollen Mills*, (2001) 5 SCC 345: AIR 2001 SC 1806.

### *Lien of Port Trust*

The general lien contained in Section 171 of the Contract Act is not covered by the provisions of Chapter VI of the Major Ports Trust (MPT) Act. This Act no doubt deals with lien in respect of, inter alia, the goods imported but it does not deal with the general lien in respect of amount due on earlier consignments for which payment has not been made. The contract to the contrary as envisaged in Section 171 of the Contract Act has to be specific. The MPT Act nowhere provides that the general lien under Section 171 of the Contract Act would not be available to wharfingers in a case where the MPT Act is applicable.<sup>182</sup>

### *“General balance of account”*

Services which are undertaken under Section 42 of the Major Ports Trust Act, 1963 have to be paid for and any amount so due would be regarded as a part of the “general balance of account”. There is no reason to give a restricted meaning to the expression to include only the wharfage charges and exclude demurrage. A comparison of the provisions of Section 171 of the Contract Act and Sections 59 and 61 of the MPT Act shows that while Section 171 enables the retention of the goods only as a trustee, Section 59 of the MPT Act gives the right of lien, while Section 61 gives the power to sell the goods and realise its dues.<sup>183</sup>

### *Lien of chit fund company*

The nature of the transaction in a chit has been held to be not that of a creditor and debtor, but contractual. The chit fund company can exercise lien over the chit amounts. The company was entitled to seek the relief of attachment before judgment against the prize amount of the surety in another chit.<sup>184</sup>

### *Set off*

Set off is different from lien in this respect that it can be carried out even without there being any bailment. A bank had loaned a sum of money to its landlord, which was still outstanding. Arrears of rent had piled up into an amount more than the sum due under the loan. Adjustment of the rent amount against the loan amount was held to be quite alright.<sup>185</sup>

182. *Port of Bombay v Sriyanesh Knitters*, (1999) 7 SCC 359: AIR 1999 SC 2947; *Om Shankar Biyani v Port of Calcutta*, (2002) 3 SCC 168: AIR 2002 SC 1217; *American President Lines Ltd v Port of Bombay*, AIR 2004 Bom 162: (2004) 4 Bom CR 809, goods delivered by shipping company to port, came within lien of the Port Trust. *Port of Madras v K.P.V. Sheik Mohammed Routher & Co Ltd*, 1963 Supp (2) SCR 915 at p. 940, goods were delivered to the port by the shipowner and, therefore, the shipowner was the bailor.

183. *Port of Bombay v Sriyanesh Knitters*, (1999) 7 SCC 359: AIR 1999 SC 2947.

184. *Margadarsi Chit Fund Co Ltd v Sd Fayazuddin*, (2001) 1 An LT 541.

185. *Central Bank of India v Keshorao Narayanrao Patil*, (2005) 1 CCC 504 (Bom).

## Types of lien covered by the Act

The Act provides for the following types of lien:

1. Lien of finder of goods [S. 168];
2. Bailee's lien:
  - (a) Particular [S. 170];
  - (b) General [S. 171];
3. Lien of pledgee or pawnee [Ss. 173–174];
4. Lien of agents [S. 221].

## 4. Right to sue

**S. 180. Suit by bailor or bailee against wrongdoer.**—If a third person wrongfully deprives the bailee of the use or possession of the goods bailed, or does them any injury, the bailee is entitled to use such remedies as the owner might have used in the like case if no bailment had been made; and either the bailor or the bailee may bring a suit against a third person for such deprivation or injury.

**S. 181. Apportionment of relief or compensation obtained by such suits.**—Whatever is obtained by way of relief or compensation in any such suit shall, as between the bailor and the bailee, be dealt with according to their respective interests.

Section 180 enables a bailee to sue any person who has wrongfully deprived him of the use or possession of the goods bailed or has done them any injury.<sup>186</sup> The bailee's rights and remedies against the wrongdoer are just the same as those of the owner. An action may, therefore, be brought by the bailee or the bailor. "Whatever is obtained by way of relief or compensation in any such suit shall, as between the bailor and the bailee, be dealt with according to their respective interests."<sup>187</sup> For example, where the railway company was induced on production of forged railway receipts to deliver certain goods, the company was held entitled as a bailee to sue to recover the goods from a person with whom they were subsequently pledged.<sup>188</sup>

"Although sub-bailment is a sub-bailment, the law has been slow to define the critical aspects of the parties' relationship."<sup>189</sup> *Morris v C.W. Martin and Sons Ltd*<sup>190</sup> has been considered to be an important starting-point of the legal

186. *Karnataka Electricity Board v Halappa*, (1987) 1 TAC 451, suit by bailee against carrier.

187. S. 181 and see *Morvi Mercantile Bank Ltd v Union of India*, AIR 1965 SC 1954, where a pledgee of the goods was held entitled to recover the same amount for the loss of the goods as the pledger could have recovered.

188. *Purshottam Das Banarsi Das v Union of India*, AIR 1967 All 549. See also *Pledge by Unauthorised Persons*, below Chapter 14, under the heading "Who can Pledge". A partnership firm which was bailee of goods was allowed to sue the third person who damaged the goods. *Umarani Sen v Sudhir Kumar Dutta*, AIR 1984 Cal 230; *Kavita Trehan v Balsara Hygiene Products Ltd*, AIR 1992 Del 92.

189. Peter Devonshire, *Sub-bailment on Terms and the Efficacy of Contractual Defences against a Non-contractual Bailor*, (1966) JBL 329.

190. (1966) 1 QB 716: (1965) 3 WLR 276 (CA).

development. The plaintiff delivered a mink stole to a furrier to be cleaned. With his consent the stole was given to the defendant, a reputed cleaner. The furrier was aware of the terms and conditions of the trade which applied to sub-bailment. One of those conditions purported to exclude liability for loss of or damage to goods. The fur was stolen by an employee of the cleaner. The owner sued him.

Lord DENNING MR spoke thus:<sup>191</sup> “Here it was not the owner, the plaintiff, who entrusted the fur to the cleaner. She handed it to Beder, who, in turn, with her authority, handed it to the cleaners who were sub-bailees for reward. Mr Beder could clearly himself sue the cleaners. But can the plaintiff sue the cleaners direct for the misappropriation by their servant.”

The plaintiff's action was accordingly allowed. The sub-bailee owed a duty to her to take care. The Court of Appeal noted with emphasis that the legal relationship of bailor and bailee of a chattel can exist independently of any contract. An exemption clause in a sub-bailment contract could be enforced against the owner only if he had expressly or impliedly consented to the bailee making a sub-bailment containing those conditions, but not otherwise.

The decision in *Johnson Mathey and Co Ltd v Constantine Terminals Ltd*<sup>192</sup> laid emphasis upon this that if the original bailor decides to sue the sub-bailee directly, he would be bound by the terms of the contract between the bailee and sub-bailee, whether there was consent or not. He could not claim to be put in a better position than that of the bailee if the latter had sued his sub-bailee.

In this case silver bullion was taken by one carrier for a part of the way and then handed over to another for completing the last leg of the journey. This latter carrier's contract with the original carrier had this clause that he would not be liable for any loss unless it was due to his wilful neglect or default. The bullion was stolen from the end carrier's possession. The clause was held to be effective against the owner.

The Privy Council examined the doctrinal basis of the concept of sub-bailment in *Pioneer Container, re*.<sup>193</sup>

The plaintiffs contracted with freight carriers for carriage of their goods by container. The Bills of Lading provided that the carriers would be entitled to sub-contract on any terms, the whole or any part of the handling, storage or carriage of the goods. The carriers sub-contracted the carriage from Taiwan to Hong Kong with the defendant shipowners. The defendants issued feeder bills of lading containing the clause that the

191. At p. 728, *ibid*. The consent theory was approved in *Compania Portorafiti Commerciale SA v Ultramar Panama Inc*, (1990) 2 Lloyd's Rep 395 see at p. 405 and the need for it was not negated in a subsequent contrary decision in *Dresser U.K. Ltd v Falcongate Freight Management Ltd*, 1992 QB 502: (1992) 2 WLR 319 (CA).

192. (1976) 2 Lloyd's Rep 215.

193. (1994) 2 AC 324: (1994) 3 WLR 1. See also *Mabkutai, The*, 1996 AC 650: (1996) 3 WLR 1 (PC) on the same point.

Bills of Lading would be governed by Chinese law and that any dispute would be determined in Taiwan. The vessel sank with the cargo as the result of a collision.

The plaintiffs commenced proceedings in Hong Kong by issuing a writ *in rem* for arresting a sister ship. The proceedings in Hong Kong suited them because if they had sued in Taiwan they would have been obliged to pay advance costs and a counter-security for the claim if the vessel was arrested. The defendants moved for stay of proceedings in Hong Kong. By the time the matter was heard the limitation period in Taiwan had expired. In reference to the contention of sub-bailment and lack of privity of contract their Lordships of the Privy Council specifically acknowledged that rights and obligations under bailment were independent of contractual doctrines. The law of bailment does not depend for its efficacy upon the doctrine of consideration and privity of contract. Their Lordships emphasised that the relationship of bailment arises automatically when a party voluntarily takes possession of another's goods. An integral element of the relationship is the assumption of a duty to the owner and direct accountability for any breach. An action would be maintained by the owner without reference to the contract of sub-bailment. It would be sufficient that the claim is founded on bailment alone. Thus, the principal bailor was not bound by the exclusive jurisdiction clause.

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The following cases from this chapter are available through EBC Explorer™:

- *Damodar Valley Corp v State of Bihar*, AIR 1961 SC 440: (1961) 2 SCR 522
- *Hutton v Car Maintenance Co*, (1915) 1 Ch 21
- *Instalment Supply (P) Ltd v Union of India*, AIR 1962 SC 53: (1962) 2 SCR 644
- *Ram Gulam v Govt of U.P.*, AIR 1950 All 206
- *Shaw & Co v Symmons & Sons*, (1917) 1 KB 799
- *UCO Bank v Hem Chandra Sarkar*, (1990) 3 SCC 389
- *Ultzen v Nicols*, (1894) 1 QB 92



# Pledge

## DEFINITION

Section 172 defines pledge:

**S. 172. "Pledge", "pawnor" and "pawnee" defined.**—The bailment of goods as security for payment of a debt or performance of a promise is called "pledge". The bailor is in this case called the "pawnor". The bailee is called the "pawnee".

Thus a pledge is only a special kind of bailment, and the chief basis of distinction is the object of the contract. Where the object of the delivery of goods is to provide a security for a loan or for the fulfilment of an obligation, that kind of bailment is called pledge. "Pawn or pledge is a bailment of personal property as a security for some debt or engagement. A pawnor is one who being liable to an engagement gives to the person to whom he is liable a thing to be held as security for payment of his debt or the fulfilment of his liability."<sup>1</sup>

Following are the essential characteristics or ingredients of a pledge:

### 1. Delivery of possession

"Delivery of the chattel pawned is a necessary element in the making of a pawn."<sup>2</sup> The property pledged should be delivered to the pawnee.<sup>3</sup> Thus, where the producer of a film borrowed a sum of money from a financier-distributor, and agreed to deliver the final prints of the film when

1. *Per SHELAT J* of the Supreme Court in *Lallan Prasad v Rahmat Ali*, AIR 1967 SC 1322; (1967) 2 SCR 233. Any kind of personal property which is movable and saleable can be the subject-matter of pledge. *Official Assignee v Madholal Sindhu*, AIR 1947 Bom 217; *Arjun Prasad v Central Bank of India*, AIR 1956 Pat 32. *Uma Kanoria v Pradip Kumar Daga*, (2002) 2 ICC 588 (Cal), pawnee is included in the definition of money lender under Bengal Money Lenders Act.
2. *See SHELAT J* at p. 1325, *ibid. Suneel Kumar Gupta v Punjab & Sind Bank*, AIR 2006 Utt 26; (2006) 4 AIR Kant (NOC) 488 (Utt) (NOC), goods pledged with creditor remaining in custody of debtor, could not be said to be pledged, delivery of possession, actual or constructive, is necessary. The creditor bank was paying from the borrower's account insurance premium. That did not establish constructive possession of the bank.
3. Things delivered would include the increments, if any, on the goods. Where shares and securities were pledged, it was held that bonus shares, dividends and interest income in respect of the securities received by the pledgee became a pledged property, *Standard Chartered Bank v Custodian*, (2000) 6 SCC 427: AIR 2000 SC 1488.

ready, the agreement was held not to amount to a pledge, there being no actual transfer of possession.<sup>4</sup> Delivery of possession may be actual or constructive.<sup>5</sup> Delivery of the key of the godown where the goods are stored, is an illustration of constructive delivery. Where the goods are in the possession of a third person, who, on the direction of the pledger, consents to hold them on pledgee's behalf, that is enough delivery. It is sometimes called delivery by attorney.<sup>6</sup> Delivery of documents of title which would enable the pledgee to obtain possession is equally effective to create a pledge. This was clearly recognised by the Supreme Court in *Morvi Mercantile Bank Ltd v Union of India*.<sup>7</sup>

Certain goods were consigned with the Railways to "self" from Bombay for transit to Okhla. The consigner endorsed the railway receipts to the appellant bank against an advance of Rs 20,000. The goods having been lost in transit, the bank as an endorsee of the railway receipts and pledgee of the goods sued the Railways for the loss of the goods which were worth Rs 35,500. The trial court rejected the action. The Bombay High Court allowed recovery up to Rs 20,000 only. There were cross-appeals against this decision.

The Supreme Court was called upon to decide whether a railway receipt could be equated with the goods covered by the word "goods" for the purpose of constituting delivery of goods. SUBBA RAO J (afterwards CJ), who delivered the majority opinion, held, that delivery of railway receipts was the same thing as delivery of goods, the pledge was, therefore, valid and the pledgee was entitled to sue for the loss. "In this vast country where goods are carried by Railways over long distances and remain in transit for long periods of time, the railway receipt is regarded as the symbol of the goods for all purposes for which a bill of lading is so regarded in England."<sup>8</sup> The Court also held that the pledgee was entitled to recover the full value of the goods lost and not merely the amount of his advance. "A pledge being a bailment of goods as security for payment of a debt, the pledgee will have the same remedies as the owner of the goods would have against third person for deprivation of the said goods or injury to them."

RAMASWAMI and MUDHOLKAR JJ dissented. They were of the view that in all cases of pledge an effective change of possession is absolutely necessary. The only exception could be in favour of a bill of lading. If the pledger has goods in his physical possession he could effect the pledge by actual delivery. If, however, the goods are in the physical possession of a third

4. *Revenue Authority v Sudarsanam Picture*, AIR 1968 Mad 319.

5. See S. 149, which provides about the mode of delivery.

6. *Madras Official Assignee v Mercantile Bank of India Ltd*, 1935 AC 53, 58–59. *Himmatnagar Nagrik Sahakari Bank Ltd v Sureshkumar Jayantilal Thakkar*, AIR 2016 Guj 68, the financing bank of a motor vehicle with whom the vehicle was pledged became liable in respect of accident of the vehicle though it was registered in the name of the owner.

7. AIR 1965 SC 1954: (1965) 3 SCR 254.

8. *Morvi Mercantile Bank Ltd v Union of India*, AIR 1965 SC 1954 at pp. 1960–61.

person, pledge should be effected by a notification to the custodian who should acknowledge to hold the goods for the bailee. There would thus be a change of possession and constructive delivery.

It has been held by the Mysore High Court that way bills issued by a public carrier have not yet acquired the character of being documents of title and, therefore, their delivery cannot be regarded as pledge of the goods.<sup>9</sup>

#### *Pledge by hypothecation*

Sometimes the goods are allowed to remain in the custody of the pledger for a special purpose. But that does not militate against the effectiveness of the pledge. *Reeves v Capper*<sup>10</sup> is an early illustration.

The captain of a ship pledged his chronometer with the shipowner who allowed him to use the instrument for the purpose of a voyage. The captain pledged it over again with another person.

The question was whether the first pledge was valid. The court held that it was. In the same way a constructive pledge comes into existence as soon as the pawnor, without actually delivering the goods, agrees to hold them for the pawnee and promises to deliver them on demand. An illustration is the decision of Andhra Pradesh High Court in *Bank of Chittoor v Narasimbulu*.<sup>11</sup>

A cinema projector and accessories were pledged with a bank. The bank allowed the property to remain with the pledgers, since they formed the equipment of a running cinema. Subsequently the pledgers sold the machinery.

The court held that the sale was subject to the pledge. "There was a constructive delivery or delivery by attornment to the bank."

Similarly, where a firm of merchants, having pledged certain railway receipts with a bank, took them back under the pretence of clearing the goods and repledged them with another bank, the Privy Council held that the first pledge was not thereby defeated.<sup>12</sup> Likewise, where certain motor vehicles pledged by a motor dealer were allowed to remain in his possession for demonstration purposes, the pledge was held to be valid.<sup>13</sup>

9. *C.I.&B. Syndicate Ltd v Ramchandra Ganapathy Probbu*, AIR 1968 Mys 133. Share certificates are not documents of title to goods, they are goods in themselves, *Lalit Mohan v Haridas*, (1916) 24 Cal LJ 335; *LIC v Escorts Ltd*, (1986) 1 SCC 264: AIR 1986 SC 1370.
10. (1838) 5 Bing NC 136: 132 ER 1057. *United Bank of India v New Glencoe Tea Co Ltd*, AIR 1987 Cal 143, valid mortgage of movables without delivery of possession. Though pledge by way of hypothecation is not dealt with under the Act, hypothecation is a valid security creating similar rights and duties as those created by a pledge. *Haripada Sadhukhan v Anatha Nath Dey*, AIR 1918 Cal 165: (1918) 22 CWN 758.
11. AIR 1966 AP 163.
12. *Mercantile Bank of India v Central Bank of India*, 1938 AC 287 (PC).
13. *Appa Rao v Salem Motors and Saleem Radios*, AIR 1955 Mad 505. In this respect a pledge becomes closer to a hypothecation because in a transaction of hypothecation, the material remains with the borrower, the lender getting only the right to seize on default and to realise the value. He is not liable for any accident caused by the motor vehicle which is under his

In such cases the other creditors cannot claim anything from such goods unless the claim of the pledgee is first satisfied.<sup>14</sup>

## 2. In pursuance of contract

“Pledge is a conveyance pursuant to a contract, and it is essential to a valid pledge that delivery of the chattel shall be made by the pledger to the pledgee in pursuance of the contract of pledge.”<sup>15</sup> But it is not necessary that delivery of possession and the loan should be contemporaneous. “Delivery and advance need not be simultaneous and a pledge may be perfected by delivery after the advance is made.”<sup>16</sup> Delivery may be made before or in contemplation of an advance, which ripens into a pledge as soon as the advance is made. For instance, in *Blundell Leigh v Attenborough*:<sup>17</sup>

On November 1, 1919, the plaintiff handed her jewellery to one Miller to value it and let her know what offer he could make as to lending her money; he was to keep the jewellery as security if he made the advance. On the same day Miller pledged the jewellery with the defendants, a pawnbroker, who in good faith advanced £ 1000 on it. On November 5, Miller advanced £ 500 to the plaintiff on the security of the ring. Miller died. The plaintiff came to know the facts. She paid the amount she had borrowed and sued the defendant for return of her jewellery.

The contention on her part was that when she gave the jewellery to Miller for examination, he only became a gratuitous bailee having no right to deal with it. There was no valid pledge then. Subsequently, when he advanced the money, no valid pledge could arise as he had already parted with the possession of the goods. But the court held that the pledge was valid. Delivery made on November 1 was a good delivery for the purpose of creating a pledge, whenever that pledge was created. “It is clear that the plaintiff intended, when she handed over the jewellery to Miller, to create a valid pledge as between him and her from the moment when he handed her the money by way of loan which she was prepared to accept.”<sup>18</sup>

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hypothecation; *Bank of Baroda v Rabari Bachubhai Hirabhai*, AIR 1987 Guj 1. A surety cannot claim the benefit of S. 141 when the security is in the shape of hypothecated goods. *Bank of India v Yogeshwar Kant Wadhera*, AIR 1987 P&H 176.

14. *Bank of India v Binod Steel Ltd*, AIR 1977 MP 188. *Bombay Mercantile Coop Bank Ltd v Paisa Fund Glass Work*, (2002) 5 Bom CR 461, goods were stored in godown for shipment by the manufacturer on the basis of which the bank issued irrevocable letters of credit. The validity of delivery of possession and of pledge was not affected by the fact that the manufacturer developed a dispute with his export agent.
15. See BANKERS LJ in *Blundell Leigh v Attenborough*, (1921) 3 KB 235 (CA). *Bank of Rajasthan Ltd v Hajarimal Milap C. Surana*, (2005) 10 SCC 238, delivery of precious stones to the lending bank for sale and realization of the amount had the effect of creating pledge for securing repayment of loan.
16. SHELAT J in *Lallan Prasad v Rahmat Ali*, AIR 1967 SC 1322, 1325. Possession may be delivered within reasonable time after the advance. *Jyoti Prakash Nandi v Mukti Prakash Nandi*, 33 IC 891: (1917) 22 CWN 297, pledge of Government promissory notes.
17. (1921) 3 KB 235 (CA).
18. See BANKERS LJ in *Blundell Leigh v Attenborough*, (1921) 3 KB 235, 240 (CA).

## RIGHTS OF PAWNEE

### 1. Right of retainer [Ss. 173–174]

**S. 173. Pawnee's right of retainer.**—The pawnee may retain the goods pledged, not only for a payment of the debt or the performance of the promise, but for the interest of the debt, and all necessary expenses incurred by him in respect of the possession or for the preservation of the goods pledged.

**S. 174. Pawnee not to retain for debt or promise other than that for which goods pledged: Presumption in case of subsequent advances.**—The pawnee shall not, in the absence of a contract to that effect, retain the goods pledged for any debt or promise other than the debt or promise for which they are pledged; but such contract, in the absence of anything to the contrary, shall be presumed in regard to subsequent advances made by the pawnee.

The first important right of a pawnee is the right to retain the goods pledged until his dues are paid. He has a right to retain the goods not only for payment of the debt or performance of the promise, but for the interest due on the debt, and all necessary expenses incurred by him in respect of the possession or for the preservation of the goods pledged.<sup>19</sup>

The pledgee can retain the goods only for the payment of that particular debt for which the goods were pledged and not for any other debt or promise, unless there is a contract to the contrary. Where, however, after a pledge is created, a subsequent advance is made without any other security, a contract to burden the same goods shall be presumed.<sup>20</sup> The right of retainer ends on proper tender of payment. If the pledgee refuses a proper tender, he opens himself up for pledger's remedies of seeking return and absolute liability of bailee under Sections 160 and 161 for failure to return in time.<sup>21</sup>

### *Special and paramount interest of pledgee*

The right of retainer is thus in the nature of a particular lien. Yet lien is different from pledge. "A pawn or pledge is an intermediate between a

19. This right of the pledgee has to be distinguished from bailee's lien. A pledge creates a special interest in the property pledged in favour of the pledgee giving him the right to sell, but a lien is only a right to retain. *Alliance Bank of Simla v Ghambani Lal Jain Lal*, AIR 1927 Lah 408: (1927) 8 Lah 373. A mortgage is different from pledge in this sense that the legal interest in the property becomes vested in the mortgagee subject only to the mortgagor's right of redemption, whereas a pledge gives to the pledgee only a special interest. *Metonic India (P) Ltd v Krishna Behl*, AIR 1997 P&H 297, the pledgee bank took over possession of the goods in the pledgor's godown and locked it, that did not amount to sub-letting of the premises for the purposes of evicting the lessee under the East Punjab Urban Rent Restriction Act, 1949.

20. *Cowasji Muncherji Banaji v Official Assignee of Bombay*, AIR 1928 Bom 507.

21. *Bank of New South Wales v O'Connor*, (1889) LR 14 AC 273. See also *State Bank of Hyderabad v Gadiraju Rama Bhaskara Viswanadha Raju*, AIR 1993 AP 337, the pledgor by a will transferred his interest in gold articles lying with the bank to his legal representative, who paid off the whole claim of the bank. The bank became bound to return the security without demanding succession certificate. The pledgee should exercise his power in a fair manner and not maliciously, *Bank of India v Lekhmoni Das*, (2000) 3 SCC 640: AIR 2000 SC 1172.

simple lien and a mortgage.”<sup>22</sup> “The pawnee gets a special property in the goods pledged. The general property remains in the pawnner and wholly reverts to him on discharge of the debt. The right to property vests in the pledgee only so far as is necessary to secure the debt.”<sup>23</sup>

Explaining the nature of the special property in the goods which is acquired by the pledgee in *Bank of Bihar v State of Bihar*<sup>24</sup> the Supreme Court observed: “This special property or interest is to be distinguished from the mere right of detention which the holder of a lien possesses, in that it is transferable in the sense that a pawnee may assign or pledge his special property or interest in the goods. Where judgment has been obtained against the pawnner of goods and execution has issued thereon, the sheriff cannot seize the goods pawned unless he satisfies the claim of the pawnee. On the bankruptcy of the pawnner the pawnee is a secured creditor with respect to things pledged.”

Thus, so long as the pawnee’s claim is not satisfied no other creditor of the pawnner has any right to take away the goods or their price. In that case, the goods which were under the pledge of a bank were seized by the State of Bihar. It was held that the seizure could not deprive the pledgee of his right to realise the amount for which the goods were pledged and, therefore, the State was bound to indemnify him up to the amount which would have been realised from the goods. The court also pointed out that the Indian law in this respect was not different from the English law.<sup>25</sup>



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22. SHELAT J in *Lallan Prasad v Rahmat Ali*, AIR 1967 SC 1322: (1967) 2 SCR 233.
  23. *Sarvopari Investments (P) Ltd v Soma Textiles & Industries Ltd*, (2003) 4 ICC 604 (Cal), pledge of shares with authority to pledgee to exercise voting rights. This right could not be taken away from the pledgee.
  24. (1972) 3 SCC 196: AIR 1971 SC 1210.
  25. *Bank of Bihar v State of Bihar*, (1972) 3 SCC 196, 200: AIR 1971 SC 1210. To the same effect, *State of A.P. v Andhra Bank Ltd*, AIR 1988 AP 18, the court pointing out that English law is no different in this respect; *Central Bank of India v Grains and Gunny Agencies*, AIR 1989 MP 28, the bank not being able to deliver goods, nor account for their loss, was held entitled to no relief; *SBI v N. Sathiah*, AIR 1989 Mad 279, the pledgee is entitled to a clean decree and not one linked with the genuineness or spuriousness of the pledged articles; workers’ claims not given precedence over that of the pledgee’s right, *Central Bank of India v Authority under the Payment of Wages Act*, 1986 SCC OnLine Mad 213: (1987) 100 LW 343.

S.Y.C.W. & S. Mills, *re*, AIR 1969 Mys 280. A. NARAYANA PAI J observed as follows:— “In the case of hypothecation or pledge of movable goods, there is no doubt about the creditor’s right to take possession, to retain possession and to sell the goods directly without the intervention of court for the purpose of recovering his dues. The position in the case of regular pledge completed by possession is undoubtedly set out in the relevant sections of the Contract Act. Hypothecation is only extended idea of pledge, the creditor permitting the debtor to retain possession either on behalf of or in trust for himself (the creditor).” *State SBI v State of Rajasthan*, 1995 AIHC 4314 (Raj), here the bank had lien over the goods in question. The attachment of such goods for payment of State Taxes was held to be illegal. *Bank of Baroda v Collector*, 1993 Cri LJ 3503 (MP), attachment of goods under bank’s pledge not lawful even if the trader who pledged them was violating the limits of the Essential Commodities Act, 1955. *O. Konavalov v Commander, Coast Guard Region*, (2006) 4 SCC 620, property pledged was seized by the State under statutory power, lien on the property for the purpose of payment of pawnee remained effective.

A sugar manufacturing company had pledged its stock of sugar with the lending bank. It was held that the rights of the bank over the pawned sugar had precedence over claims of the Cane Commissioner for payment to cane growers and claims of workmen. In the absence of winding up of the company, their claims ranked as those of unsecured creditors.<sup>26</sup> A sugar mill took bank loan by pledging sugar stock. The stock was sold in auction pursuant to a recovery certificate issued against the mill for payment of sugarcane growers. Provident fund dues of mill employees were also outstanding. It was held that disbursement of sale proceeds first towards PF dues and cane growers was improper. The pawnee bank had to be given precedence over other dues.<sup>27</sup>

Records proved that sugar factories had entered into a tagging agreement as per Section 17(5) of the UP Sugarcane (Regulation of Supply and Purchase) Act, 1953 which provided that an advance obtained on the security of stock of sugar which is produced or to be produced has to be utilised for payment of dues of cane growers irrespective of any other financial agreement in respect of the same stock of sugar. It was held that financial institutions would be entitled to assert their rights only after dues of cane growers as per tagging agreement were duly fulfilled.<sup>28</sup>

#### *Hypothecatee has no direct right of seizure*

Where the pledge is by way of hypothecation, the creditor cannot directly seize the goods by entering premises or otherwise. He has to do so either with the consent of the borrower or through a court order. The creditor does not have the right to enter the premises, lock and seal the same. In *Union of India v Shenthilnathan*<sup>29</sup> the most conspicuous feature of the agreement was that in case the borrower committed default in payment of the debt as stipulated, the lender was at liberty to seize the goods. The court held that this power was not directly exercisable. No possession was delivered on the date when the hypothecation deed was entered into. What was contemplated was a future *overt act* on the part of the creditor to sequester the goods, if so desired and that too by a process known to law. At best the right which the plaintiff had under the agreement was to file a suit on the debt and after obtaining a decree to proceed against the property specified in realisation of the decree.<sup>30</sup>

26. *Central Bank of India v Siriguppa Sugars & Chemicals Ltd*, (2007) 8 SCC 353: AIR 2007 SC 2804.
27. *Sahyadri Coop Credit Society Ltd v State of Maharashtra*, AIR 2016 SC 1580.
28. *Rashtriya Kisan Mazdoor Sangathan v State of U.P.*, AIR 2015 NOC 423 (All).
29. (1977) 2 MLJ 499.
30. Followed in *Sukra Shoe Fabric v UCO Bank*, 1990 SCC OnLine Mad 567: (1991) 1 LW 452 (Mad). The court also pointed out that such claims cannot be raised through writ jurisdiction even when the claim is against Government agencies, such as nationalised banks, because the subject-matter of the litigation is purely contractual. Where the financier who is hypothecatee of the material financed by him takes possession on default in lawful manner and in accordance with the terms of the agreement, he cannot be charged with theft under S. 379 of the Indian Penal Code, 1860, *Shriram Transport Finance Co Ltd v R. Khaimlla Khan*, (1993)

Where the contract provided that the hypothecatee would have the power to take possession of and sell hypothecated goods without intervention of the court, it was held that a dispute resulting from the exercise of this power was outside the scope of determination in a writ jurisdiction.<sup>31</sup>

Where the purchase of a vehicle was financed, and the financier neither gave information as to the latest position of instalments nor gave any notice before seizure of the vehicles by force, the fact being that all instalments had already been paid, the seizure was held to be illegal. The order of the trial court awarding damages to the extent of Rs 50,000 for breach of contract by the financier was upheld.<sup>32</sup>

A clause in the agreement permitting the financier to forfeit payments already made in the event of a default was held to be void. The amounts paid by the borrower would have to be accounted for and credited to his account. The right of the financier is only to recover the balance amount.<sup>33</sup>

### Duty of care

Where the bank admitted that the goods in question were actually hypothecated to it and since the goods were not traceable, the High Court said that the courts below were correct in holding that the goods were lost.

1 Kant LJ 62 (DB). Such right has also been *upheld* in *S.B. Shah Ali*, AIR 1995 AP 134, including the right of sale without intervention of court. *Haripada Sadhukhan v Anatha Nath Dey*, AIR 1918 Cal 165: (1918) 22 CWN 758, hypothecation is not a creation of statute, security is created by the intention of the parties. *Nanhuji v Chimna*, (1911) 10 IC 869, hypothecation without delivery of possession, valid security. *Chinni Venkatachalam Chetti v Athivarapu Venkatrami Reddi*, AIR 1940 Mad 929, under S. 3 of the Transfer of Property Act, 1882, there can be valid mortgage of movable property, mortgage of crop in this case, *Simla Banking Co v Pritams*, AIR 1960 Punj 42, validity and points of difference with pledge emphasised. *Nadar Bank Ltd v Canara Bank Ltd*, AIR 1961 Mad 326, pledging of godown with certain powers of control in favour of the bank, pledge, not hypothecation. *Gopal Singh Hira Singh v Punjab National Bank*, AIR 1976 Del 115, hypothecatee is deemed to be in possession of the goods. *Union of India v C.T. Shentilanathan*, (1978) 48 Comp Cas 640, hypothecation accepted in law merchant by long usage and practice. *Ahmad Alimohamed Khoja, re*, AIR 1932 Bom 613, rights of hypothecatee not inferior to those of mortgagee. Hypothecation is a species of pledge which creates a charge in favour of the hypothecatee, *Hindustan Machine Tools Ltd v Nedungadi Bank Ltd*, AIR 1995 Kant 185. *S.Y.C.W. & S. Mills, re*, AIR 1969 Mys 280, hypothecation provides a security which the bank can use by making private sale in accordance with the terms of the hypothecation deed. *Tarun Bhargava v State of Haryana*, AIR 2003 P&H 98: ILR (2003) 1 P&H 26, hypothecatee should take possession either with consent or with order of court. *Shibi Francis v State of Kerala*, AIR 2007 Ker 296, bank financed vehicle, a term that the banker's representative would have right of access to the place where the vehicle was lying and seize it, the court said that such power could not be used through hired hoodlums or *goondas*, it could be exercised only through police action, the police was obliged to take report against any such direct action.

31. *State Bank of Mysore v K. Amarnath*, (2003) 2 Kant LJ 31 (DB). *Business Bankers v K. Anandan*, (2005) 1 KLJ 97, vehicle repossessed without terminating hire-purchase agreement and without informing the purchaser about the intention to sell and sale also affected absolutely in a haphazard manner. The procedural formalities should have been complied with.
32. *Muthoot Leasing & Finance Ltd v Vasudeva Publicity Service*, AIR 2003 Del 372.
33. *Tarun Bhargava v State of Haryana*, AIR 2003 P&H 98: ILR (2003) 1 P&H 26, the financier can be held criminally liable if he forcibly seizes the vehicle on default in the payment of an instalment.

It was for the bank to show that sufficient care was taken. But no proof was offered. The bank was held liable for loss of the goods while they were in its possession.<sup>34</sup>

## 2. Right to extraordinary expenses [S. 175]

The pawnee is entitled to receive from the pawnor extraordinary expenses incurred by him for the preservation of the goods pledged. For such expenses, however, he does not have the right to retain the goods. He can only sue to recover them. This right is provided for in Section 175 which is as follows:

In an agreement of term loan and hypothecation with a bank, there was no provision empowering the bank to debit any amount by way of xerox charges or legal fees. The court did not permit the bank to debit such amounts.<sup>35</sup>

**S. 175. Pawnee's right as to extraordinary expenses incurred.**— The pawnee is entitled to receive from the pawnor extraordinary expenses incurred by him for the preservation of the goods pledged.

## 3. Right to sell [S. 176]

Section 176 which provides for this important right is as follows:

**S. 176. Pawnee's right where pawnor makes default.**—If the pawnor makes default in payment of the debt, or performance, at the stipulated time, of the promise, in respect of which the goods were pledged, the pawnee may bring a suit against the pawnor upon the debt or promise, and retain the goods pledged as a collateral security; or he may sell the thing pledged, on giving the pawnor reasonable notice of the sale.

If the proceeds of such sale are less than the amount due in respect of the debt or promise, the pawnor is still liable to pay the balance. If the proceeds of the sale are greater than the amount so due, the pawnee shall pay over the surplus to the pawnor.

Upon a default being made by the pawnor in the payment of the debt or performance of the promise, the pledgee gets two distinct rights under Section 176 of the Act. Firstly, the pledgee may sue upon the debt and retain the goods as a collateral security.<sup>36</sup> Secondly, he may sell the goods after reasonable notice of the intended sale to the pawnor.<sup>37</sup>

34. *Canara Bank v Bhavani Oil Co*, AIR 2004 Ker 273: (2004) 2 BC 192 (Ker DB).

35. *Syndicate Bank v Mahalaxmi Ginning Factory*, 2004 AIR Kant HCR 3155.

36. *S.K. Engg Works v New Bank of India*, AIR 1987 P&H 90: (1986–92) 90 PLR 546; *Chandradhar Goswami v Gauhati Bank Ltd*, AIR 1967 SC 1058. A pledgee cannot be nonsuited only because instead of realising the security, he is proceeding against the pledger personally. *Kamla Prasad Jadawal v Punjab National Bank*, AIR 1992 MP 45.

37. The right of personal action does not take away the right of realising the security. *Mahalinga Nadar v Ganapathi Subbien*, ILR (1903–05) 27 Mad 528. Where the amount was fully recovered personally from the borrower, a claim of penal interest after full recovery was not allowed, *S.N. Choubey v Central Coalfields Ltd*, AIR 2001 Jhar 13.

The right to sue is a personal action and rests upon the contract of loan quite apart from the pledge. But until the money due is recovered, the pledged goods may be retained, though they would have to be surrendered when the loan is realised. If by reason of his own act, the pledgee is unable to return the goods, he cannot have judgment for the debt. This was laid down by the Supreme Court in *Lallan Prasad v Rahmat Ali*.<sup>38</sup>

The defendant borrowed Rs 20,000 from the plaintiff on a promissory note and gave him aeroscrapes worth about Rs 35,000 as security for the loan. The plaintiff sued for repayment of the loan, but was unable to produce the security, having sold it, and, therefore, his action for the loan was rejected.

SHELAT J after examining the rights of the parties to a pledge, cited the following passage from the decision of the House of Lords in *Trustees of the Property of Ellis & Co v Dixon Johnson*:<sup>39</sup>

“If a creditor holding security sues for the debt, he is under an obligation on payment of the debt to hand over the security, and that if, having improperly made away with the security he is unable to return it to the debtor he cannot have judgment for the debt.”

“If it were otherwise,” SHELAT J added, “the result would be that he would recover the debt and also retain the goods pledged and the pawnee in such a case would be placed in a position where he incurs a greater liability than he bargained for under the contract of pledge.”<sup>40</sup>

The Orissa High Court followed this decision so as to hold that a bank holding gold by way of collateral security and suing the borrower on the

38. AIR 1967 SC 1322: (1967) 2 SCR 233. The goods are retained in such a case as a collateral security. See *S.K. Engg Works v New Bank of India*, AIR 1987 P&H 90: (1986–92) 90 PLR 546, the right of the bank to sue, while retaining the goods as a collateral security subject, of course, to the precondition of being able to return the things pledged allowed. *Bank of Baroda v Rabari Bachubhai Hirabhai*, AIR 1987 Guj 1, the bank does not become the owner of the hypothecated goods, it has only the right to sell. *T.S. Kotagi v Tahsildar Gadag*, AIR 1985 Kant 265, the right to sue can be exercised without notice, but not right of sale: *Tapanga Light Foundry v SBI*, AIR 1987 Ori 174. No right to repayment unless securities produced where the pledgee was in possession; *Union Bank of India v Debendra Nath Roy Choudhury*, AIR 1992 Gau 88.

39. 1925 AC 489. At p. 1325, *ibid*.

40. *Fakhruddin v State of M.P.*, AIR 1967 SC 1326. The right of sale arises only by reason of the pledge. It has been held by the Supreme Court that giving a loan and keeping goods in stock does not amount to pledge for the purposes of S. 176. *P.S.N.S. Ambalavanan Chettiar v Express Newspapers Ltd*, AIR 1968 SC 741: (1968) 2 SCR 239. Where the goods were delivered by a godown-keeper under the order of the Controller of Foodgrains, he not pointing out that he was only a pledgee, he was not afterwards permitted to raise the plea of pledge. *Ram Prasad v State of M.P.*, (1969) 3 SCC 24: AIR 1970 SC 1818. The court does not restrain a pledgee from exercising his right of sale. *State Bank of Bikaner v Firm Ballabh Das*, AIR 1984 Raj 107. The Kerala High Court in its decision in *Dena Bank v Glorophis James*, (1993) 2 KLT 105: (1994) 1 BC 240 distinguished this case from the decision in *Lallan Prasad v Rahmat Ali*, AIR 1967 SC 1322 and held that even where the security is lost on account of the negligence of the bank, it would not lose its right to recover back the loan amount if there is clause in the agreement exempting the bank from liability for loss caused by negligence.



promissory note would get a decree conditional upon return of the gold to the borrower<sup>41</sup> and a decree for sale of the articles if the borrower does not satisfy the decree.<sup>42</sup> Where certain fixed deposit receipts were pledged with a bank as a collateral security, they being in the nature of goods, it was held that the bank could exercise the option of retaining them and file a suit for recovery of the loan. It was also held that the bank was not obliged to adjust the monthly instalments of FDR refunds towards the loan amount.<sup>43</sup> Thus the creditor has two rights which are concurrent and the right to proceed against the property is not merely accessory to the right to proceed against the debtor personally. The same principles have been held to be applicable to cases of hypothecation or mortgage of movable property.<sup>44</sup> Section 176 has been held to be mandatory.<sup>45</sup> Where the bank took over possession of the hypothecated truck but thereafter neither sold it according to the agreed terms nor took care of it, leaving it in open place, the bank was liable for the extraordinary depreciation in the value of the vehicle.<sup>46</sup>

Where the bank provided money for purchase of a lorry and also paid insurance premium and subsequently the owner reported loss by theft, it was held that the insurance company was liable to pay the insurance money to the bank irrespective of the fact that the insurance was not in the name of the bank. The bank was the hypothecatee and both the insurance company and the borrower were joint debtors, the insurance company to the extent of insured value and the borrower for the balance.<sup>47</sup>

Where certain shares were pledged with the bank, it was held that the bank had the right to sell them without intervention of the court. The court also directed the company to register the transfer because without such registration the title of the purchaser could not be perfected.<sup>48</sup>

### *The two rights are disjunctive*

The pawnee's two rights, namely the right to sue the pawnor for personal recovery or resort to sell the security after reasonable notice, are disjunctive, being independent of each other. The fact that a period is prescribed for filing suit would not mean that the prescribed period would also apply to the alternative remedy of selling the goods.<sup>49</sup>

41. *Dodla Bhaskar Rao v SBI*, AIR 1992 Ori 161.

42. *Haridas Mundra v National and Grindlays Bank Ltd*, AIR 1963 Cal 132.

43. *SBI v Neela Ashok Naik*, AIR 2000 Bom 151: (2000) 1 Mah LJ 801.

44. *Gulambussain Lalji Sajan v Clara D'Souza*, AIR 1929 Bom 471.

45. *Official Assignee v Madholal Sindhu*, AIR 1947 Bom 217.

46. *Central Bank of India v Abdul Mujeeb Khan*, 1997 AIHC 299 (MP). See also *Punjab and Sind Bank v Nagrath Industries (P) Ltd*, AIR 1996 MP 32, goods handed over to the bank by the judgment-debtor, the bank should have sold them immediately and not retained them. Interest not allowed from the date on which the goods were made available for realising sale proceeds.

47. *SBI v Suresh Kumar*, 1995 AIHC 3889.

48. *Hindustan Devp Corp v Modiluft Ltd*, (2005) 4 CHN 14 (Cal).

49. *K.M. Hidayathulla v Bank of India*, AIR 2000 Mad 251: (2003) 2 BC 484.

The security holder is not bound to proceed against the security first or surrender it before maintaining a summary suit against the buyer.<sup>50</sup>

#### *Priority of employees' PF dues*

The employer had defaulted in depositing employees' PF dues. The property of employer was pledged with a bank by way of security for repayment of a loan. It was held that such property could be attached and sold for recovery of PF dues.<sup>51</sup>

#### **Requirement of notice**

Alternatively, the pledgee may sell the goods. Before making the sale he is required to give to the pawnner, a reasonable notice of his intention to sell.<sup>52</sup> The requirement of "reasonable notice" is a statutory obligation and, therefore, cannot be excluded by a contact to the contrary.<sup>53</sup> Thus, for example, in a case before the Allahabad High Court:

One of the terms of an agreement of loan enabled the lending banker to sell the securities without any notice to the pawnner. The pawnner defaulted in payment. The bank sent a reminder, but the pawnner asked for more time. The bank thereupon disposed of the securities.

The sale was held to be bad in law. "What is contemplated by Section 176," the court said, "is not merely a notice but a 'reasonable' notice, meaning thereby a notice of intended sale of the security by the creditor within a certain date so as to afford an opportunity to the debtor to pay up the amount within the time mentioned in the notice."<sup>54</sup> The court refused to agree with the bank's contention that the sale notice should be inferred from the pawnner's

50. *Suraj Sanghi Finance Ltd v Credential Finance Ltd*, AIR 2002 Bom 481.

51. *Maharashtra State Coop Bank Ltd v Astt. Provident Fund Commr*, (2009) 10 SCC 123.

52. *Kersarimal v Gundabathula Suryanarayananmurthy*, AIR 1928 Mad 1022, once proper notice is given, no further authorisation or permission of the pawnner to effect the actual sale is needed, nor he is bound to dispose of within reasonable time thereafter; *Motilal Babulal v Lakhmichand*, AIR 1943 Nag 234. *Sunderlal Saraf v Subhash Chand Jain*, (2005) 3 MPLJ 73: AIR 2006 MP 35: 2006 AIHC 1323 (MP), the word "sale" means intended sale and not a sale actually arranged for a particular date. A notice under the section does not require a specification of the date, time and place of sale. *Bharat Bank Ltd v Sheoji Prasad*, AIR 1955 Pat 288, a notice was valid though it stated only that sale would be arranged. The place of the bank was in a small town. It was necessary that the sale of the costly metal was to be held in a suitable market.

53. Pledger's right to redeem cannot be taken away, nor he can be foreclosed from redeeming the pledge. *Carter v Wake*, (1877) LR 4 Ch D 605. Where the pledgee acquiesces in the sale, it amounts to ratification of sale without notice. *Madholal Sindhu v Official Assignee of Bombay*, AIR 1950 FC 21.

54. *Prabhat Bank v Babu Ram*, AIR 1966 All 134; *Sri Raja Kakral Puni Venkatasudarasana Sundara etc. v Andhra Bank Ltd*, (1960) 1 An WR 234. It is enough if the notice carries an intimation of the proposed sale, whether it is signed or not, or whether it specifies the amount due or not have been held to be immaterial. A. *Srinivasulu Naidu v Gajraj Mehta*, (1990) 1 MLJ 188; *Sankaranarayana Iyer Saraswathy Ammal v Kottayam Bank Ltd*, AIR 1950 TC 66, no advance arrangement for sale necessary; *Hulas Kunwar v Allahabad Bank Ltd*, AIR 1958 Cal 644. Sale without notice is void as between the parties. *Official Assignee v Madholal Sindhu*, AIR 1947 Bom 217; *Sankaranarayana Iyer Saraswathy Ammal v Kottayam Bank*



request for time. "A notice of the character contemplated by Section 176 cannot be implied. Such notice has to be clear and specific in language...."<sup>55</sup>

If the proceeds of sale are less than the amount due in respect of the debt or promise, the pawnner is still liable to pay the balance. If the proceeds of sale are greater than the amount so due, the pawnee shall pay over the surplus to the pawnner.<sup>56</sup>

In a case before the Patna High Court,<sup>57</sup> a banker, with whom some jute bales were pledged, sold them in the exercise of his right of resale, but refunded the price to the buyer when the latter rejected the goods on the ground that they contained "gudri" and not merely jute. The banker resold the goods to another buyer at a lower figure and then sued the pawnner for the balance still due after adjusting the sale proceeds. The court rejected his action. He should have referred to the pawnner before refunding the price. UNTWALLA J said: "I find no principle or authority to support the contention that all that was done by the bank in regard to the dispute was incidental to the power of sale of the bank under Section 176. It would be disastrous for the commercial world to accept and uphold it to be good."

The right of sale can be exercised even against a time-barred debt. In lieu of sale, the court can order the pawnner to pay off the time-barred debt but such an order must inevitably be accompanied with an order to the pawnee to return the pledged articles.<sup>58</sup>

The fact that the date, time and place of sale were not mentioned in the notice did not have the effect of rendering the notice to be ineffective. No payment was made even after receiving notice. Requesting the bank to postpone sale could not deprive the bank of its right to proceed with the sale.<sup>59</sup>

Supposing that a due notice of sale has been given so that the pledgee gets the right to sell, may he buy the goods himself? The Punjab High Court held,<sup>60</sup> following a Privy Council decision<sup>61</sup> that a sale to the pledgee himself is not void. It does not terminate the contract of pledge so as to entitle the pledger to have back the goods without payment of loan. But the pledger may hold the pledgee liable for any loss he may have suffered by reason of that fact, for example, that the goods have been given a value less than their market price.

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Ltd, AIR 1950 TC 66, notice to the surety for the pledger not needed, but it would be better to inform him too so as to give him the opportunity to pay and save the security.

55. Sale of items by a cold store after giving proper notice and advertisement, depositor not turning up, sale proper and binding on him, *Himachal Fruit Growers Coop Mktg & Processing Society Ltd v Upper India Food Preservers & Processors (P) Ltd*, AIR 1984 HP 18; *Sri Rama Finance Corpn v Chajla Yellaiah Reddi*, (1976) 1 An WR 107, the pledgee is not bound to sell immediately after the date on which notice period expires.

56. S. 176 (2nd para).

57. *Laxmi Narayan Arjundas v SBI*, AIR 1969 Pat 385.

58. *T.S. Kotagi v Tahsildar Gadag*, AIR 1985 Kant 265.

59. *Sunderlal Saraf v Subhash Chand Jain*, (2005) 3 MPLJ 73: AIR 2006 MP 35: 2006 AIHC 1323 (MP).

60. *Dhani Ram & Sons v Frontier Bank Ltd*, AIR 1962 Punj 321, 322-23.

61. *Neckram Dobey v Bank of Bengal*, ILR (1891) 19 Cal 322, 323.

### *Loss of security due to pledgee's negligence*

Where goods are lost due to the negligence of the pledgee, the liability of the pledger is reduced to the extent of the value of such goods. In a case before the Supreme Court:

Certain goods in the godown of a firm were under the pledge of a bank. The godown was insured against fire. A part of them was damaged by fire. The bank received insurance money to the extent of the fire.

The bank was obliged by the court to give credit to the firm in its cash-credit account for the amount so received. The court also pointed out that bank was not entitled to hold it under lien against partners' personal accounts. The goods were of the firm. They were not the goods of the partners. They were not offered as security for the individual debts of the partners. The goods were pledged against the cash-credit facility allowed to the firm.<sup>62</sup>

### **Pawner's right to redeem [S. 177]**

Section 177 provides for the most valuable right of the pawner.

**S. 177. Defaulting pawnor's right to redeem.**—If a time is stipulated for the payment of the debt, or performance of the promise, for which the pledge is made, and the pawnor makes default in payment of the debt or performance of the promise at the stipulated time, he may redeem the goods pledged at any subsequent time before the actual sale of them; but he must, in that case, pay, in addition, any expenses which have arisen from his default.

“Satisfaction of the debt or engagement extinguishes the pawn and the pawnee on such satisfaction is bound to redeliver the property. The pawner has an absolute right to redeem the property pledged upon tender of the amount advanced.”<sup>63</sup> It has been pointed out by the Supreme Court<sup>64</sup> that “the special interest of the pledgee comes to an end as soon as the debt for which the goods were pledged is discharged. It is open to the pledger to redeem the pledge by full payment of the amount for which the pledge had been made at any time if there is no period fixed for redemption, or at any time after the fixed date and the right continues until the thing pledged is lawfully sold”. The right to redeem clearly continues up to the time on the expiry of which the pawnee has notified that the goods would be sold. But the right continues even longer, for Section 177 clearly provides that the

62. *Gurbax Rai v Punjab National Bank*, (1984) 3 SCC 96: AIR 1984 SC 1012, 1013. *Haryana Pesticides v Bank of Rajasthan Ltd*, AIR 2004 P&H 83, the pledgor was under duty to insure the goods, the bank could also do so on his default, but neither did so, the pledgor not allowed to say that he was discharged from his liability to the extent of loss caused by want of insurance, distinguishing *Durga Dass v Sansar Singh*, 2003 AIHC 2800.

63. *Per SHELAT J in Lallan Prasad v Rahmat Ali*, AIR 1967 SC 1322: (1967) 2 SCR 233. *Vasant Deorao Deshpande v SBI*, (1996) 1 Mah LJ 914, the pledgor giving notice to the bank that he was willing to pay off the loan provided the bank would return his gold securities, bank making no reply, interest did not cease to run from the date of such notice.

64. *Jaswantrai Manilal Akhaney v State of Bombay*, AIR 1956 SC 575: 1956 SCR 483, 498.

pawner may redeem the goods at any subsequent time before the actual sale of them. "So long as the sale does not take place the pawnor is entitled to redeem the goods on payment of the debt." In other words, the right to redeem is extinguished not by the expiry of time specified in the notice of sale, but by the actual sale of the goods.

Where the pawnor redeems after the expiry of the specified time, he is bound to pay to the pawnee such expenses as have arisen on account of his default. [S. 177] Where the pawnor redeems before the expiry of the specified period, he would remain bound by the terms of the loan, if any, that a premium would be leviable on premature repayment.<sup>65</sup>

The pawnor has the right to take back with the goods the increase, if any, that the goods have undergone during the period of pledge. In a case before Delhi High Court,<sup>66</sup> the pledge was that of certain shares of a company and during the period of pledge the company issued bonus and rights shares. It was held that these increases belonged to the pawnor.

Redemption means the enforcement of the right to have the title to corpus of the pledged property restored to the pledgor free and clear of the pledge. A suit for redemption has to be filed for exercising this specific remedy and not just for a declaration of the right of redemption.<sup>67</sup>

The suit was for redemption of pledged gold ornaments. The premises of the pawnee were raided and the ornaments were seized by officers of the Income Tax Department. The transaction of pledge between the parties was proved. Section 293 of the Income Tax Act could not defeat the right of the pawnor to institute the suit for recovery of his ornaments.<sup>68</sup>

#### *Legal heir's right to redeem*

Certain gold ornaments were pledged with the bank as security for gold loan. The pawnor died. He left behind a will enabling his widow to redeem. The bank demanded probate. It was held that the bank had no right to do so. Neither probate nor succession certificate was necessary. The son and daughter of the deceased had raised no objection.<sup>69</sup>

### WHO CAN PLEDGE

Ordinarily goods may be pledged by the owner or by any person with the owner's authority. A pledge made by any other person may not be valid. Thus, for example, where goods were left in the possession of a servant, while the owner was temporarily absent, a pledge made by the servant was

65. *Hotel Vrinda Prakash v Karnataka State Financial Corp*n, AIR 2007 Kant 187.

66. *M.R. Dhawan v Madan Mohan*, AIR 1969 Del 313.

67. *Nabha Investment (P) Ltd v Harmishan Dass Lukhmi Dass*, (1995) 58 DLT 285. The pledgor cannot seek any relief without tendering the amount due against him.

68. *Union of India v Deep Chand*, AIR 2007 NOC 1756 (Utt).

69. *Kamili Sarjini v Indian Bank*, AIR 2008 AP 71.

held to be invalid.<sup>70</sup> Similarly, where certain goods are left in the care of a person for some special purpose, he cannot pledge them.<sup>71</sup> In a case before the Allahabad High Court,<sup>72</sup> the railway company delivered goods on a forged railway receipt. The goods were then pledged with the defendants. In a suit by the Railways to recover the goods, the defendants contended that the Railways were too negligent in delivering the goods to a wrong person. But the court held that this would not constitute an estoppel against the company and that pledge was not valid. The principle is necessary to protect the individual interest in the ownership of property. But interest acquired in the course of lawful commercial transactions equally deserves to be protected. Accordingly, Sections 178 and 179 provide for certain circumstances in which a person, being left in possession with the consent of the owner, may make a valid pledge though without the owner's authority.

### 1. Pledge by mercantile agent [S. 178]

**S. 178. Pledge by mercantile agent.**—Where a mercantile agent is, with the consent of the owner, in possession of goods or the documents of title to goods, any pledge made by him, when acting in the ordinary course of business of a mercantile agent, shall be as valid as if he were expressly authorised by the owner of the goods to make the same: Provided that the pawnee acts in good faith and has not at the time of the pledge notice that the pawnor has no authority to pledge.

*Explanation.*—In this section, the expressions "mercantile agent" and "documents of title" shall have the meanings assigned to them in the Indian Sale of Goods Act, 1930 (III of 1930).

The first exception is in favour of a pledge created by a mercantile agent. Section 178 provides that where a mercantile agent is, with the consent of the owner, in possession of goods or documents of title to goods, any pledge made by him while acting in the ordinary course of business shall be valid, provided that the pawnee acts in good faith and has no notice of the fact that the agent has no authority to pledge.<sup>73</sup> The necessary conditions of validity under the section are as follows:

70. *Biddomoy Dabee v Sittaram*, ILR 4 Cal 497. *SBI v Manglabai G. Deshmukh*, (2005) 3 CCC 487 (Bom), borrower's widow offered to pay back bank loan and to redeem gold ornaments. The bank refused and asked her to produce letters of administration. The court said that such letters were not necessary. The court further said that the refusal was wrongful and that interest ceased to run from the date of refusal.

71. *Shankar Murlidhar v Mohanlal Jaduram*, ILR (1887) 11 Bom 704; *J.W. Seager v Hukma Kessa*, ILR (1899–1900) 24 Bom 458; *Naganda Davay v Bappa Chettiar*, ILR (1904) 27 Mad 424.

72. *Purshottam Das Banarsi Das v Union of India*, AIR 1967 All 549.

73. Ordinary examples are: pledge of customer's jewellery by a jewellery broker, *Sesappier v Subramania Chettiar*, ILR (1917) 40 Mad 678; pledge of customer's shares by sharebroker, *Fuller v Glyn*, (1914) 2 KB 168. *Munjal Gases v SBI*, (2004) 2 ICC 518 (P&H), the court stated the applicable requirements, the case dealt with the liability to return gas cylinders after use.



### 1. *Mercantile agent*

There should be a mercantile agent. The explanation to the section says that the expression “mercantile agent” has the same meaning as is assigned to it by Indian Sale of Goods Act, 1930. In this Act, “mercantile agent means an agent having in the customary course of business as such agent authority either to sell goods, or to consign goods for the purpose of sale, or to buy goods or to raise money on the security of goods”. [S. 2(9), Sale of Goods Act]

### 2. *Possession with owner's consent*

The mercantile agent should be in possession of the goods or documents of title with the consent of the owner. The Supreme Court has laid down that the word “consent” for this purpose means agreeing on the same thing in the same sense as defined in Section 13 of the Contract Act. If the consent is real, it is immaterial that it was obtained by fraud or misrepresentation or with dishonest intention. All these things may make the person receiving possession liable for some offence, but the consent of the owner actually given is not annulled thereby. Thus, where a goldsmith obtained possession of certain jewellery under the pretence that he had a customer, and instead pledged the jewellery, the pledgee was held to have obtained a good title.<sup>74</sup> Similarly, where a French Company sent to their London agents certain pictures, some being for exhibition only, but the agent pledged them, the pledge was held to be valid, the court saying that the principle applies to all goods in the custody of the mercantile agent whether for sale or not.<sup>75</sup>

In *Sharadin v Gokulchand*,<sup>76</sup> the court interpreted “possession” appearing in Section 178 as juridical possession as distinguished from mere physical possession or bare custody. It has been held that a servant or a relation entrusted by the owner with the custody of goods during his absence cannot be said to be in possession thereof so as to be entitle to make a valid pledge thereof.

### 3. *In the course of business*

Goods should have been entrusted to the agent in his capacity as a mercantile agent and he should be in possession in that capacity. If the goods are entrusted to him in a different capacity, it is not open to a third party who takes a pledge from him to say that they were in his possession as a mercantile agent and therefore, he had the power to create a pledge.<sup>77</sup> In Chalmer's *SALE OF GOODS*,<sup>78</sup> the principle is explained by this illustration:

74. *U. Sulaiman v Ma Ywet*, AIR 1934 Rang 198: (1934) 151 IC 413; *Ah San v Maung Ba Thi*, (1937) 169 IC 221.

75. *Moody v Pall Mall Deposit & Forwarding Co*, (1917) 33 TLR 306. The Supreme Court held in *Central National Bank Ltd v United Industrial Bank Ltd*, AIR 1954 SC 181: 1954 SCR 391, that when an agent to whom goods were given for repairs sells them, the owner's consent is not thereby affected.

76. AIR 1931 Lah 526.

77. See *MACKINNON J in Staffs Motor Guarantee Ltd v British Wagon Co Ltd*, (1934) 2 KB 305.

78. (13th Edn by Steighart, 1957) 202.

Suppose a house were let furnished to a man who happened to be an auctioneer. Could he sell the furniture by auction and give a good title to the buyer? Surely not?

It is further necessary that he should make the pledge in the ordinary course of his business as such agent.

The plaintiff, a dealer in diamonds at Amsterdam, sent some diamonds to a diamond broker in London for sale. The broker asked a friend of his to pledge the diamonds for him. The friend pledged them with the defendants, who were pawnbrokers.<sup>79</sup>

In the owner's action against the defendants for the diamonds, the pledge was held to be invalid. "It was not the ordinary course of business of a mercantile agent to ask a friend to pledge goods entrusted to him, but to pledge them himself."

#### 4. Good faith

The last essential requirement is that the pawnee should act in good faith and should not have at the time of the pledge notice that the pawnier has no authority to pledge. The expressions "good faith" and "notice" are not defined in the Act. The definition of "good faith" as given in the General Clauses Act, 1895 is, therefore, applicable. According to that Act a thing is said to be done in good faith when it is done honestly, whether negligently or not. "Notice" will mean actual as well as constructive notice.<sup>80</sup>

#### Pledge by documents of title [S. 178]

Where a mercantile agent is in possession of the documents of title relating to his principal's goods, and if he pledges the same, the pledgee gets a good title if he acts in good faith and without notice. An explanation to Section 178 says that the expression "documents of title" shall have the same meaning as is assigned to it in the Sale of Goods Act, 1930. Section 2(4) of this Act provides that "documents of title to goods" includes a bill of lading, dock warrant, warehouse keeper's certificate, wharfinger's certificate, railway receipt, warrant or order for the delivery of goods and any other

79. *De Gorter v Attenborough & Sons*, (1904) 21 TLR 19. Similarly it is not in the ordinary course of business to pledge outside the agent's business premises or out of business hours. *Oppenheimer v Attenborough & Sons*, (1908) 1 KB 221; sale of a motor car without registration book is also not in the ordinary course of business. *Pearson v Rose & Young Ltd*, (1951) 1 KB 275 (CA). *Poonamchand Shankarlal & Co v Deepchand Sireymal*, AIR 1972 MP 40, the firm through which the plaintiff used to purchase and sell cotton and cotton seeds was directed to deliver the goods to a designated company, but instead the firm pledged the goods and the same was held to be binding on the plaintiff. *Ah Cheung v Ah Wain*, AIR 1938 Rang 243, the section is intended to protect persons who in good-faith deal with persons about whom they knew were mercantile agents.

80. Burden lies upon the person who disputes the pledge to prove that the pledgee had notice or that he did not act in good faith. *Stadium Finance Ltd v Robbins*, (1962) 2 QB 664: (1962) 3 WLR 453 (CA). A pledge after termination of authority would be equally valid unless the pledgee had notice of it, *Moody v Pall Mall Deposit & Forwarding Co*, (1917) 33 TLR 306.

documents used in the ordinary course of business as proof of the possession or control of goods, or authorising or purporting to authorise, either by endorsement or by delivery, the possessor of the document to transfer or receive goods hereby represented.

Before the Sale of Goods Act was separated from the Contract Act in 1930, "railway receipts" were not included in the meaning of the expression "documents of title". But the Privy Council had held that "railway receipts" were also documents of title as they are treated as a symbol of possession and control of goods covered by them.<sup>81</sup> In 1930 when the Sale of Goods Act was enacted "railway receipt" was expressly included in the definition of "documents of title to goods". "This indicates the legislative intention to accept the mercantile usage found by the Judicial Committee in *Ramdas Vithaldas Durbar v S. Amerchand & Co.*<sup>82</sup>"

May the owner himself pledge the goods by transferring documents of title? It has been held both by the Privy Council and the Supreme Court that it is impossible to justify a restriction on the owner's power to pledge which was not imposed on the powers of the mercantile agent.<sup>83</sup>

## 2. Person in possession under voidable contract [S. 178-A]

**S. 178-A. Pledge by person in possession under voidable contract.**—When the pawnor has obtained possession of the goods pledged by him under a contract voidable under Section 19 or Section 19-A, but the contract has not been rescinded at the time of the pledge, the pawnee acquires a good title to the goods, provided he acts in good faith and without notice of the pawnor's defect of title.

Where goods are pledged by a person who has obtained possession under a voidable contract, the pledge is valid, provided that the contract has not been rescinded at the time of the pledge and the pledgee has acted in good faith and without notice of the pledger's defect of title. *Phillips v Brooks Ltd*<sup>84</sup> is a well-known authority.

A fraudulent person, pretending to be a man of credit, induced the plaintiff to give him a valuable ring in return for his cheque which proved worthless. Before the fraud could be discovered, the ring was pledged with the defendants.



CASE PILOT

81. *Ramdas Vithaldas Durbar v S. Amerchand & Co.*, (1915–16) 43 IA 164; *Official Assignee v Mercantile Bank of India Ltd*, (1933–34) 61 IA 416, considered and followed by SUBBA RAO J (afterwards CJ) in *Morvi Mercantile Bank Ltd v Union of India*, AIR 1965 SC 1954.

82. (1915–16) 43 IA 164: AIR 1961 PC 7.

83. *Morvi Mercantile Bank Ltd v Union of India*, AIR 1965 SC 1954. See also *C.I.&B. Syndicate Ltd v Ramchandra Ganapathy Probhu*, AIR 1968 Mys 133, where it was held that way bills issued by a public carrier have not yet acquired the character of being "documents of title". Share certificates and cash receipts have been held to be not documents of title, *LIC v Escorts Ltd*, (1986) 1 SCC 264: AIR 1986 SC 1370.

84. (1919) 2 KB 243.

The pledge was held to be valid, it being made by a person in possession under a voidable contract. The effect of fraud is to render the transaction voidable and not void and if, therefore, an innocent person has taken the goods under a pledge before the transaction is avoided, the true owner cannot claim them back. Explaining the principle, DENNING LJ observed in *Pearson v Rose & Young Ltd.*<sup>85</sup> "For instance, if a mercantile agent should induce the owner to pass the property to him by some false pretence as by giving him a worthless cheque, or should induce the owner to entrust property to him for display purposes, by falsely pretending that he was in a large way of business when he was not, then the owner cannot claim the goods back from an innocent purchaser (or pledgee) ...."

But if the contract under which possession is obtained is void, the person in possession cannot create a valid pledge. The following passage in the judgment of B.K. MUKHERJEA J in *Central National Bank Ltd v United Industrial Bank Ltd*<sup>86</sup> explains the principle: "The position, however, is entirely different if the fraud committed is of such a character as would prevent there being consent at all on the part of the owner to give possession of the goods to a particular person. Thus A might obtain possession of the goods from the owner by falsely representing himself to be B. In such cases the owner can never have consented to the possession of goods by A; the so-called consent being not a real consent is a totally void thing in law .... The position, therefore, is that when the transaction of possession is voidable merely by reason of its being induced by fraud, which can be rescinded at the option of the owner, the consent which follows false representation is a sufficient consent. But where the fraud induced an error regarding the identity of the person to whom or the property in respect of which possession was given, the whole thing is void and there is no consent in the sense of an agreement between two persons on the same thing in the same sense."<sup>87</sup>

The contract must not have been rescinded at the time of the pledge. The usual method of rescinding a contract is by giving notice to the other party of the intention to rescind. If he pledges the goods after receiving such notice, the pledge will not be valid. Where the person who has taken away the goods keeps out of the way so that he cannot be contacted, the contract can be rescinded by doing whatever the owner can do to regain possession. Thus, informing the police and requesting the Automobile Association to trace the car which has been taken away by a swindler by giving a fake cheque has been held to be a sufficient demonstration of the intent to rescind and any dealing with the goods after this will not bind the owner.<sup>88</sup>



CASE PILOT

85. (1951) 1 KB 275 (CA).

86. AIR 1954 SC 181, 184: 1954 SCR 391.

87. See also *James Cundy v Thomas Lindsay*, (1878) LR 3 AC 459: 38 LT 573: 47 LJ QB 481 and *Ingram v Little*, (1961) 1 QB 31 (1960) 3 WLR 504 (CA).

88. *Car & Universal Finance Co Ltd v Caldwell*, (1965) 1 QB 525: (1964) 2 WLR 600 (CA). The method of avoiding a contract as prescribed by S. 66 is giving notice to the other party of the intention to avoid.

### 3. Pledge by pledgee [S. 179]

**S. 179. Pledge where pawnor has only a limited interest.**—Where a person pledges goods in which he has only a limited interest, the pledge is valid to the extent of that interest.

Section 179, which is the relevant provision says that where a person pledges goods in which he has only a limited interest, the pledge is valid to the extent of that interest. Thus, when a pledgee further pledges the goods the pledge will be valid only to the extent of his interest and his interest is the amount for which the goods have been given to him as a security. If he pledges for a larger amount, the original pledger will still be entitled to his goods on paying the amount for which he himself pledged the goods.<sup>89</sup>

Where, on the other hand, an effective pledge in favour of the pledgee has not taken place, any repledge made by him will be equally ineffective. The Supreme Court decision *Jaswantrai Manilal Akhaney v State of Bombay*<sup>90</sup> is an instructive, though a bit complicated, illustration.



CASE PILOT

A Co-operative Bank had an overdraft account with the Exchange Bank, which was secured by the deposit of certain securities. After many dealings and adjustments the last position of the account was that the overdraft limit was set at Rs 66,150 and the securities under the pledge of the bank were worth Rs 75,000. The Co-operative Bank did not, however, make use of this overdraft facility for a very long time and when it attempted to sue the Exchange Bank it was itself in financial straits and had pledged the securities first with the Canara Bank and then having redeemed them, pledged them again with a private financier.

The Supreme Court held that the pledge was not valid. If the Co-operative Bank had in fact operated the overdraft account and drawn sums within the limit, the Exchange Bank would have had *pro tanto* an interest in these securities and might then have been entitled to pledge the securities with a third party. But so long as there was no overdraft by the pledger, the pledgee had no such interest as would have enabled it to sub-pledge to a third party.

### *Additional exceptions under the Sale of Goods Act*

In addition to these exceptions, a pledge by a seller remaining in possession after sale and by a buyer obtaining possession before sale is valid.<sup>91</sup> Where one of several joint-owners is in possession with the permission of all, a pledge by him would be valid, if the buyer had no notice of the situation.<sup>92</sup>

89. *Firm Thakur Das v Mathura Prasad*, AIR 1958 All 66.

90. AIR 1956 SC 575; 1956 SCR 483.

91. See S. 30(1) and (2) of the Sale of Goods Act, 1930 and *City Fur Mfg Co Ltd v Fureenbond (Brokers) London Ltd*, (1937) 1 All ER 799, goods left in the broker's warehouse after purchase; *Haji Rahim Bux v Central Bank of India*, AIR 1929 Cal 447, goods remaining in the seller's godown; *Belsize Motor Supply Co v Cox*, (1914) 1 KB 244, buyer obtaining possession before sale.

92. *Shadi Ram v Mahtab Chand*, (1895) Punj Rec 1.

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- *Bank of Bihar v State of Bihar*, (1972) 3 SCC 196
- *Biddomoy Dabee v Sittaram*, ILR 4 Cal 497
- *Central National Bank Ltd v United Industrial Bank Ltd*, AIR 1954 SC 181: 1954 SCR 391
- *Jaswantrai Manilal Akhaney v State of Bombay*, AIR 1956 SC 575: 1956 SCR 483
- *Lallan Prasad v Rahmat Ali*, AIR 1967 SC 1322: (1967) 2 SCR 233
- *Phillips v Brooks Ltd*, (1919) 2 KB 243
- *Prabhat Bank v Babu Ram*, AIR 1966 All 134



15

# Agency

## DEFINITION OF “AGENT”

Representative capacity, hallmark of agency

“Agent” is defined in Section 182 of the Act in the following words:

**S. 182. “Agent” and “principal” defined.**—An “agent” is a person employed to do any act for another, or to represent another in dealings with third persons. The person for whom such act is done, or who is so represented, is called the “principal”.

The emphasis is on the power of the agent to represent his principal in dealings with third persons. But the above “definition is wide enough to embrace a servant pure and simple, even a casual employee, a man who is engaged by me in the street to black my boots; but it cannot for a moment be contended that they are all to be placed in the same category”.<sup>1</sup> Thus what distinguishes an agent from a person appointed to do an act, is the agent’s representative capacity coupled with a power to affect the legal relations of the principal with third persons. “The essence of the matter is that the principal authorised the agent to represent or act for him in bringing the principal into contractual relation with a third person.”<sup>2</sup>

The concept of “agency” was thus explained by RAMASWAMI J of the Madras High Court in *P. Krishna Bhatta v Mundila Ganapathi Bhatta*:<sup>3</sup>

“In legal phraseology, every person who acts for another is not an agent. A domestic servant renders to his master a personal service; a person may till another’s field or tend his flocks or work in his shop or factory or mine or may be employed upon his roads or ways; one may act for another in aiding in the performance of his legal or contractual obligations of third persons .... In none of these capacities he is an agent and he is not acting for another in dealings with third persons. It is only when he acts as a

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1. VIVIAN BOSE J in *Kalyanji Kuwarji v Tirkaram Sheolal*, AIR 1938 Nag 255.
  2. *Mohesh Chandra Bosu v Radha Kishore Bhattacherjee*, (1907–08) 12 CWN 28, 32. A person performing ministerial acts is not an agent. *Mohanlal Jain v Sawai Man Singhji*, AIR 1962 SC 73: (1962) 1 SCR 702. For the position of post office, see *C.I.T. v Patney & Co*, AIR 1959 SC 1070; *Shri Jagdish Mills Ltd v CIT*, AIR 1959 SC 1160: (1960) 1 SCR 236; *Malwa United Mills Ltd v CIT*, AIR 1966 SC 1466: (1966) 2 SCR 651; *CIT v Ogale Glass Works Ltd*, AIR 1954 SC 429: (1955) 1 SCR 185.
  3. AIR 1955 Mad 648.

representative of the other in business negotiations, that is to say, in the creation, modification or termination of contractual obligations, between that other and third persons, that he is an agent.... Representative character and derivative authority may briefly be said to be the distinguishing feature of an agent.<sup>4</sup>

The same appears from an observation of the Supreme Court<sup>5</sup> to the effect that "the expression agency is used to connote the relation which exists where one person has an authority or capacity to create legal relations between a person occupying the position of principal and third parties". The National Textile Corporation Ltd was held to be neither a Government in itself nor a department of the Government. It is only a Government company. It could not equate itself with the Central Government. It could not be regarded as an agent of the Central Government. It is an independent legal person. An agent is merely an extended hand of the principal and cannot claim independent rights.<sup>6</sup>

#### *Test of determining existence of agency relationship*

The test of determining the existence of agency relationship has been explained by DHAWAN J of the Allahabad High Court in the following words:<sup>7</sup>

"Agency depends on true nature of relationship. The American jurisprudence refers to a case in which it was held that the use of the words 'agency agreement' and 'agent' by the parties in a contract does not necessarily establish a relationship of agency in the legal sense. The law in India is the same. It has been held in several decisions that the fact that the parties have called their relationship an agency is not conclusive, if the incidence of this relationship, as disclosed by evidence does not justify a

4. *P. Krishna Bhatta v Mundila Ganapathi Bhatta*, AIR 1955 Mad 648, 651. Post Office is agent of the sender, *CIT v P.M. Rathod & Co*, AIR 1959 SC 1394: (1960) 1 SCR 401; buyers from manufacturers for export purposes, only channel allowed by the State for export, not agents. *State of Mysore v Mysore Spg & Mfg Co Ltd*, AIR 1958 SC 1002. *State of Maharashtra v Deepak*, (1996) 2 Bom CR 468, an agent cannot challenge the authority of the principal from whom he derived his appointment. An agent appointed to collect toll tax on a bridge was not allowed to say that the Government should not recover anything from him because the cost of the bridge had already been recovered.
5. *Syed Abdul Khader v Rami Reddy*, (1979) 2 SCC 601: AIR 1979 SC 553, 557. *Babulal Swarupchand Shah v South Satara (F.D.) Merchants' Assn Ltd*, AIR 1960 Bom 548, formal agreement not necessary; *Laxmi Ginning & Oil Mills v Amrit Banaspati Co Ltd*, AIR 1962 Punj 56. An agency can arise without any formal contract. *Govind Prasad Sharma v Board of Revenue*, AIR 1965 MP 66. *A.P. State Coop Rural Irrigation Corpn Ltd v Coop Tribunal*, (2006) 6 ALD 814, representative capacity is the test of agency relationship, merely because the respondent had undertaken to supply machinery for certain period did not make him an agent of the petitioner.
6. *National Textile Corpn Ltd v Nareshkumar Badrikumar Jagad*, (2011) 12 SCC 695: AIR 2012 SC 264.
7. *Loon Karan Sohan Lal v John & Co*, AIR 1967 All 308, 310-11; *Purshottamdas v Gulab Khan*, AIR 1963 Pat 407, all the circumstances to be examined, and not merely labels used by the parties.

finding of agency, and that the court must examine the true nature of the relationship and the functions and responsibilities of the alleged agent.”

Applying this test to the facts of the case before him the learned Judge held that when the Assam Government placed its quota of a commodity at the hands of a dealer for resale to consumers, he was not an agent of the Government even if he was described as such in the agreement.<sup>8</sup> Similarly “a person does not become an agent merely because he gives advice in matters of business”.<sup>9</sup> A “procurement agent” has been held to be not an agent, as he is only a person directed to do an act on a commission and not to represent another.<sup>10</sup>

A person who was described under the Madras Foodgrains Procurement Order, 1947, as a “wholesale dealer” has been held to be an agent. He was to purchase and sell at price fixed by the State and he was also responsible for safety. Thus, he was a channel through which the State was operating and became an agent of the State.<sup>11</sup> Similarly, where a person was authorised by the Government of India to procure rice in Nepal, to have it milled at a specified mill in Bihar and to dispatch it to different States as directed, he was held to be an agent of the State.<sup>12</sup> Coal dispatched by a colliery under colliery control order has been held to constitute the colliery into an agency for the consignee making the latter liable for freight and demurrage.<sup>13</sup> A cheque

8. *Loon Karan Soban Lal v John & Co*, AIR 1967 All 308; *State of Madras v Jayalakshmi Rice Mill Contracto Co*, AIR 1959 AP 352; ILR 1958 AP 671. Where, on the other hand, the miller was given the authority for hulling paddy and distributing the same according to Government directions and also for accountability, he was held to be an agent. *A.Z. Mohammed Farooq v State Govt*, 1984 KLT 346 (FB).
9. *Mohesh Chandra Bosu v Radha Kishore Bhattacherrjee*, (1907–08) 12 CWN 28, see at p. 32.
10. *State of Madras v Jayalakshmi Rice Mill Contractor Co*, ILR 1958 AP 671. The Supreme Court held that an independent buyer is not an agent, even if so described in the contract. *Gordon Woodroffe & Co (Madras) Ltd v Sk M.A. Majid*, AIR 1967 SC 181: 1966 Supp SCR 1.
11. *Gumupati Alluraiah v State of A.P.*, AIR 1963 AP 394. For another example of a running State agency, see *Hari Chand Madan Gopal v State of Punjab*, (1973) 1 SCC 204: AIR 1973 SC 381. See also *Liberty Sales Services v Jakki Mull & Sons*, 1997 AIHC 2368 (Del), handing over of shop on exclusive possession basis for business, the sub-lettee to be responsible for all expenses like payment of staff, telephone, electricity, etc, agency, not tenancy. *Happy Home Builders (P) Ltd v Delite Enterprises*, (1995) 2 AIHC 1320, a legal counsel is not agent. A counsel appointed by the managing director of a company to negotiate the sale of the company’s property was held not to be in a position to act as an agent of the company and in that capacity to rescind a contract and to forfeit the earnest money of the contractor and appropriate it towards his claims against the company. *Vijay Traders v Bajaj Auto Ltd*, (1995) 6 SCC 566, appointment of a distributor for Bajaj vehicles, the distributor had to pay the price of the vehicles ordered by him, delivery was to be given on payment of price and he had to bear damage to vehicles in transit. The relationship was held to be that of principal to principal buyer and seller and not that of principal and agent. S. 206 which prescribes a notice for terminating an agency was not applicable.
12. *Govt of India v Jamunadhar Rungta*, AIR 1960 Pat 19. Sellers who collect Sales Tax do not become agents for tax collection: *State Tax Commr v Sada Sukh Vyapar Mandal*, (1959) 10 STC 57 (All); *Babulal v State of U.P.*, AIR 1966 All 204.
13. *Kuchwar Lime & Stone Co v Dehri Rohtas Light Rly and Co Ltd*, AIR 1969 SC 193: (1969) 1 SCR 350. *Dilawari Exporters v Alitalia Cargo*, (2010) 5 SCC 754: AIR 2010 SC 2233, the person in question acted as an agent of the cargo owner as well as that of the carrier airliner. The cargo-owner’s complaint under the Consumer Protection Act, 1986 could not be rejected

was sent by the UTI by registered post, but it was not received by the payee. There was no understanding with or request by the payee that it should be sent by post. The court said that the post office acted as the agent of UTI. Liability for non-delivery was that of the UTI and not the post office.<sup>14</sup>

### Agency in hire-purchase transactions

To know whether a person occupies the position of an agent or not, the law has to go by his functions. The law has to see the substance of the transaction and not the parties' terminology.<sup>15</sup> The relevance of the expressions used in an agreement has often been considered in connection with hire-purchase transactions. A transaction of this kind generally involves three parties, the dealer, who provides the goods; the financier, who provides money to the dealer and the hirer, who takes the goods and pays hire-purchase instalments to the financier. What happens in real substance is that the dealer hands over goods as directed by the financier. Lest the dealer be regarded as an agent of the financier a hire-purchase agreement often expressly declares that the dealer is not an agent. The Hire Purchase Act, 1972 (repealed) regards the dealer as an agent of the financier for some purposes, one of them is that if any representations are made by the dealer to promote the sale of the product, he would be deemed to be an agent of the financier. But whether he is a general agent of the finance company remains an open question. The Court of Appeal has witnessed two views being expressed.

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for want of privity of contract with the carrier. Official receiver is not the insolvent's agent, *Ramgopal Naicker v Muthukrishna Ayyar*, AIR 1957 Mad 1. A carrier who forwards goods to another carrier does not do so as an agent, *Sukul Bros v H.K. Kavarana*, AIR 1958 Cal 730. A person who purchases goods to supply them to his constituents, it depends, whether he is an agent. See generally the opinion of the Supreme Court in this matter in *State of Mysore v Mysore Spg & Mfg Co Ltd*, AIR 1958 SC 1002; *Ganesh Export and Import Co v Mahadeo*, AIR 1950 Cal 188, the use of the word "commission" for price does not convert the vendor and purchaser into principal and agent; *State of Madras v Jayalakshmi Rice Mill Contractor Co*, AIR 1959 AP 352, payment for work by way of commission, not exhaustive of the matter; *Fruits and Vegetable Merchants Union v Delhi Improvement Trust*, AIR 1957 SC 344: 1957 SCR 1, a trust constituted to hold and manage an estate, held, agency. *Ghasiram Agarwalla v State*, AIR 1967 Cal 568, fair-price shop is not agency, but ownership, held not liable for movement of goods to some other place; *S.N. Barich v State of W.B.*, AIR 1963 Cal 79; an independent buyer is not an agent, *Varsha Engg (P) Ltd v Vijay Traders, Baroda*, AIR 1983 Guj 166.

14. *Unit Trust of India v Ravinder Kumar Shukla*, (2005) 7 SCC 428: AIR 2005 SC 3528. *Sagar Warehousing Corp v Pawan Hans Helicopter Ltd*, AIR 2009 Del 8 (DB), in a contract for sale of goods to be delivered through carrier, the transporter was to be arranged by the buyer. He was regarded as the buyer's agent. The buyer company went into liquidation. The seller was allowed to take back the goods from the transporter for his price till the matter was decided in arbitration. *Mumbai Agricultural Produce Market Committee v Minister for Mktg*, AIR 2015 Bom 234, agency is created when authority is given to a person to represent the principal in dealings with third persons or to do something for the principal. An agent cannot perform an act in his own right and for himself.
15. *Supt of Stamps v Breul & Co*, (1944) 46 Bom LR 686: AIR 1944 Bom 325; *Shri Tirumala Venkateshwara Timber & Bamboo Firm v CTO*, AIR 1968 SC 784: (1968) 2 SCR 476; *Firm Murlidhar Banarilal v Kishorilal Jagannath Prasad*, AIR 1960 Raj 296, description as *pucca adatia* not exhaustive.

In one of them it was stated that the dealer is a party to the hire-purchase transaction in his own right and not as a representative of any other party, though for many purposes he is an intermediary between the two others.<sup>16</sup>

The other view considered the dealer as an agent of the finance company for many purposes of law.<sup>17</sup> The House of Lords has expressed (obiter) the opinion that the questions of liability of the finance company for acts or defaults of dealers can be resolved only in reference to the general mercantile structure within which they arise or, if one prefers the expression, to mercantile reality. The reality of the situation is that customers often do not know about the finance company. They come only to the counter of the dealer, who does everything. "If this is so, a general responsibility of the finance company for the acts, receipts and omissions of the dealer in relation to the proposed transaction of hire-purchase ought to flow from this general structure of relationship and expectation."<sup>18</sup>

### *Co-agents and co-principals*

Where the authority given to co-agents is joint, it would be necessary for them to act jointly and only then their principal would be bound. Where the authority is joint and several any one of them would be competent to act for the principal.<sup>19</sup> An agent who represents more than one principals in one and the same transactions, should account for to all of them jointly, for an account given to one may not absolve him from his liability.<sup>20</sup>

### **Essentials of agency principal should be competent to contract**

An agency being a contract of employment to bring the principal into legal relations with a third party, the first requisite is that the principal should be competent to contract:<sup>21</sup>

**S. 183. Who may employ agent.**—Any person who is of the age of majority according to the law to which he is subject, and who is of sound mind, may employ an agent.

It follows that a minor cannot appoint an agent. The appointment of an agent involves a contract, and a minor's agreement is void. Emphasising this principle, DENNING LJ observed in *Shephard v Cartwright*:<sup>22</sup> "An infant cannot appoint an agent to act for him neither by means of a power of attorney, nor by any other means. If he purports to appoint an agent, not only is

16. *Mercantile Credit Co Ltd v Hamblin*, (1965) 2 QB 242, 269; (1964) 1 WLR 423; (1964) 2 All ER 592, 600–01 (CA).

17. *Financings Ltd v Stimson*, (1962) 1 WLR 1184.

18. *Branwhite v Worcester Works Finance Ltd*, (1969) 1 AC 552; (1968) 3 WLR 760.

19. *Liverpool Household Stores Anns, re*, (1890) 59 LJ Ch 616.

20. *Raghbar Dayal v Piare Lal Bhora Mal*, AIR 1933 Lah 93.

21. The base of an agency is an agreement, *Garnac Grain Co Inc v HMF Faure and Fairclough Ltd*, 1968 AC 1130; (1967) 3 WLR 143 (HL); noted, Fridman, 84 LQR 224.

22. 1953 Ch 728, 755; (1953) 1 WLR 460 (CA).

the appointment itself void, but everything done by the agent on behalf of the infant is also void and incapable of ratification."

Explaining the reason for the infant's incapacity, his Lordship said: "An infant has not sufficient discretion to choose an agent to act for him. He is all too likely to choose a wrong man; and so the law declares him to be incapable of choosing an agent at all."

But in situations where a minor is capable of binding himself by contract he may appoint an agent to contract on his behalf. "Whatever a person can do personally he can do through an agent."<sup>23</sup> The following article in BOWSTEAD ON AGENCY<sup>24</sup> emphasises the same principle: "An infant or a lunatic is bound by a contract made by his agent with his authority, where the circumstances are such that he would have been bound if he had himself made the contract."<sup>25</sup>

Further, "there is nothing in the Act which prohibits the guardian of a minor from appointing an agent for him".<sup>26</sup>

Where a principal who had executed a power of attorney became old, weak, mentally infirm and not in a position to think independently, it was held that the power of attorney had become worthless; that the engagement of a lawyer under it came to an end, the principal being unable to give instructions because of mental infirmity and that the holder of the power was no longer competent to give evidence on behalf of the principal.<sup>27</sup>

The principle that every person has the right to appoint an agent for any purpose does not apply where the act to be performed is personal in character or when it is annexed to a public office or to an office involving any fiduciary obligation.<sup>28</sup>

23. Powell, THE LAW OF AGENCY (1952) 242, citing *Beaven v Webb*, (1901) 2 Ch 59, 77.

24. (11th Edn) 14. See also *Kusa Parida v Baishnab Malik*, AIR 1966 Ori 60.

25. See Webb, *The Capacity of an Infant to Appoint an Agent*, (1955) 18 Mod LR 461, and a note by R.E.M. on *Shephard v Cartwright*, 1953 Ch 728, 755: (1953) 1 WLR 460 (CA).

26. *Madanlal Dhariwal v Bherulal*, AIR 1965 Mys 272. Only natural guardian can deal with the property of a minor for the benefit of his estate. Dealings by a *de facto* guardian without the permission of the court are void. See *Gurmel Singh v Ujagar Singh*, (1991) 99 Punj LR 571. No specific enforcement of such a contract was allowed. The court cited: *Abdul Haq v Mohd Yehia Khan*, AIR 1924 Pat 84; *Babu Rameshwar Prasad Sabi v Anandi Devi*, AIR 1956 Pat 53; R.M. P. Ramanathan Chettiar v P.S.L. Ramanathan Chettiar, AIR 1960 Mad 207; *Gujoba Tulsiram v Nilkanth*, AIR 1958 Bom 202; *Bholanath v Balbhadrappa Prasad*, AIR 1964 All 527; *Narpat Raj v Babulal*, AIR 1964 Raj 92.

27. *Mahendra Pratap Singh v Padam Kumari Devi*, AIR 1993 All 143. *Kaju Devi v H.S. Rudrappa*, (2005) 4 ICC 515, general power of attorney holder held to be competent to appear as a witness as to matters covered by his power.

28. *T.C. Mathai v District & Sessions Judge*, (1999) 3 SCC 614: AIR 1999 SC 1385. This statement was reiterated in *K. Ramachandra Rao v State of A.P.*, (2005) 2 CTC 417 (AP FB), a general power of attorney can file a criminal complaint. This statement was repeated in *K. Gopalakrishnan v Karunakaran*, (2004) 6 CTC 333 (Mad), acts done by a power of attorney holder in the exercise of his authority given by the principal are protected even if done by him in his own name. *Pratap Balkrishna Kedari v Premadevi Laxminarayan Agarwal*, (2002) 3 Bom CR 46, owner of a licence for liquor vend appointed agent in exchange for royalty, agent not entitled to an injunction that his agency was not to be terminated. Such assignment was not allowed by the terms of licence. The fact that liquor authorities had on an earlier occasion countersigned the assignment could not create a precedent of legality.

### Agent need not be competent

**S. 184. Who may be an agent.**—As between the principal and third persons, any person may become an agent, but no person who is not of the age of majority and of sound mind can become an agent, so as to be responsible to his principal according to the provisions in that behalf herein contained.

The agent need not be competent to contract. Section 184 lays down very clearly that “as between the principal and third persons any person may become an agent”. Ordinarily, an agent incurs no personal liability while contracting for his principal and, therefore, it is not necessary that he should be competent to contract.<sup>29</sup> Thus a person may contract through a minor agent, but the minor will not be responsible to his principal.<sup>30</sup> “In the days when married women lacked contractual capacity they could nonetheless act as agents.”<sup>31</sup> A company may act as an agent beyond its capacity (*ultra vires*).<sup>32</sup> A person may act as a trustee despite his contractual competence.<sup>33</sup>

### Consideration for appointment not necessary

**S. 185. Consideration not necessary.**—No consideration is necessary to create an agency.

Lastly, Section 185 provides that no consideration is necessary to create an agency. Generally an agent is remunerated by way of commission for services rendered, but no consideration is immediately necessary at the time of appointment.

### Agent and servant

An agent occupies a position which is in many respects similar to that occupied by a servant, bailee or trustee. The distinction between an “agent” and a “servant” has been underlined by the Supreme Court in *Lakshminarayan Ram Gopal & Sons Ltd v Govt of Hyderabad*.<sup>34</sup> BHAGWATI J adopted the distinction as it is stated in Powell’s LAW OF AGENCY<sup>35</sup> and HALSBURY’S LAWS OF ENGLAND.<sup>36</sup> The main points of distinction which have been emphasised are as follows—

29. *Mohomedally Ebrahim Pirkhan v Schiller*, ILR (1889) 13 Bom 470, no liability of a foreign commission agent. *L.C. De Souza, re*, AIR 1932 All 374, minor son acting for his father, notice to son effective.
30. *Foreman v Great Western Rly Co*, (1878) 38 LT 851.
31. Treitel, THE LAW OF CONTRACT (5th Edn, 1979) 534, citing *Stevenson v Hardie*, (1773) 2 Black W 872: 96 ER 513.
32. *Bell Houses Ltd v City Wall Properties Ltd*, (1966) 2 QB 656: (1966) 2 WLR 1323 (CA). Commission for financial advise allegedly beyond the company’s powers.
33. *Shantiniketan Coop H.S. Ltd v Distt Registrar of Coop Societies*, AIR 2002 Guj 428, a French citizen was appointed as a trustee of a private trust, RBI granted its permission. In that capacity he was allowed to become a member of the cooperative society. *Arun Kumar v BSNL*, (2002) 3 KLT (SN) 92.
34. AIR 1954 SC 364: (1955) 1 SCR 393.
35. (1952) 19–20.
36. Vol 22 (Hailsham Edition) 113, para 192.

- (1) An agent has the authority to act on behalf of his principal and to create contractual relations between the principal and a third party. This kind of power is not generally enjoyed by a servant.
- (2) “A principal has the right to direct what the agent has to do; but a master has not only that right, but also the right to say how it is to be done.”<sup>37</sup> “A servant acts under the direct control and supervision of his master and is bound to conform to all reasonable orders given to him in the course of his work. But an agent, though bound to exercise his authority in accordance with all lawful instructions ... is not subject in its exercise to the direct control of supervision of the principal.”<sup>38</sup>
- (3) The mode of remuneration is generally different. A servant is paid by way of salary or wages, an agent receives commission on the basis of work done.<sup>39</sup>
- (4) A master is liable for a wrongful act of his servant if it is committed in the course of the servant’s employment. A principal is liable for his agent’s wrong done within the “scope of authority”.
- (5) A servant usually serves only one master, but an agent may work for several principals at the same time.<sup>40</sup>

The managing director of a company is an employee of the company, but in the matter of the company’s relation with third parties he occupies the position of an agent.<sup>41</sup> Similarly, the secretary of a company is its servant, but in respect of the matters that come under his domain, he becomes an agent in his dealings with third persons.<sup>42</sup> “Professional advisers, such as stockbrokers and architects often act as agents for their clients. Other professional persons are engaged simply to produce a specified result; for example, to prepare a report or to paint a picture. Such persons have no power to act on behalf of their clients; ....”<sup>43</sup>

The court is not bound by the terminology of the parties, but by the substance of the relation. Where an agent was described and treated as a servant, but the nature of the dealings showed that he was in essence an agent, it was held that he having invested his personal money and resources

37. *Per Bramwell B* in *R. v Walker*, 1858 LJMC 207, 208: 31 LT (OS) 137.

38. Powell, THE LAW OF AGENCY. See also *Qamar Shaffi Tyabji v Commr, Excess Profits Tax*, AIR 1960 SC 1269: (1960) 3 SCR 546, 551.

39. But see *Performing Right Society Ltd v Mitchell & Booker (Palais de Donse) Ltd*, (1924) 1 KB 762.

40. *Khedut Sahakari Ginning & Pressing Society v State of Gujarat*, (1971) 3 SCC 480, 484: AIR 1972 SC 1786.

41. *Hely-Hutchinson v Brayhead Ltd*, (1968) 1 QB 549: (1967) 3 WLR 1408 (CA); *K.R. Koithandarman v CIT*, AIR 1967 Mad 143: AIR 1960 SC 1269.

42. *Panorama Development (Guildford) Ltd v Fidelis Furnishing Fabrics*, (1971) 2 QB 711: (1971) 3 WLR 440 (CA); *Chandi Prasad Singh v State of U.P.*, AIR 1956 SC 149: (1955) 2 SCR 1049.

43. See G.H. Treitel, THE LAW OF CONTRACT (5th Edn, 1979) 532, citing *Leicestershire Country Council v Michael Faraday & Partners Ltd*, (1941) 2 KB 205, valuers not agents, nor bound to surrender valuation documents prepared for the purpose of report; *Fraser v B.N. Furman (Productions) Ltd*, (1967) 1 WLR 898, 910 (2) (CA), stockbrokers not agents.

in the working of the agency, the same could not be summarily terminated. It required some reasonable notice.<sup>44</sup>

### Agent and bailee

An agent differs from a bailee in certain respects. Firstly, the relationship of bailor and bailee subsists only so long as the bailee holds some goods belonging to the bailor, but this is not necessary for the subsistence of agency relationship. Sometimes an agent may be in possession of his principal's property and to that extent he may also be a bailee. And sometimes an ordinary bailee may become an agent when he is authorised to dispose of the bailor's property according to his directions.

Secondly, an agent is a representative with a power to contract on behalf of his principal. A bailee does not have that power. The Supreme Court accepted these points of distinction in a case in which a banker had assumed the responsibility of receiving the goods on behalf of an account-holder and to release them in favour of his customers against payment. The banker was held thereby not to have become an agent. He remained only a bailee.<sup>45</sup>

### Agent and buyer

A selling agency has to be distinguished from a transaction resulting in an out and out sale. The legal position of an independent buyer is enormously different from that of an agent. An illustration is to be found in the decision of the Supreme Court in *Gordon Woodroffe & Co (Madras) Ltd v Sk M.A. Majid*.<sup>46</sup> The court pointed out that even an agent can become a purchaser when he pays the price to the principal and discloses to him that fact. The opening words of the contract in question were that the defendants were buying the goods for resale in the UK. If it were not an outright sale, but only an agency, it would not have been necessary to provide for the price, for the time of delivery and for the fact that sales tax was to be borne by the defendants.

### Kinds of agent

Agents are of several kinds. The word "agent" is used to describe various types of activity. For instance, Lord HERSCHELL observed in *Kennedy v De Trafford*:<sup>47</sup> "No word is more commonly and constantly abused than the word 'agent'. A person may be spoken of as an agent and no doubt in popular sense of the word he may properly be said to be an agent, although when it is attempted to suggest that he is an agent under such circumstances

44. *Popular Shoe Mart v K. Srinivasa Rao*, (1989) 2 An LT 541: AIR 1990 NOC 87 (AP).

45. *UCO Bank v Hem Chandra Sarkar*, (1990) 3 SCC 389, 396. In the subsequent case of *Vijaya Bank v United Corpn*, AIR 1991 Ker 209, the pledgee bank being bailee, and not an agent, was allowed to recover compensation from the godown-keeper for damage to the goods.

46. AIR 1967 SC 181: 1966 Supp SCR 1.

47. 1897 AC 180, 188 (HL).

as create the legal obligations attaching to agency that use of the word is only misleading."

"The description 'agent' is often employed in business in a complimentary and not in a legal sense."<sup>48</sup> Thus one hears of "dress agency; private inquiry agent; secret agent"<sup>49</sup>, and the word is also used in reference to mechanical agents, such as washing or cleansing agent. The types of agent that are known to the business world are, however, fewer. Only those may be briefly described here.

### *Factor*

"The word 'factor' in India as in England, means an agent entrusted with the possession of goods for the purpose of selling them."<sup>50</sup> "He is a mercantile agent whose ordinary course of business is to dispose of goods, of which he is entrusted with the possession or control by his principal."<sup>51</sup>

### *Broker*

A "broker" is also a kind of mercantile agent.<sup>52</sup> He is appointed to negotiate and make contracts for the sale or purchase of property on behalf of his principal, but is not given possession of the goods.

### *Del credere agent*

A "*del credere agent*" is another type of mercantile agent. In ordinary cases the only function of an agent is to effect a contract between his principal and a third party. The agent then drops out.<sup>53</sup> He can neither sue on the contract, nor he is held liable for the failure of the third party to perform. But where an agent undertakes, on the payment of some extra commission, to be liable to the principal for the failure of the third party to perform the contract, he is called *del credere* agent and his extra commission for the guarantee is known *del credere* commission. The position of such agent was explained in *Hastie v Couturier*:<sup>54</sup>

The defendants acting as *del credere* agents sold the plaintiff's goods which were supposed to be on a voyage but which unknown to the parties had already been sold by the captain owing to damage by heat. The buyer repudiated the contract and, therefore, the agents were sued for the buyer's failure to perform.

48. HALSBURY'S LAWS OF ENGLAND (2nd Edn) 1, para 194(g).

49. Powell, THE LAW OF AGENCY (1952) 27, f.n. 3.

50. See STUART CJ in *E.H. Parakh v King Emperor*, AIR 1926 Oudh 202.

51. BOWSTEAD ON AGENCY (11th Edn, 1951) 2.

52. See *Commercial Enterprisers v Madan Mohan Singh*, AIR 1951 Hyd 47 and *William Son Magor & Co v Keshoram Agarwalla*, ILR 1956 Ass 268.

53. See PAL J in *Sukumari Gupta v Dharendra Nath*, AIR 1941 Cal 643, 655.

54. (1856) 5 H.L. Cas 673. A *dubash* is an agent of this kind, namely, a guarantor plus an agent. *K.V. Periyamianna Marakkayar and Sons v Banians & Co*, ILR (1925) 49 Mad 156: AIR 1926 Mad 544.

The question was “whether the defendants are responsible by reason of their charging a *del credere* commission, though they have not guaranteed by writing”. The court said that they were. “A higher reward is paid in consideration of their taking greater care in sales to their customers and also for assuming a greater share of responsibility than ordinary agents, namely, responsibility for the solvency and performance of their contracts by their vendees. This is the main object of the reward being given to them.” Keeping this in view, the court held that a *del credere* agency is not a contract of guarantee, even if it may terminate in a liability to pay the debt of another, because the agent has a personal interest in the transaction and, therefore, a writing is not necessary.

The nature of liability incurred by a *del credere* agent has been explained by the Allahabad High Court in the following words:<sup>55</sup>

“A *del credere* agent incurs only a secondary liability towards the principal. His legal position is partly that of an insurer and partly that of a surety for the parties with whom he deals to the extent of any default by reason of any insolvency or something equivalent. His liability does not go to the extent of making him responsible to the principal where there can be no profit by reason of any stringency in the market.”

A *del credere* agent is, however, not liable to the buyer for any default on the part of his principal.<sup>56</sup> Nor is he liable for any disputes between the principal and the buyer relating to the contract or the sum due.<sup>57</sup> The extent of his involvement as a guarantor was thus explained by BUCKLEY LJ:<sup>58</sup>

“The liability of the *del credere* agent is contingent pecuniary liability, not a liability to perform the contract; it is a pecuniary liability to make good in the event of the default of the buyer in respect of a pecuniary liability. It does not extend to other obligations of the contract. It does not expose *del credere* agent to an action to ascertain the sum due. It is limited to a contingent pecuniary liability in respect of a sum which as between the seller and the buyer is an ascertained sum.”

### CREATION OF AGENCY

In the words of DESAI J of the Supreme Court:<sup>59</sup> “The relation of agency arises whenever one person called the agent has authority to act on behalf of another called the principal and consents so to act. The relationship has its genesis in a contract.”

The relationship of principal and agent may be created in any of the following ways: (1) by express appointment; (2) by the conduct or situation of

55. *Champa Ram v Tulsiram*, (1927) 26 All LJ 81, *per SENJ* at p. 82.

56. *Shaw v Woodcock*, (1872) 7 B&C 73; 31 RR 158.

57. *Churchill & Sim v Goddard*, (1937) 1 KB 92 (CA).

58. *Thomas Gabriel & Sons v Churchill Sim*, (1914) 3 KB 1272 (CA).

59. *Syed Abdul Khader v Rami Reddy*, (1979) 2 SCC 601: AIR 1979 SC 553, 557.

the parties; (3) by necessity of the case; or (4) by subsequent ratification of an unauthorised act.

### Express appointment

Any person who is competent to contract and who is of sound mind may appoint an agent. The appointment may be expressed in writing or it may be oral.<sup>60</sup> “In English law no man can become the agent of another except by the will of that other person. His will may be manifested by writing or orally or simply by placing another in a situation in which, according to the ordinary rule or law, or perhaps it would be more correct to say, according to the ordinary usage of mankind, that other is understood to represent and act for the person who has so placed him; but in every case, it is only by the will of the employer that an agency may be created.”

“The relationship of principal and agent can only be established by the consent of the principal and the agent. They will be held to have consented if they have agreed to what amounts in law to such a relationship, even if they do not recognize it themselves and even if they have professed to disclaim it... But the consent must have been given by each of them, either expressly or by implication from their words and conduct”.

“In Indian law the definition given in Section 182 seems to be somewhat wider in this respect.... The definition does not limit the employment to one by the principal only.... It will include an employment by any authority authorised by law to make the employment.” Thus, where an agent was appointed under the provisions of a statute for the protection of the interests of quarrelling co-owners and of third persons, the Calcutta High Court held that the agent so appointed would come within the definition, though he would not have the same “well-known and settled incidents” attached to him as arise in the case of contractual agency.<sup>61</sup> Similarly, loan incurred by an agent appointed under the terms of a statute was held binding on the proprietors.<sup>62</sup>

In England also, “the law may attribute an agent to a person: for example, when a company is first formed, its original directors are its agents by operation of law .... A statute may empower the court to appoint a person to act on behalf of another and so enable the court to create the relation of principal and agent. Thus a person appointed by the court to manage the affairs of a mental patient has been held to be the patient’s agent.”<sup>63</sup>

60. *Delhasse, ex p*, (1878) LR 7 Ch D 511.

61. The appointment was under the provisions of Bengal Tenancy Act, 1885. *Dept of Animal Husbandry v K. Rinzing*, AIR 1998 Sik 7, letter of appointment under a statute stated that the appointment has been made with the approval of the Government. It was held that the plaintiff need not give any further proof of his appointment.

62. *Sukumari Gupta v Dharendra Nath*, AIR 1941 Cal 643.

63. G.H. Treitel, THE LAW OF CONTRACT (5th Edn, 1979) 530, citing *Plumpton v Burkinshaw*, (1908) 2 KB 572.

Where the appointment is made by a deed, it is called a “power of attorney”.<sup>64</sup> In a case before the Supreme Court<sup>65</sup> a power of attorney, by which a person was appointed as a caretaker of certain agricultural lands, was signed by the three owners of the lands and one of the arguments was that the appointment was ineffective because how could three persons become the principals of one agent and that too by a single power of attorney. Overruling the objection, DESAI J said: “The relationship of agency has its genesis in a contract. If agency is the outcome of a contract between the principal and the agent, in order to show that three principals jointly constituting an agent by a deed called ‘Power of Attorney’ something which was impermissible, provisions of the Contract Act or the general law of contract should have been shown as having been violated by such a contract. Nothing of the kind was pointed out to us. On the contrary, in HALSBURY’S LAWS OF ENGLAND,<sup>66</sup> the following proposition has been stated: ‘Co-principals may jointly appoint an agent to act for them and in such case become jointly liable to him and may jointly sue him.’”

The three principals who signed the power of attorney had no joint property. Even so the power was regarded to be valid and applicable to their respective agricultural lands.<sup>67</sup>

An oral appointment is also valid even though the contract which the agent is authorised to make has to be in writing.<sup>68</sup>

Under the Salary Saving Scheme adopted by the Life Insurance Corporation of India the employer, when authorised by the LIC to collect premium amount from the salary of an employee and forward it to the LIC, becomes an agent of the LIC for that purpose. Where such an employer failed in forwarding the amount to the LIC and consequently the policy was in the state of lapse at the time of the employee’s death, the National Commission under the Consumer Protection Act, 1986 directed the employer to pay the amount due to the employee under the policy. The Supreme Court did not approve this decision and directed the LIC to make payment under the policy. The employer was directed to pay Rs 25,000 as the costs of the proceedings.<sup>69</sup>

64. *Amina Begum v Mohd Ramzan*, AIR 2005 Raj 41, the power of attorney carried the words “general power of attorney” and not “special power of attorney”, it related naturally to various cases pending in courts and not to any particular transaction. *State of Rajasthan v Basant Nahata*, (2005) 12 SCC 77: AIR 2005 SC 3401, registration of deed for appointing power of attorney is not necessary unless required under the Registration Act.

65. *Syed Abdul Khader v Rami Reddy*, (1979) 2 SCC 601: AIR 1979 SC 553, 557.

66. Vol 1, 4th Edn, para 726.

67. A person performing the ministerial act of signing letters on behalf of the military secretary of an ex-Ruler, held, not an agent. *Mohanalal Jain v Sawai Man Singhji*, AIR 1962 SC 73: (1962) 1 SCR 702. Post office becomes an agent when the agreement between parties is that cheques may be sent by post. *C.I.T. v Patney & Co*, AIR 1959 SC 1070: 1959 Supp (2) SCR 868; *Indore Malwa United Mills Ltd v CIT*, AIR 1966 SC 1466: (1966) 2 SCR 651. Important members of a community are not its agents. *Sk Peru Bux v Kalandi Pati Rao*, AIR 1970 SC 1885: (1969) 2 SCR 563. There can be no agency for illegal acts. *A. Thangal Kunju Musaiar v M. Venkatachalam Potti*, AIR 1956 SC 246: (1955) 2 SCR 1196.

68. *Heard v Pilley*, (1869) LR 4 Ch 548.

69. *Delhi Electric Supply Undertaking v Basanti Devi*, (1999) 8 SCC 229: AIR 2000 SC 43.

The court referred to its own earlier decision in *Harshad J. Shah v LIC*.<sup>70</sup> The Supreme Court cited the following passage from HALSBURY'S LAWS OF ENGLAND:<sup>71</sup> "Under the law governing contracts of insurance the premium may be paid by the assured to the insurers or to an insurance agent acting on behalf of the insurers and if the agent has the authority to receive it the payment binds the insurers. The authority need not be an express authority; it may be implied from the circumstances."

### Implied agencies

Implied agencies arise from the conduct, situation or relationship of parties. Whenever a person places another in a situation in which that other is understood to represent or to act for him, he becomes an implied agent. Thus, where a woman allowed her son to drive a car for her, she paying all the expenses of maintenance and operation, it was held that the son was an implied agent of the mother and when he made a collision injuring his wife, the wife could sue the mother for the fault of her agent.<sup>72</sup> A permission granted to a person to ferry a car from one place to another makes him an agent for that limited purpose so as to create liability for consequences of negligent driving.<sup>73</sup> The borrower of a car would not occupy that position.<sup>74</sup> Unauthorised pretensions do not have that effect.<sup>75</sup> An employer allowed to collect premiums from his employees and forward the collection to the organisation, became the implied agent of the latter though described explicitly in the scheme as the agent of the employees.<sup>76</sup>

### Estoppel

One of the well-known illustrations of implied agency is agency by holding out or estoppel. The principle of holding out has been thus stated in an American case: "Where a principal has by his voluntary act placed an agent in such a situation that a person of ordinary prudence, conversant with business usages and the nature of the particular business, is justified in presuming that such agent has authority to perform a particular act and therefore deals with the agent, the principal is estopped as against such third person from denying the agent's work."<sup>77</sup>

An early illustration is *Pickering v Busk*<sup>78</sup>:

70. (1997) 5 SCC 64: AIR 1997 SC 2459. Regulations and the conditions of his service did not authorise the agent to collect premium on behalf of LIC.

71. Vol 25, 254, para 460.

72. *Smith v Mosse*, (1940) 1 KB 424.

73. *Ormrod v Crosville Motor Services Ltd*, (1953) 1 WLR 1120 (CA).

74. *Hewitt v Bonvin*, (1940) 1 KB 188 (CA); *Morgans v Launchbury*, 1973 AC 127: (1972) 2 WLR 1217 (HL).

75. *Kennedy v De Traufford*, 1897 AC 180, 188 (HL).

76. *Delhi Electric Supply Undertaking v Basanti Devi*, (1999) 8 SCC 229: AIR 2000 SC 43.

77. IRVINE C in *Johnson v Milwaukee*, (1895) 46 Neb 480: 64 NW Rep 1100; borrowed from John S. Ewart, *Estoppel—Principal and Agent*, 16 Harv LR 186, 187–88.

78. (1812) 15 East 38.

A purchaser of hemp allowed it to remain in the custody of the broker through whom he had bought it. The broker's ordinary business was to buy and sell hemp. He sold the hemp and received the price.

The Court held that the sale and receipt of money were binding on the principal. Lord ELLENBOROUGH explained the principle thus: "If a person authorises another to assume the apparent right of disposing of property in the ordinary course of trade, it must be presumed that the apparent authority is the real authority. He may bind the principal within the limits of authority with which he has been apparently clothed by the principal; and there could be no safety in commercial transactions if he could not."

An illustration is a decision of the Orissa High Court, in which<sup>79</sup> a landlord appointed a *tahsildar* to manage his agricultural lands. He let out the lands to tenants on certain terms.

An authority of this kind was not given to him and, therefore, the question was whether the tenancy agreements would bind the landlord. It was held that the landlord had, by making the *tahsildar* incharge of the lands, created an appearance of authority which, according to the prevailing usages, included the right to let.

### Husband and wife

A wife living with her husband has the implied authority of the husband to buy articles of household necessity. In the striking words of Hornby: "As long as people continue to live in houses, the wife will normally do the household shopping, and the husband will pay the bills.... The law of principal and agent will always cut deeply into the law of husband and wife."<sup>80</sup>

A wife's implied authority to bind her husband by her credit purchases is, however, subject to some important limitations. In the first place, it is necessary that the husband and wife should be living together. If the wife is living apart from the husband without his fault and if she has been left unprovided for, she may become an agent of necessity of her husband to pledge his credit to the extent to which a reasonable maintenance makes it necessary, but she will not be an implied agent.<sup>81</sup>

Secondly, they must be living together in a domestic establishment of their own. "The mere fact of marriage does not make the wife an agent in law of her husband"; nor the fact of living together is sufficient. There must be a domestic establishment of which the wife is the incharge. If there is a domestic establishment of which a person is acting as the manager, the

79. *Kasinath Das v Nisakar Rout*, AIR 1962 Ori 164. See also *Gaya Sugar Mills Ltd v Nand Kishore Bijoria*, AIR 1955 SC 441.

80. THE PRINCIPLES OF AGENCY (1952) 32.

81. A wife who went away to live apart from the husband because of his bringing second wife into the home was held to be not justifiably living apart. *Nathubhai v Jauher Raiji*, ILR (1876) 1 Bom 121. A woman purchasing in her own right does not purchase as a representative, the husband not liable. *Kanhayalal Bisandayal Bhiwapurkar v Indarchandji Hamirmalji Sisodia*, AIR 1947 Nag 48.

presumption of agency will arise even if that person is not the wife. This well-known principle was established in *Debenham v Mellon*:<sup>82</sup>

The defendant was the manager of a hotel, where his wife acted as the manageress. They lived together in the same hotel, but had no domestic establishment of their own. The wife incurred with a tradesman a debt for clothes, payment for which was demanded from the husband.

But he was held not liable, the court saying that the mere fact of cohabitation did not give rise to presumption of agency, unless it was in a domestic establishment.

If these conditions are fulfilled it is immaterial whether the tradesman did or did not know that the buyer was a married woman.<sup>83</sup>

Thirdly, the wife can run her husband into debt only for necessaries. "The domestic arrangement of the family being usually left to the control of the wife, her authority extends to all those matters which fall within her department, as, for example, the supply of provisions for the house, clothing for herself and things of that sort."<sup>84</sup> The word "necessaries" is no doubt not free from ambiguity. But it has been held to include articles suited to the style in which the husband chooses to live, because "the husband conducting himself in the manner of a wealthy man no doubt expects his wife to conduct herself in the manner of a wealthy man's wife".<sup>85</sup> But the wife cannot embark upon the purchase of things beyond the station in which they live.<sup>86</sup> Thus where the goods supplied to a wife included a gold pen and pencil, a sealskin cigar case, a sealskin tobacco pouch, a glove and a handkerchief, the husband was held not liable.<sup>87</sup>

Lastly, the husband will not be liable if he makes a reasonable allowance to his wife for her needs. Thus, for example, in *Girdhari Lal v W. Crawford*<sup>88</sup> the Allahabad High Court held that the husband will not be liable even if the fact of allowance is not known to the seller.

The husband can negative liability by proving—

- (1) that he expressly warned the tradesman not to supply goods on credit;<sup>89</sup>
- (2) that the wife was already supplied with sufficiency of the articles in question;
- (3) that the wife was supplied with sufficient means for the purpose of buying the articles without pledging the husband's credit.

Further, the (English) Matrimonial Proceedings and Property Act, 1970, which restricts the implied agency of wife, provides in Section 4(1) that:

82. (1880) LR 6 AC 24.

83. *Paquin Ltd v Beauclerk*, 1906 AC 148 (HL).

84. *Phillipson v Hayter*, (1870) LR 6 CP 38.

85. *Robert Simpson Co Ltd v Rugglas*, borrowed from 8 Can BR 722.

86. *Seymore v Kingscote*, (1922) 38 TLR 586.

87. *Phillipson v Hayter*, (1870) LR 6 CP 38.

88. ILR (1887) 9 All 147.

89. *Morel Bros & Co v Earl of Westmorland*, 1904 AC 11: (1900–03) All ER Rep 397 (HL).

“Any rule of law and equity conferring on a wife authority, as agent of necessity to her husband, to pledge his credit or to borrow money on his credit is hereby abolished.”

### *Husband not implied agent of wife*

A husband has no original, inherent or implied power to act as an agent for his wife. His authority can arise from an appointment as agent, expressly or impliedly, or by ratification by his wife of acts done by him on her behalf. Accordingly, a wife was held not liable on a contract made by her husband in her name and without her authority when she disaffirmed the contract within reasonable time after getting to know of it.<sup>90</sup> A husband has no implied authority to sell his wife's property.<sup>91</sup>

### **Agencies of necessity**

The reason for the agency of necessity has been thus stated by Story:<sup>92</sup> “Although the powers of the agents are, ordinarily, limited to particular acts; yet...extraordinary emergencies may arise, in which a person, who is an agent, may, from the necessities of the case, be justified in assuming extraordinary powers; and...his acts fairly done, under such circumstances, will be binding upon his principal.”

### *Originated with marine adventures*

The principal of agency of necessity was first applied to cases of marine adventures. Unforeseen emergencies may arise in the course of a marine adventure which may threaten the goods and the master of the ship is not able to communicate with the principal. In such circumstances the master gets the power and it is also his duty to sell the goods in order to save their value. The sale will bind the cargo owner. Initially it was supposed “that this doctrine of authority by reason of necessity is confined to certain well-known exceptional cases, such as those of the master of a ship or the acceptor of the bill of exchange for the honour of the drawer”. But in subsequent cases the same principle was applied to carriers by land. Thus, in *Sims & Co v Midland Rly Co*.<sup>93</sup>

A quantity of butter was consigned with the defendant railway company. It was delayed in transit owing to a strike. The goods being perishable the company sold them.

The sale was held binding on the owner. The company's action was justified by the necessities of the case and it was also not practicable to get instructions from the owner.

90. *K. Kasulu v Commission, Endowments Deptt*, 1986 Andh LT 44.

91. *Jawaharlal Daima & Co v Chinta Chittemma*, (1989) 1 An LT 335.

92. ON AGENCY (9th Edn) S. 141 as cited by McCARDIE J in *Prager v Blastpiel Stamp & Heacock Ltd*, (1924) 1 KB 566, 571.

93. (1913) 4 KB 103.

Similarly, in *Great Northern Rly Co v Swaffield*:<sup>94</sup>

A horse, having been consigned with the defendant-company, was not received by anyone at the destination. The company had no arrangement of its own to keep animals and, therefore, placed the horse with a livery stable-keeper.

The company's action was held to be reasonably necessary in the circumstances and, therefore, the company was allowed to recover the charges of the stable-keeper.

#### *And then became principle of general application*

"Thus the basic principle is a broad and useful one. It lies at the root of various classes of cases of which the carrier decisions are merely an illustration." The reason for this wide rule as to agency of necessity was thus stated by McCARDIE J in *Prager v Blastpiel Stamp & Heacock Ltd*:<sup>95</sup> "The object of common law is to solve difficulties and adjust relations in social and commercial life. It must meet, so far as possible, sets of facts abnormal as well as usual. It must grow with the development of the nation. It must face and deal with changing or novel circumstances. Unless it can do that it fails in its function and declines in its dignity and value. An expanding society demands an expanding common law."



#### *Pre-existing agency not necessary*

It was also supposed at one time that agency of necessity is confined to cases in which there is subsisting relationship of principal and agent and the agent, in some emergency, exercises an authority which is not expressly provided in the contract. For example, SCRUTTON LJ observed in *Jebara v Ottoaman*<sup>96</sup> that "the agency of necessity develops from an original and subsisting agency and only applies itself to unforeseen events not provided for in the original contract". According to him the principle would not apply "when there is no pre-existing agency, as in the case of a finder of perishable chattels or animals". Two cases have been usually cited in support of this proposition, namely, where the finder of a dog spent money on feeding it,<sup>97</sup> and a person spent money on rescuing logs from a river<sup>98</sup> and neither of them could claim a lien on the goods for his trouble and expense. BOWEN LJ observed in one of the cases on the subject that "liabilities are not to be forced upon people behind their backs, any more than you can confer a benefit upon a man against his will".<sup>99</sup> The case where help is volunteered by a pure stranger are covered in Roman law by the doctrine of

94. (1874) LR 9 Exch 132.

95. (1924) 1 KB 566.

96. (1927) 2 KB 254, 257 (CA), reversed sub nom. *Ottoman Bank v Jebara*, 1928 AC 269.

97. *Binstead v Buck*, (1776) 2 Wm Bl 117: 96 ER 660.

98. *Nicholson v Chapman*, (1793) 2 Hy Bl 254.

99. *Falcke v Scottish Imperial Insurance Co*, (1886) LR 34 Ch D 234 (CA).

*Negotiorum Gestio.*<sup>100</sup> Referring to this doctrine it is observed in Anson's LAW OF CONTRACT:<sup>101</sup> "Our law does not recognise the *negotiorum gestor* of Roman law—the man who voluntarily spends his own money upon the necessary protection of the property of another."

This may be the general principle of English law. But exceptions have been admitted. A person who carries on salvage at sea is entitled to his compensation from the person whose property has been salvaged.<sup>102</sup> Similarly, where a bill of exchange has been dishonoured either by non-acceptance or by non-payment, any person may honour it by acceptance or payment for protecting the honour of the drawer and may subsequently recover from such person. But it has been pointed out by Lord GODDARD CJ in *Sacha v Milkos*<sup>103</sup> "that the court should be slow to increase the classes of those who can be looked upon as agents of necessity in selling or disposing of other people's goods without the authority of the owners".

"In the United States it is fairly clear law that a finder of lost goods is entitled to recover from the owner his necessary and reasonable expenses incurred in the successful recovery and preservation of the goods."<sup>104</sup> In India a finder has no right of action, but he is entitled to lien unless his lawful charges are paid. He has also a limited right of sale. [S. 177]

### *Relief of injured persons*

Another occasion for a person to act as an agent of necessity arises when an injured person is in urgent need of medical attendance. Any person acting on his behalf may call the services of a doctor; or any doctor may volunteer his services. The person benefited is bound to pay the charges of the service. Williston in his article on *Agency of Necessity*<sup>105</sup> cites the following cases as an illustration of the principle:

In *Matheson v Smiley*<sup>106</sup> the Manitoba Court of Appeal held that a surgeon was entitled to recover from the deceased man's estate reasonable remuneration for his services when he had, without request, given aid to a man who had attempted suicide.

### *Conditions for application of the principle*

The conditions which enable a person to act as an agent of necessity of another have been stated by McCARDIE J in *Prager v Blastpiel Stamp & Heacock Ltd.*<sup>107</sup>

100. Meaning of the phrase, Walter B. Williston, *Agency of Necessity*, (1944) 22 Can BR 492.

101. (22nd Edn by Guest, 1964) 535.

102. *The Five Steel Barges*, (1890) 15 PD 142.

103. (1948) 2 KB 23, 36 (CA).

104. Williston, *Agency of Necessity*, (1944) 22 Can BR 492, 504 and the authorities cited there.

105. (1944) 22 Can BR 492, 506.

106. (1932) 2 DLR 781.

107. (1924) 1 KB 566, 571-72; 1924 All ER Rep 524.

**INABILITY TO COMMUNICATE WITH PRINCIPAL.**—“In the first place, it is of course clear that agency of necessity does not arise if the agent can communicate with his principal. The basis of this requirement is that if the principal’s directions can be obtained the agent should ask it before acting.” A well-known illustration is *Gwilliam v Twist*.<sup>108</sup>

While the defendants’ omnibus was being driven by their servant, a policeman, thinking that the driver was drunk, ordered him to discontinue driving, the omnibus being then only a quarter of a mile from the defendants’ yard. The driver and the conductor then authorised a person who happened to be standing by to drive the omnibus home. That person through his negligence injured the plaintiff.

The plaintiff’s action against the owners failed, because the defendants might have been easily communicated with and, therefore, there was no necessity for their servants to employ another person.

**ACT SHOULD BE REASONABLY NECESSARY.**—“In the next place, it is essential for the agent to prove that the sale was necessary. What does this mean?”<sup>109</sup> LINDLEY LJ observed in a case that “by necessary is meant reasonably necessary and in considering what is reasonably necessary every material circumstances must be taken into account, e.g. danger, distance, accommodation, expense, time and so forth”.<sup>110</sup> *Sacha v Milkos*<sup>111</sup> is an illustration explaining absence of necessity:

The defendant allowed the plaintiff to store certain furniture in his house free of charge. Thereafter they lost touch with each other. Some three years later the defendant needed the space taken up by the furniture and wrote two letters to the plaintiff at an address supplied by his bank, but received no reply. His attempt to reach the plaintiff by telephone also failed. He then sold the furniture. Six years later the plaintiff claimed the furniture.

It was held that those facts gave rise to no agency of necessity since they exhibited nothing in the nature of an emergency compelling the defendant to sell the furniture. As to the question of damages the court pointed out that if the plaintiff received the letters, he would be entitled to recover only the actual sale proceeds of the furniture. But that if he did not receive the letters, he would be entitled to compensation for the increased value of furniture between the date of sale and his discovery of it.

A year later the same court faced another problem of the same kind in *Munro v Willmott*.<sup>112</sup>

108. (1895) 2 QB 84 (CA).

109. McCARDIE J in *Prager v Blastpiel Stamp & Heacock Ltd*, (1924) 1 KB 566.

110. *Phelps James & Co v Hill*, (1891) 1 QB 605, 610–11 (CA).

111. (1948) 2 KB 23 (CA).

112. (1949) 1 KB 295.

The plaintiff left her car in the defendant's yard without payment. The storage was intended to be for a short time, but the car remained there for several years. It became an obstacle owing to the conversion of the yard into a garage. After unsuccessful efforts to communicate with the plaintiff the car was repaired and sold.

The court held that the facts showed no emergency which would have entitled the defendant to sell as an agent of necessity.

Another interesting decision is *Prager v Blastpiel Stamp & Heacock Ltd.*<sup>113</sup>

During the First World War the defendant purchased for the plaintiffs, as their agents, fur skins to be despatched to Romania. Owing to the occupation of Romania by German forces it became impossible for the defendants to send the skins or any communication to the plaintiffs. In the last year of the war, the defendants sold the skins.

When peace returned the plaintiffs claimed their goods. The defendants sought to justify their action under the principle of agency of necessity. But the court held that there was no necessity to sell the goods. They had been purchased by the plaintiff in time of war in the hope of receiving them when peace arrived. The goods being dressed furs were not likely to deteriorate if care was used.

**BONA FIDE IN THE INTEREST OF PARTY CONCERNED.**—“In the third place, an alleged agent of necessity must satisfy the court that he was acting *bona fide* in the interest of the parties concerned. In *Tronson v Dent*,<sup>114</sup> the Privy Council plainly indicated that *bona fides* was essential in addition to actual necessity.”<sup>115</sup>

### Relations of principal and agent

#### DUTIES OF AGENT

Mutual rights and duties of principal and agent may be wholly provided for in their contract. But the following duties of general nature are imposed by law upon every agent, unless they are modified or excluded by special contract.

##### 1. Duty to execute mandate

The first and the foremost duty of every agent is to carry out the mandate of his principal. He should perform the work which he has been appointed to do. Any failure in this respect would make the agent absolutely liable for the principal's loss. Thus it has been held in a number of cases that: “The rule of equity is, that if an order is sent by a principal to a factor to make an

113. (1924) 1 KB 566; 1924 All ER Rep 524.

114. (1853) 8 Moo PC 419, 452.

115. See also LINDLEY LJ in *Phelps James & Co v Hill*, (1891) 1 QB 605, 611–12 (CA).

insurance, and he charges his principal, as if it was made, if he never in fact made that insurance, he is considered as the insurer himself.”<sup>116</sup>

In such cases the agent is held liable to the principal for the amount which would have been recovered if the goods had been insured.<sup>117</sup> Thus, for example, in *Pannalal Jankidas v Mohanlal*:<sup>118</sup>

A commission agent purchased goods for his principal and stored them in a godown pending their despatch. The agent was under instruction to insure them. He actually charged the premium for insurance, but failed to insure the goods. The goods were lost in an explosion in the Bombay harbour.

The agent was held liable to compensate the principal for his loss minus the amount received under the Bombay Explosion (Compensation) Ordinance, 1944, under which the Government paid compensation up to fifty per cent in respect of the uninsured merchandise lost in the explosion.<sup>119</sup>

## 2. Duty to follow instructions or customs [S. 211]

**S. 211. Agent's duty in conducting principal's business.**—An agent is bound to conduct the business of his principal according to the directions given by the principal, or in the absence of any such directions, according to the custom which prevails in doing business of the same kind at the place where the agent conducts such business. When the agent acts otherwise, if any loss be sustained, he must make it good to his principal, and if any profit accrues, he must account for it.

### *Illustrations*

- (a) A, an agent engaged in carrying on for B a business, in which it is the custom to invest from time to time, at interest, the moneys which may be in hand, omits to make such investment. A must make good to B the interest usually obtained by such investments.
- (b) B, a broker, in whose business, it is not the custom to sell on credit, sells goods of A on credit to C, whose credit at the time was very high. C, before payment, becomes insolvent. B must make good the loss to A.

Section 211 provides that an agent is bound to conduct the business of his principal according to the directions given by the principal and to keep himself within the confines of his authority. For example, an estate agent cannot make a binding contract on behalf of his principal with a third party.<sup>120</sup> In the absence of directions, the agent has to follow the custom which prevails in businesses of the same kind and at the place where the agent conducts such businesses. When the agent acts otherwise, if any loss be sustained,

116. Lord Chancellor in *Tichel v Short*, (1750) 2 Ves Sen 239: 28 ER 154. Adopted by the Supreme Court in *Pannalal Jankidas v Mohanlal*, AIR 1951 SC 144, 146: 1950 SCR 979: (1951) 21 Comp Cas 1.

117. See *Smith v Lascelles*, (1788) 2 TR 187: 1 RR 457 cited by the Supreme Court, *ibid.*

118. AIR 1951 SC 144: 1950 SCR 979: (1951) 21 Comp Cas 1.

119. See also Illustration (d) to S. 212 and *Savoy Solvent Oil Extraction Ltd v Indian Bank*, (1996) 2 An WR 184, failure of the person under duty to ensure, liability.

120. *John v Philip*, (1987) 2 KLT 50 (SN).

he must make it good to his principal, and, if any profit accrues, he must account for it.<sup>121</sup> [S. 212] Thus, for example, in *Lilley v Doubleday*:<sup>122</sup>

An agent was instructed to warehouse his principal's goods at a particular place. He placed a part of them at a different warehouse which was equally safe. But the goods were destroyed without negligence.

The agent was held liable for the loss. Any disobedience of, or departure from, the instructions makes the agent absolutely liable for the loss.<sup>123</sup>

Where a principal had given instructions of ambiguous nature which were capable of two meanings, he was not permitted to argue as against the agent that he should have read the instruction in the other sense than what he actually did.<sup>124</sup>

In the absence of instructions, business customs must be followed. Where, for example, the customs of a particular trade require that goods should not be sold on credit or in return for a negotiable instrument, the agent should not do so. If he does so, he would be liable to the principal for any loss resulting from the transaction.<sup>125</sup> In reference to a broker the importance of acting according to customs was highlighted in the following words:<sup>126</sup> "Brokers employed to sell goods are bound to do so in the usual way, and if it is usual to send the seller an estimate of value in order that he may be enabled to fix a reserve price, they ought to do so; and whether it is so or not they are bound for their own guidance to make a careful estimate of the value; and if they sell, even by public auction at a price much below their fair value, then not having made such an estimate, will be evidence of negligence, and if a loss is caused thereby, they will be liable."

Where a booking agent did not prepare the airway bill with proper skill and diligence inasmuch as the relevant boxes relating to the items as to 'cash on delivery' and collection of charges by the carrier were left blank by him,

121. See KANIA CJ in *Pannalal Jankidas v Mohanlal*, AIR 1951 SC 144, 147.

122. (1881) LR 7 QBD 510. "Where the act which an agent is employed to perform is one which by law is void (such as the making of a wagering contract), the principal cannot recover damages for the failure to perform it." CHITTY ON CONTRACTS (24th Edn, 1977) 51, para 2095. Citing *Cheshire & Co v Vaughan Bros & Co*, (1920) 3 KB 240.

123. See further *Bostock v Jardine*, (1865) 3 H&C 700: (1865) 159 ER 707, an agent authorised to buy cotton, bought for the principal and divers others in one large-scale contract so that the principal had no particular contract to enforce, held bound to refund principal's money; *National Coffee Palace Co, re, Panmure, ex p*, (1883) LR 24 Ch D 367 (CA), purchasing shares of companies other than those directed.

124. *Ireland v Livingston*, (1866) LR 2 QB 99: (1872) 27 LT 79. Where the directors of a company were instructed to purchase a business as it then stood, they were held not liable when the business turned out to be insolvent. It was an imprudent instruction on the part of the principal. *Overend & Gurney Co v Gibb*, (1872) LR 5 HL 480.

125. *Ferrier v Robbins*, (1835) 2 CM & R 152.

126. *Soloman v Barker*, (1862) 2 F&F 726: 121 RR 828, the broker sold goods at an inadequate price whereas he was under a duty to sell at a value in accordance with the customs of the particular trade, held liable for the principal's loss. *Paul Beier v Chotalal Javerdas*, ILR (1904) 30 Bom 1, customs of the place of business.

he being in breach of duty, he was not allowed to recover his expenses in arranging consignment of the goods.<sup>127</sup>

Akin to this is the duty to maintain the business secrets of the principal. A bank is under a similar duty of secrecy so far as the customer's dealings with him are concerned and would be liable in damages if any loss is caused to the customer by leakage of secret information. Certain currency notes were deposited with a bank for demonetisation. The bank informed the Income Tax Authorities and the customer thereby lost the utilisation of that money. Even so the customer's action against the bank failed. The bank was under a higher national duty which superseded the duty to the customer.<sup>128</sup>

An agent is also under a duty to maintain confidence, secrecy and non-disclosure of any sensitive information about the affairs of his principal. A banker may be liable if the state of his customer's account is leaked, except where the disclosure is under compulsion of law, e.g., duty to obey an order under Bankers' Books Evidence Act, or under higher duty owed to State or public institutions which supersedes lower duty or under any statement in a formal claim or with customer's permission.<sup>129</sup>

### 3. Duty of reasonable care and skill [S. 212]

**S. 212. Skill and diligence required from agent.**—An agent is bound to conduct the business of the agency with as much skill as is generally possessed by persons engaged in similar business, unless the principal has notice of his want of skill. The agent is always bound to act with reasonable diligence, and to use such skill as he possesses; and to make compensation to his principal in respect of the direct consequences of his own neglect, want of skill or misconduct, but not in respect of loss or damage which are indirectly or remotely caused by such neglect, want of skill, or misconduct.

#### *Illustrations*

- (a) A, a merchant in Calcutta, has an agent, B, in London, to whom a sum of money is paid on A's account, with orders to remit. B retains the money for a considerable time. A, in consequence of not receiving the money, becomes insolvent. B is liable for the money and interest from the day on which it ought to have been paid, according to the usual rate, and for any further direct loss—as e.g., by variation of rate of exchange—but not further.
- (b) A, an agent for the sale of goods, having authority to sell on credit, sells to B on credit, without making the proper and usual enquiries as to the solvency of B. B, at the time of such sale, is insolvent. A must make compensation to his principal in respect of any loss thereby sustained.
- (c) A, an insurance-broker employed by B to effect an insurance on a ship, omits to see that the usual clauses are inserted in the policy. The ship is afterwards lost. In consequence of the omission of the clauses nothing can be recovered from the underwriters. A is bound to make good the loss to B.

127. *Sinclair Freight and Chartering Consultants (P) Ltd v Fiel Traders*, AIR 1987 Cal 201.

128. *Shankarlal Agarwalla v SBI*, AIR 1987 Cal 29.

129. *Ibid.*

- (d) A, a merchant in England, directs B, his agent at Bombay, who accepts the agency, to send him 100 bales of cotton by a certain ship. B, having it in his power to send the cotton, omits to do so. The ship arrives safely in England. Soon after her arrival the price of cotton rises. B is bound to make good to A the profit which he might have made by the 100 bales of cotton at the time the ship arrived, but not any profit he might have made by the subsequent rise.

Thus every agent is bound to carry on the business of agency with reasonable skill and care.<sup>130</sup> For example,<sup>131</sup> a bank was instructed by the plaintiff to collect a certain amount on his behalf and to remit it to him. There was no specific instruction as to the manner of remittance. The bank sent the amount by draft placed in a letter sent by ordinary post. The bank was held negligent in sending the amount like that. Certain cheques were paid into a bank for collection. The bank sent them to the drawee bank for collection, but they were lost in transit. The bank was held liable to the customer for the principal value of the cheques.<sup>132</sup>

The standard of care and skill which an agent has to bestow depends upon the nature of his profession.<sup>133</sup> An agent, having authority to sell on credit, must take care to ascertain the solvency of his buyer. An insurance broker must see that usual clauses for the protection of the principal are inserted in the policy. An estate agent should know the land laws and also must take care to ascertain the solvency of the tenant.<sup>134</sup> If an agent is retained for assisting his principal for lending money on a mortgage, he must make reasonable inquiry about the value of the property.<sup>135</sup> A stockbroker should know the regulations of the stock exchange. An agent should command enough legal knowledge to sufficiently and adequately safeguard the interests of the principal in the course of the agency.<sup>136</sup> He may become answerable for the incompetence of the labour employed by him.<sup>137</sup>

If the principal suffers any loss owing to the agent's want of care or skill, the agent must compensate the principal for such loss. Section 212 limits the agent's liability to "direct consequences".<sup>138</sup> It provides that the agent must "make compensation to his principal in respect of the direct consequences of his own neglect, want of skill or misconduct, but not in respect of loss

130. Duties and liabilities are the same whether the agent is working for consideration or without it. *Agnew v Indian Carrying Co*, (1865) 2 Mad HC Cases 449.

131. *Bank of Bihar Ltd v Tata Scob Dealers (Controlled Stock) Calcutta Ltd*, AIR 1960 Cal 475. If he satisfies the required standard, he is not liable for the principal's loss, if any, and it would be no cause of action that the loss could have been avoided if the agent had acted differently. *Raja Ram v Abdul Rashim*, (1973) 9 SLR 77: (1915) 31 IC 450; *Lagunas Nitrate Co v Lagunas Syndicate*, (1899) 2 Ch 392 (CA).

132. *State Bank of Indore v National Textile Corp*n, (2004) 4 MPLJ 214.

133. Every person who acts as a skilled agent is duty-bound to exercise reasonable skill and knowledge in the performance of his duty. *Pandurang v Jairamdas Pandurang*, AIR 1925 Nag 166; *Lee v Walker*, (1872) LR 7 CP 121.

134. *Heys v Tindal*, (1861) 1 B&S 296.

135. *Baxter v F. W. Gapp & Co Ltd*, (1939) 2 KB 271 (CA).

136. *Park v Hammond*, (1816) 6 Taunt 495: 128 ER 1127.

137. *Nagendra Nath v Nagendra Bala*, AIR 1929 Cal 988.

138. *Krishna Chandra Ganpati v K. Hanumantha Rao*, AIR 1950 Ori 241.

or damage which are indirectly or remotely caused by such neglect, want of skill or misconduct". If, for example, an agent fails to send the principal's money in time, he may be liable for the money and the loss of interest, but not if the principal becomes insolvent by that reason. An example of direct loss is to be seen in the facts of *Keppel v Wheeler*<sup>139</sup>. An agent was appointed to sell a house. He received an offer which he promptly communicated to his principal. The latter accepted it provisionally "subject to contract". Subsequently the agent received a higher offer which he failed to pass on to the principal. This resulted in final acceptance of the first offer in ignorance of the second. The agent was held liable to make good the principal's loss in terms of the difference in the two prices.

The meaning of the expression "direct consequences" has been explained by the Supreme Court in *Pannalal Jankidas v Mohanlal*<sup>140</sup>:

An agent, having been instructed to insure certain goods, failed to do so. The goods were lost in an explosion at the docks. Even if the agent had taken out a fire insurance policy in the usual form it would not have covered a loss of this kind, as fire due to explosion would have been an excepted peril. But the Bombay Government passed an ordinance under which it undertook to pay half loss in cases of uninsured goods. Thus the principal got only half of what he would have got if the goods had been insured.



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The agent contended that as the passing of the Ordinance could not have been anticipated, the loss was too remote. But, it was held by a majority, that the loss was the direct result of the agent's negligence. Their Lordships, following English decisions,<sup>141</sup> felt that the intervention of the Government Ordinance did not break the chain of causation. KANIA CJ said: "Once misconduct is admitted or proved the fact that the Ordinance did not exist and could not have been in the contemplation of the parties is irrelevant for deciding the question of liability."

In cases of difficulty the agent's duty is to use all reasonable diligence in communicating with his principal, and in seeking to obtain his instructions, if the principal can be communicated with by reasonable care, before taking any steps in facing the difficulty or emergency.<sup>142</sup>

**S. 214. Agent's duty to communicate with principal.**—It is the duty of an agent, in cases of difficulty, to use all reasonable diligence of communicating with his principal, and in seeking to obtain his instructions.

Where the agent informed his principal that purchases have been effected on his behalf and subsequently confirmed it by reporting that the goods

139. (1927) 1 KB 577.

140. AIR 1951 SC 144; 1950 SCR 979.

141. The following English decisions bearing on the question were considered: *Polemis and Furness Withy & Co, re*, (1921) 3 KB 560 (CA); *Liesbosch Dredger v S S Edison*, 1933 AC 449.

142. For example, in selling shares otherwise than as directed. *Buddulal Goerlal Mahajan v Shrikisan Chandmal*, AIR 1961 MP 57, 61; *Pani Bai v Sire Kanwar*, AIR 1981 Raj 184.

would be despatched as soon as transport strike was over whereas he had done nothing in the matter, it was held by the Supreme Court that such a neglect and misconduct of the agent misinforming the principal was squarely within the wide terms of Section 212. “He must bear the brunt to pay damages,” the court said.<sup>143</sup>

#### 4. Duty to avoid conflict of interest

**S. 215. Right of principal when agent deals, on his own account, in business of agency without principal's consent.**—If an agent deals on his own account in the business of the agency, without first obtaining the consent of his principal and acquainting him with all material circumstances which have come to his own knowledge on the subject, the principal may repudiate the transaction; if the case shows, either that any material fact has been dishonestly concealed from him by the agent, or that the dealings of the agent have been disadvantageous to him.

##### *Illustrations*

- (a) A directs B to sell A's estate. B buys the estate for himself in the name of C. A, on discovering that B has bought the estate for himself, may repudiate the sale, if he can show that B has dishonestly concealed any material fact, or that the sale has been disadvantageous to him.
- (b) A directs B to sell A's estate. B, on looking over the estate before selling it, finds a mine on the estate which is unknown to A. B informs A that he wishes to buy the estate for himself, but conceals the discovery of the mine. A allows B to buy in ignorance of the existence of the mine. A, on discovering that B knew of the mine at the time he bought the estate, may either repudiate or adopt the sale at his option.

**S. 216. Principal's right to benefit gained by agent dealing on his own account in business of agency.**—If an agent, without the knowledge of his principal, deals in the business of the agency on his own account instead of on account of his principal, the principal is entitled to claim from the agent any benefit which may have resulted to him from the transaction.

##### *Illustration*

A directs B, his agent, to buy a certain house for him. B tells A it cannot be bought, and buys the house for himself. A may, on discovering that B has bought the house, compel him to sell it to A at the price he gave for it.

An agent occupies fiduciary position and, therefore, it is his duty not to do anything which would bring his personal interest and his duty to the principal in conflict with each other. This conflict invariably arises when the agent is personally interested in the principal's transaction, for example, where he himself buys the property he is appointed to sell or delivers his own goods when he is instructed to buy on behalf of the principal. A stockbroker was employed to buy some shares for his principal. He submitted to his

143. *Jayabharathi Corp v Sv.P.N.Sn. Rajesekara Nadar*, 1993 Supp (1) SCC 401: AIR 1992 SC 596. *Sushila Devi v State of Bihar*, 2005 AIHC 1514 (Pat), the matter of information in connection with an accident was being handled by the police. Information of death to the police was attributed to the insurer.

principal for signature certain papers which showed that the purchase was being effected in the market. But, in fact, the agent was transferring his own shares to the principal. The principal was allowed to claim rescission.<sup>144</sup> A well-known illustration is the case of *De Busche v Alt*:<sup>145</sup>

The plaintiff consigned a ship to a company in China for sale "at £90,000 payable in cash". With the consent of the plaintiff the company appointed the defendant, a Japanese agent, to sell the ship. The defendant attempted to sell the ship, but having failed to find a customer, bought the ship himself and without disclosing this, remitted the above sum through the company to the plaintiff. Soon thereafter a war broke out and ships were again in great demand. A Japanese prince bought it from the defendant at £1,60,000. The plaintiff sued the defendant to recover the profit made on resale.

He was held bound to account for the profit. There would have been nothing wrong if the agent had bought the ship after disclosing the fact to his principal. The agent might have been honest in this particular case. But if his contention was accepted, many an agent would make secret profits by feigning inability to sell.<sup>146</sup>

The principle is incorporated in Section 215, which provides that if an agent deals on his own account in the business of agency, without first obtaining the consent of his principal and acquainting him with full facts, the principal may repudiate the transaction if he can show that—

- (a) a material fact has been dishonestly concealed from him, or
- (b) the dealing of the agent has been disadvantageous to him.<sup>147</sup>

The first illustration to the section says that if the agent has secretly bought the principal's property for himself, the principal may repudiate the transaction if he can show that the agent has concealed any material fact or that the sale has been disadvantageous to him. Where, for example, the agent discovers a mine on the principal's estate and without disclosing this fact buys the estate for himself, the principal may repudiate the transaction. The mere fact of the agent buying the principal's property brings his interest in conflict with his duty to the principal and, therefore, it has been pointed out that the conflict is in itself a sufficient disadvantage to the principal.<sup>148</sup>

144. *Armstrong v Jackson*, (1917) 2 KB 822. WILLIES J observed in *Mollett v Robinson*, (1870) LR 5 CP 646, 655 that "it is an axiom of the law of principal and agent that a broker employed to sell cannot himself become the buyer without distinct notice to the principal so that the latter may object to it if he thinks proper".

145. (1878) LR 8 Ch D 286.

146. The principle is applicable even where there is a mere possibility of conflict and the agent acts in good faith. *Boardman v Phipps*, (1967) 2 AC 46: (1966) 3 WLR 1009 (HL).

147. Detriment of the principal is a question of fact. *Firm of Rameshidas Benarashidas v Tansookhrai Bashesbarilal Firm*, AIR 1927 Sind 195. Repudiation by the principal must be within reasonable time after discovering the facts. *Armstrong v Jackson*, (1917) 2 KB 822: (1916-17) All ER Rep 1117.

148. See, for example, *Janakidas v Dhumanmal*, AIR 1917 Sind 5. But it has been held in *Mamchand v Chajuram & Sons*, (1937) 169 IC 827, that some disadvantage in addition to

### 5. Duty not to make secret profit

Another aspect of this principle is the duty of the agent not to make any secret profit in the business of agency. His relationship with the principal is of fiduciary nature and this requires absolute good faith in the conduct of agency. What is meant by secret profit? It means any advantage obtained by the agent over and above his agreed remuneration and which he would not have been able to make but for his position as agent. Acceptance of bribe is a profit of this kind, even "if the employers are not actually injured, and the bribe fails to have the intended effect".<sup>149</sup> A military officer who took bribe and allowed goods to pass under the authority of his uniform, was held liable to account for the same to the Crown.<sup>150</sup> Similarly, where an auctioneer received from the buyer commission in addition to what his principal paid him, he was held bound to hand over the commission to the principal.<sup>151</sup>

Where an agent sells his own stock to the principal without disclosing the fact, he is bound to account for any profit he made in the transaction. It is immaterial that the agent charged only the prevailing market price.<sup>152</sup> A principal agreed to buy horses from a dealer provided that his veterinary surgeon would pass them as sound. The seller bribed the surgeon and obtained his certificate. The horses turned out to be unsound. The principal was held justified in rejecting them and countermanding the cheque which he had issued for the price.<sup>153</sup>

Knowledge which is acquired by an agent in the course of the business of agency and which he converts into advantage does not require accountability if the agent neither uses the principal's property in the process nor diverts his business opportunities.<sup>154</sup>

As a part of the agent's duty to be honest to his principal, it is necessary that the agent should not disclose any confidential information received by

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this bare conflict must be shown. *Grant v Gold Exploration and Development Syndicate Ltd*, (1900) 1 QB 233 (CA), an agent for sale and purchase cannot act for the other party at the same time or take a commission from him unknown to the principal. *Nabi Khan v Roofdar*, AIR 2010 Raj 128, agent appointed to sell land, sold it below natural price and that too to his own father, thus self-dealing, recovery of property by the principal ordered.

149. *Harrington v Victoria Graving Dock Co*, (1878) LR 3 QBD 549.

150. *Reading v Attorney General*, 1951 AC 507 (HL).

151. *Andrews v Ramsay & Co*, (1903) 2 KB 635.

152. *Bentley v Craven*, (1853) 18 Beav 75: 104 RR 373. See S. 216 and its illustration.

153. *Shipway v Broadwood*, (1899) 1 QB 369 (CA). The principal is entitled to claim interest on the illicit profits made by the agent. *Tota Ram v Kunwar Zalim Singh*, AIR 1940 All 69, following *Regier v Campbell Stuart*, (1939) 1 Ch 766, the agent forfeits his commission. *Andrews v Ramsay & Co*, (1903) 2 KB 635, by taking bribe; the section gives option to the principal to avoid the transaction in reference to the third party or to affirm it and hold the agent liable for his breaches. *Vinayak Rao v Ransordas*, (1870) 7 BHC (OC) 90; *Joachinson v Meghjee Vallabhdas*, ILR (1910) 34 Bom 292; *Haslam and Hier-Evans, re*, (1902) 1 Ch 765 (CA), recovery of commission from solicitor.

154. *Nordisk Insulinlaboratorium v Gorgate Products Ltd*, 1953 Ch 430: (1953) 2 WLR 879 (CA); *Aas v Benham*, (1891) 2 Ch 244 (CA).

him from his principal. If he does so, the principal may terminate the contract and hold the agent liable in damages for his loss, if any.<sup>155</sup>

## 6. Duty to remit sums [S. 218]

**S. 218. Agent's duty to pay sums received for principal.**—Subject to such deductions,<sup>156</sup> the agent is bound to pay to his principal all sums received on his account.

The agent is bound to pay to his principal all sums received on his account. The agent is, however, entitled to deduct his lawful charges, but subject only to this right, the principal's money must be remitted to him even if it has been received in pursuance to a void or illegal contract. The agent has to perform this duty even if his earnings for the principal flow out of void or illegal transactions. "If an agent receives money on his principal's behalf under an illegal and void contract, the agent must account to the principal for the money so received and cannot set up the illegality of contract as a justification for withholding payment, which illegality the other contracting party has waived by paying the amount."<sup>157</sup>

The agent has the right to make a counter claim. The Bombay High Court did not consider it fair or in the interest of justice to compel the agent to deposit the amount in the court as a measure of protecting his principal, particularly when there was a claim against the claim.<sup>158</sup>

## 7. Duty to maintain accounts [S. 213]

**S. 213. Agent's accounts.**—An agent is bound to render proper accounts to his principal on demand.

Accounts are necessary for the proper performance of the agent's other duties, for example, the duty to remit sums to the principal.<sup>159</sup>

There is no provision in the Act enabling an agent to institute a suit for accounts against the principal. The Supreme Court in *Narandas Morardas Gajiwala v S.P.A.M. Papammal*<sup>160</sup> laid down that the provisions of the Contract Act are not exhaustive in this regard and that the right of an agent to sue the principal for accounts is an equitable right arising under special

155. *Harris (L.S.) Trustees Ltd v Power Packing Services Ltd*, (1970) 2 Lloyd's Rep 65. The agent can also be restrained by means of an injunction from disclosing confidence. *Anton Piller K.G. v Mfg Processes Ltd*, 1976 Ch 55: (1976) 2 WLR 162 (CA).

156. Deductions indicated in S. 217.

157. *Bhola Nath v Mul Chand*, ILR (1901–03) 25 All 639 (wagering transactions); *Palaniyappa Chettiar v Chockalingam Chattiar*, ILR (1921) 44 Mad 334. Illegal agency is itself not as such enforceable.

158. *National Shipping Co of Saudi Arabia v Sentrans Industries Ltd*, (2004) 2 Bom CR 1.

159. As a part of the obligation to render accounts the agent has to produce vouchers in support of expenditure incurred by him. See *S. Paul & Co v State of Tripura*, AIR 1984 Cal 378. The principal can recover from agent's estate anything that he can show to be due from the deceased agent. *R. Bhawani Singh v Misbah-ud-din*, (1929) 30 LW 21: AIR 1929 PC 119; *Purshotam Vasudeo v Ramkrishna Govind*, AIR 1945 Bom 21.

160. AIR 1967 SC 333.

circumstances. One of those special circumstances is where all the accounts are in the possession of the principal. In a case before the Madras High Court,<sup>161</sup> an agent was running a mill which was taken over by the owners. The agent claimed that he lost his accounts in the process of take-over and, therefore, claimed accounts from the principal. The court did not provide him any relief because he was not able to give any proof of the loss of his accounts. Where an agent was appointed to secure orders for supply of goods, his commission to be payable when the principal received payment for supplies, it was held that quite naturally an account would have to be maintained by the principal and the agent had the right to demand an account.<sup>162</sup> The same is the position where the accounts are so complicated that a suit for a definite sum of money is not possible. In cases where settlement of accounts alone can do complete justice between the parties, the agent can sue the principal for accounting even if he is having some evidence of the transaction with him.<sup>163</sup>

The Lahore High Court faced a case of this kind in *Ram Lal Kapur & Sons v Asian Commercial Assurance Co Ltd*<sup>164</sup> TAPP J observed: "The right to claim a statement of accounts is an unusual form of relief, only granted in certain specific cases and is only to be claimed when the relationship between the parties is such that this is the only relief which will enable the claimant to satisfactorily assert his legal rights."

In that case, the plaintiffs, who were insurance agents, were to be remunerated by a commission calculated on the premia paid on all policies effected or introduced through them. The court held that as the plaintiffs could not know which of the policies had lapsed, matured or forfeited, they were entitled to demand rendition of accounts.

The Sind High Court<sup>165</sup> explained the position in the following words:

"An agent has no statutory right to the account from his principal. Nevertheless where it is equitable from the particular circumstances and the relationship of the parties that one should account to the other, a suit for account will lie. If an agent can satisfy that all accounts are rightly in possession of the principal and that he (the agent) has not and could not have in his possession accounts which would enable him to determine his claim for commission against his principal, he will be entitled to sue for an account. But if it is found that the agent has no accounts because of his own failure or fault, he should not be granted the relief he claims, much less if it is found that he has accounts which he is withholding."

A suit by an agent against his principal for a specific sum of money is not a suit for accounts. It is only in exceptional cases where the agent's

161. *State of T.N. v S. Alagirsubramanian Chettiar*, AIR 1988 Mad 248.

162. *Saroj Kapur v Nitin Castings Ltd*, AIR 1987 Del 349.

163. *Thiruvenkidam v Quilon Pencil Factory*, (1990) 2 KLT 327.

164. AIR 1933 Lah 483.

165. *Gulabrai Dayaram v India Equitable Insurance Co Ltd*, AIR 1937 Sind 51.

remuneration depends on the extent of dealings which are not known to him or where he cannot be aware of the amount due to him unless the accounts of his principal are gone into, that a suit by an agent for accounts against his principal might be competent.<sup>166</sup>

The Division Bench of the Nagpur High Court allowed a sale pusher of books to know from his principal an account of the volume of sale induced by his efforts.<sup>167</sup>

The principle behind these rulings was affirmed by the Supreme Court in *Narandas Morandas Gajiwala v S.P.A.M. Papammal*.<sup>168</sup> The agent sued for an account and the principal sought enforcement of promissory note given by the agent to the principal. The court passed a decree on the promissory note subject to set-off for amounts due from the principal to the agent. The principal thus became accountable for those dues.<sup>169</sup>

#### *Inspection of agent's accounts.*

Conceding the right to the principal of inspecting his underwriting agent's computerised accounts, the court said: "That obligation to provide an accurate account in the fullest sense arises by reason of the fact that the agent has been entrusted with the authority to bind the principal to transactions with third parties and the principal is entitled to know what his personal contractual rights and duties are in relation to those third parties as well as what he is entitled to receive by way of payment from the agent. He is entitled to be provided with those records because they have been created for preserving information as to the very transactions which the agent was authorised by him to enter into.

Being the participant in the transactions, the principal is entitled to the records of them."<sup>170</sup>

Explaining the source of the agent's obligation to maintain accounts and to provide inspection the court held that the obligation to keep records and provide records to the principal arises out of the agency relationship and does not depend on that relationship having been created by contract. The duty would coexist with a contract of agency. The express arrangements for inspection do not oust this, though they qualify the implied duty, for instance, by relieving the agent of duty to deliver their original books, accounts and records.

The duty to provide access to the records survives the termination of the contract. It would be extremely inconvenient and potentially very damaging to the principal if the obligation does not survive termination of the

166. *Ramachandra Madhavadoss Co v Moovakat Moidunkutti Birankutti & Bros, Firm*, AIR 1938 Mad 707.

167. *Basant Kumar Mishra v Roshanlal Shrivastava*, AIR 1954 Nag 300.

168. AIR 1967 SC 333: 1966 SCR 38.

169. *State of T. N. v S. Alagirsubramanian Chettiar*, AIR 1988 Mad 248.

170. *Yasuda Fire and Marine Insurance Co v Orion Marine Insurance Underwriting Agency Ltd*, 1995 QB 174: (1995) 2 WLR 49.

contract. It is clear that there can be obligations under the contract which do survive its termination. The classic example is of course an agreement for arbitration.<sup>171</sup>

The principal specifically admitted that he was ready to settle all claims and liabilities. The court said that such claim revealed that there was necessity for rendition of accounts. Accounts were still not crystallised. The suit for rendition of accounts was maintainable.<sup>172</sup>

### 8. Duty not to delegate [S. 190]

*Delegatus non potest delegare* is a well-known maxim of the law of agency. The principal chooses a particular agent because he has trust and confidence in his integrity and competence. Ordinarily, therefore, the agent cannot further delegate the work which has been delegated to him by his principal.

It was laid down in *John McCain and Co v Pow*<sup>173</sup> that unless so authorised by the principal, an estate agent has no right to appoint a sub-agent and delegate to him his powers which require special skill and care. No implied authority could be pleaded. In this case the sub-agent effected a sale on his own account. The agent (plaintiff) had sued for his commission. The court negatived the claim as the contract of agency did not permit appointment of sub-agent.

This principle and its exceptions are stated in Section 190:

**S. 190. When agent cannot delegate.**—An agent cannot lawfully employ another to perform acts which he has expressly or impliedly undertaken to perform personally, unless by the ordinary custom of trade a sub-agent may, or, from the nature of the agency, a sub-agent must, be employed.

But there are exceptions. In the following cases the agent may delegate the work to another:

#### 1. Nature of work

Sometimes the very nature of work makes it necessary for the agent to appoint a sub-agent. For example, an agent appointed to sell an estate may retain the services of an auctioneer and the one authorised to file a suit may engage a lawyer. A banker instructed to make payment to a particular person at the particular place may appoint a banker who has an office at that place.<sup>174</sup> A banker authorised to let out a house and collect rents may entrust the work to an estate agent.<sup>175</sup>

171. *Heyman v Darwins Ltd*, (1942) AC 356.

172. *P.T. Mathew v Kerala SEB*, AIR 2014 NOC 588 (Ker).

173. (1974) 1 WLR 1643 (CA).

174. *Summan Singh v National City Bank of New York*, AIR 1962 Punj 172; ILR 1952 Punj 189.

175. *Mohinder v Mohan*, AIR 1939 All 188; *Union of India v Amar Singh*, AIR 1960 SC 233; (1960) 2 SCR 75, goods received from another railway, sub-agency not constituted; *Nagpur Electric Light and Power Co v R.B.S.R. Pandit*, AIR 1937 Nag 379, director of a company

## 2. *Trade custom*

Secondly, a sub-agent may be appointed and the work delegated to him if there is ordinary custom of trade to that effect. Thus architects generally appoint surveyors.<sup>176</sup>

## 3. *Ministerial action*

An agent cannot, of course, delegate acts which he has expressly or impliedly undertaken to perform personally, e.g., acts requiring personal or professional skill. But the agent may delegate acts which are purely ministerial in nature, e.g., authority to sign.<sup>177</sup>

## 4. *Principal's consent*

The principal may expressly allow his agent to appoint a sub-agent. His consent may also be implied from the conduct of the parties. The principal may ratify his agent's unauthorised delegation.

A person who is appointed by the agent and to whom the principal's work is delegated is known as "sub-agent". Section 191 defines "sub-agent" as "a person appointed by and acting under the control of the original agent in the business of the agency".

**S. 191. "Sub-agent" defined.**—A "sub-agent" is a person employed by, and acting under the control of, the original agent in the business of the agency.

In a case before the Supreme Court:<sup>178</sup>

A person had sent certain parcels by VPP to a destination in Pakistan. The articles reached Pakistan. They were delivered to the addressee and their value was collected. The Government of Pakistan, having snapped the postal treaty with the Government of India, did not forward the amount. The Indian Post Office could not pay to the sender. The sender sued the Government.

Holding the Government not liable, the court said that when two sovereign powers enter into a postal treaty, neither of them can be described as an agent of the other. Neither can be said to be employed or acting under the control of the other as required of a sub-agent under Section 191.

When a sub-agent is appointed, what relationship is constituted between the principal and the sub-agent and the agent? The answer depends upon whether the sub-agent has been properly or improperly appointed.

## 1. Improper delegation [S. 193]

**S. 193. Agent's responsibility for sub-agent appointed without authority.**—Where an agent, without having authority to do so, has appointed

appointing an advocate; *Ramdeo Tilokchand Agarwal v Lalu Natha*, AIR 1937 Nag 65, a general agent appointing an advocate for a suit.

176. *Moon v Witney Union*, (1837) 43 RR 802.

177. *Mason v Joseph*, (1804) 1 Smith KB 406.

178. *Union of India v Mohd Nazim*, (1980) 1 SCC 284: AIR 1980 SC 431.

a person to act as a sub-agent, the agent stands towards such person in the relation of a principal to an agent, and is responsible for his acts both to the principal and to third persons; the principal is not represented by or responsible for the acts of the person so employed, nor is that person responsible to the principal.

Delegation is improper when it is not authorised, that is, when it is not within any of the recognised exceptions. The effect is that the principal is not bound by the appointment. He is not represented by that person, nor bound by his acts. That person is also not responsible to the principal. But the agent will be responsible to the principal for any act of that person. The agent stands in the position of principal towards that person and is as such responsible for his acts to third parties.<sup>179</sup>

## 2. Proper delegation [S. 192]

**S. 192. Representation of principal by sub-agent properly appointed.**—Where a sub-agent is properly appointed, the principal is, so far as regards third persons, represented by the sub-agent and is bound by and responsible for his acts, as if he were an agent originally appointed by the principal.

**Agent's responsibility for sub-agent.**—The agent is responsible to the principal for the acts of the sub-agent.

**Sub-agent's responsibility.**—The sub-agent is responsible for his acts to the agent, but not to the principal, except in case of fraud or wilful wrong.

In *Calico Printers' Assn v Barclays Bank*<sup>180</sup> WRIGHT J explained the effect of proper delegation:

"Even where the sub-agent is properly employed, there is no privity between him and the principal; the latter is entitled to hold the agent liable for breach of the mandate, which he has accepted, and cannot, in general claim against the sub-agent for negligence or breach of duty."

The following effects of the appointment are stated in Section 192:

### 1. Principal represented by sub-agent

In the first place, so far as regards third persons, the principal is represented by the sub-agent. He is bound by and responsible for his acts as if he were an agent originally appointed by the principal.<sup>181</sup>

179. A person who was appointed as a sole agent was held to have no authority to delegate. *McCann John & Co v Pow*, (1974) 1 WLR 1643 (CA).

180. (1931) 145 LT 51 (CA). A similar explanation occurs in *Mercantile Bank of India Ltd v Chetumal Bulchand*, AIR 1930 Sind 247, 250; *Indian Airlines v Renu Gupta*, AIR 2007 (DOC) 116: (2006) 3 CPR 201, Indian Airlines sells tickets to its consumers through its agents. One of them failed to inform the buyer of change in time of departure with the result that the consumer had to wait for 6–7 hours. The Airlines was held vicariously liable for deficiency of service by agent.

181. See also *Raghunath Prasad v Seva Ram Tikam Das*, AIR 1980 All 15.

## 2. Agent's responsibility for sub-agent

Secondly, the agent is responsible to the principal for the acts of the sub-agent. If, for example, the sub-agent has misappropriated the principal's property or its sale-proceeds, the agent is responsible for the same. There is no privity of contract between the principal and the sub-agent and, therefore, he cannot sue the sub-agent, except for fraud or wilful wrong. Even where fraud or wilful wrong is established the principal has the choice to sue either the agent or the sub-agent.<sup>182</sup> But the agent may exempt himself from such liability.<sup>183</sup>

## 3. Sub-agent's liability to principal

The sub-agent is not directly liable to the principal, except for fraud and wilful wrong. A well-known illustration is *Calico Printers' Assn v Barclays Bank*<sup>184</sup>.

A sub-agent failed to insure the principal's goods, which were destroyed by fire. But the principal could not recover against the sub-agent.

Similarly, in *Summan Singh v N.C. Bank of New York*:<sup>185</sup>

The plaintiff in a foreign country appointed the N.C. Bank to deliver a sum of money to one Pritam Singh of Jullundur, whose address was given. The bank instructed its Bombay branch accordingly. The Bombay branch appointed the Punjab National Bank which delivered the money to a wrong person.

The plaintiff's action against either bank failed. The Punjab National Bank was held not liable on the principle that a sub-agent is not liable to the principal except when he is guilty of fraud or wilful wrong. The wrong delivery was due only to negligence. The N.C. Bank had exempted itself from the consequences of wrong delivery.

A sub-agent is, however, bound by all the duties of an ordinary agent.

His rights cannot go beyond those of the main agent and they have to be exercised through the agent except where direct action would be necessary to give business efficacy to the appointment of a sub-agent. Where a sub-agent (fire-protection coating specialist) was appointed on agreed basis for the purpose of coating the 52-storey building undertaken by the contractor, it was held to be an implied term that his work would not be rejected except on reasonable basis.<sup>186</sup> A sub-broker was allowed to recover his agreed commission from the broker irrespective of the fact whether the broker had been

182. *Nensukhdas v Birdichand*, 1917 SCC OnLine Bom 47: AIR 1917 Bom 19.

183. *Summan Singh v National City Bank of New York*, AIR 1962 Punj 172: ILR 1952 Punj 189.

184. (1931) 145 LT 51 (CA); *New Zealand and Australian Land Co v Watson*, (1881) LR 7 QBD 374 (CA), privity not constituted by mere knowledge or consent to appointment; *Stephens v Badcock*, (1832) 3 B&Ad 354: 110 ER 133, money paid to sub-agent, principal could sue the agent, not sub-agent.

185. AIR 1952 Punj 172.

186. *Obbayashi-Gumi Ltd v Industrial Fireproofing (P) Ltd*, (1991) 3 Curr LJ 2330 (Singapore).

paid by the principal or not. The court said that it wholly depends upon terms of the appointment as interpreted in the background of factual background of market practices.<sup>187</sup>

### Substituted agent [Ss. 194–195]

**S. 194. Relation between principal and person duly appointed by agent to act in business of agency.**—Where an agent, holding an express or implied authority to name another person to act for the principal in the business of the agency, has named another person accordingly, such person is not a sub-agent but an agent of the principal for such part of the business of the agency as is entrusted to him.

#### *Illustrations*

- (a) A directs B, his solicitor, to sell estate by auction, and to employ an auctioneer for the purpose. B names C, an auctioneer, to conduct the sale. C is not a sub-agent, but is A's agent for the conduct of the sale.
- (b) A authorises B, a merchant in Calcutta to recover the moneys due to A from C & Co. B instructs D, a solicitor, to take legal proceedings against C & Co, for the recovery of the money. D is not a sub-agent, but is solicitor for A.

**S. 195. Agent's duty in naming such person.**—In selecting such agent for his principal, an agent is bound to exercise the same amount of discretion as a man of ordinary prudence would exercise in his own case; and, if he does this, he is not responsible to the principal for the acts or negligence of the agent so selected.

#### *Illustrations*

- (a) A instructs B, a merchant, to buy a ship for him. B employs a ship surveyor of good reputation to choose a ship for A. The surveyor makes the choice negligently and the ship turns out to be unseaworthy and is lost. B is not, but the surveyor is, responsible to A.
- (b) A consigns goods to B, a merchant, for sale. B, in due course, employs an auctioneer in good credit to sell the goods of A, and allows the auctioneer to receive the proceeds of the sale. The auctioneer afterwards becomes insolvent without having accounted for the proceeds. B is responsible to A for the proceeds.

A sub-agent has to be distinguished from a substituted agent. Sections 194 and 195 contain special provisions about substituted agents. According to Section 194 when an agent has an express or implied authority of his principal to name a person to act for him and the agent has accordingly named a person, such person is not a sub-agent, but he becomes an agent for the principal in respect of the business which is entrusted to him. The two illustrations to the section further explain the position of a substituted agent. A solicitor is appointed to sell an estate by auction and to employ an auctioneer for the purpose. The auctioneer thus appointed is not a sub-agent but an agent of the employer himself for the purpose of the sale. Similarly, when an agent is authorised to recover debts and he appoints a solicitor for

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187. *Crema v Cenkos Securities plc*, 2011 Bus LR 943 (CA).

the purpose, the latter is not a sub-agent, but a full-fledged agent for the purpose.<sup>188</sup>

One of the effects of appointing a substitute is that a direct privity of contract is established between the principal and the "substitute". The agent is not concerned about the work of the substitute. His only duty is to make the selection of the substitute with reasonable care. Section 195 says that "in selecting such agent for his principal, an agent is bound to exercise the same amount of discretion as a man of ordinary prudence would exercise in his own case; and, if he does this he is not responsible to the principal for the acts or negligence of the agent so selected". The two illustrations appended to the section explain the point. A merchant is instructed to buy a ship for his principal. The merchant employs a ship surveyor of good reputation to choose a ship for the principal. The surveyor makes the choice negligently, the ship turns out to be unseaworthy, and is lost: The surveyor, but not the agent, is liable to the principal. In the second illustration, goods are consigned to a merchant for sale. The merchant employs an auctioneer in good credit to sell the goods and allows him to receive the proceeds. The auctioneer becomes bankrupt without having accounted for the proceeds to the principal. The merchant is responsible to the principal for the proceeds.

### Remedies of principal for breach of duty

"A principal has threefold rights against an agent who fails in his duty:

- (a) to ask for an account and also demand payment of secret and illicit profits earned by him as an agent;<sup>189</sup>
- (b) to seek damages for disregard of the terms of agency as also for want of skill and care;
- (c) to resist the claim of the agent for commission and indemnity by the plea that the agent had acted for himself, i.e. as a principal."<sup>190</sup>

188. See also the decision of the Supreme Court in *Qamar Shaffi Tyabji v Commr, Excess Profits Tax*, AIR 1960 SC 1269: (1960) 3 SCR 546, 551, where a person named as an agent for the company with the approval of the Board of Directors was held to be a substituted agent; *Aggarwal Chamber of Commerce Ltd v Ganpat Rai Hira Lal*, AIR 1958 SC 269; 1958 SCR 938, privity of contract established. *Central Bank of India Ltd v Firm Kur Chand Kurra Mal*, AIR 1958 Punj 59, the principal asking his bank to collect the proceeds of their invoice through a particular bank, the matter handed over to that bank which, therefore, became a substituted agent. *A.C. Rangaswami v D.J. Renuka*, 1997 AIHC 975 Kant, holder of power of attorney is equal in the right of transfer to the owner, part payment taken by the attorney, sale failed to go through, attorney liable for refund as much as the owner.

189. *Beaumont v Boultbee*, (1802) 7 Ves 599, 608, account of profits made by lessee-agent by entering into arrangement with adjacent owners.

190. V.G. Ramachandran, *LAW OF AGENCY* (1985) 401, citing *Maneklal Mansukhbhai v Jwaladutt Pilani*, AIR 1947 Bom 135. Where no loss is caused by breach of duty, the principal is entitled to recover only nominal damages. *Manchubhai v John H. Tod*, ILR (1896) 20 Bom 633. In the case of a delayed sale, the difference recoverable is the price actually realised and that which would have been realised when the goods ought to have been sold, *Challapathi v Suruuya*, 12 MLJ 375.

### RIGHTS OF AGENT

The following are some of the important rights of an agent:

#### 1. Right to remuneration [S. 219]

**S. 219. When agent's remuneration becomes due.**—In the absence of any special contract, payment for the performance of any act is not due to the agent until the completion of such act; but an agent may detain moneys received by him on account of goods sold, although the whole of the goods consigned to him for sale may not have been sold, or although the sale may not be actually complete.

Every agent is clearly entitled to his agreed remuneration, or if there is no agreement, to a reasonable remuneration.<sup>191</sup> Where the amount of remuneration is left on principal's discretion, even then reasonableness would be the criterion.<sup>192</sup> The difficult question is as to when remuneration becomes due. Section 219 says that "in the absence of any special contract, payment for the performance of any act is not due until the completion of such act...".

This provision raises two questions. When is the act complete? and secondly, is the act a result of the agent's services? Both questions depend "first and last on particular terms of the particular contract"<sup>193</sup> Thus where an agent was appointed to secure orders for advertisements in a newspaper, the commission in respect of an advertisement being payable when it was published, the agent was held entitled to commission on orders actually obtained by him although the advertisements to which the orders related were not published until after the termination of employment.<sup>194</sup> As against it, where an agent was engaged to negotiate for the purchase of a house at a commission of 2 per cent on the purchase price, he was held not entitled to any commission till the completion of the purchase of the house.<sup>195</sup> Much depends upon the nature of the service that the agent undertakes to provide.

191. For example, the Lahore High Court held in *Khursheed Alam v Asa Ram*, AIR 1933 Lah 784 that "where a person is proved to have acted as broker, he is entitled to his commission; and even if he fails to prove the rate of commission agreed upon, a reasonable amount ought to be awarded to him as such commission". The mode, manner and time of payment may be provided for by a special contract. *Vasanji Moolji v Karsondas Tejpal*, AIR 1928 Bom 270, where remuneration is payable on completion of sale, no *quantum meruit* if the transaction proved unsuccessful. *Hindustan Antibiotics Ltd v Kobli Medical Stores*, 1997 AIHC 2630 (MP), recovery of agreed commission for the extended period of agency.

192. *Kofi Sunkerette Obu v A. Strauss & Co Ltd*, 1951 AC 243 (PC). Where there is no express contract, custom or usage of the particular trade become applicable. *Read v Mann*, (1830) 10 B&C 438.

193. *Sellers v London Countris Newspapers*, (1951) 1 KB 784 (CA).

194. *Ibid*. Another similar case is *Bilbee v Hasse & Co*, (1889) 5 TLR 677, the agent was entitled to commission on orders received from the customer introduced by him even after the termination of his agency.

195. *Ayyanah Chetty v Subramania Iyer*, (1923) 45 MLJ 409. The court relied upon the following statement of Lord ESHER in *Peacock v Freeman*, (1888) 4 TLR 541 (CA): "Land could only be said to have been sold when the conveyance was complete not when there was a mere contract to sell."

Thus, in a case before the Allahabad High Court,<sup>196</sup> an agent was appointed to introduce a purchaser willing to purchase the defendant's property. He did introduce one and even the sale was settled and earnest money paid, but it could not be completed through the purchaser's inability to find money. The agent was nevertheless held entitled to his agreed commission.<sup>197</sup>

Secondly, the transaction that results must be due to the agent's services. The bargain must be direct result of his service.<sup>198</sup> In *Green v Bartlett*<sup>199</sup> an agent was appointed to sell a house. He held an auction but failed to find a purchaser. One of the persons attending the auction obtained from him the address of the principal and purchased the house from him without intervention of the agent. Even so the transaction was held to be a result of the agent's effort entitling him to his commission.

The principle of this case was followed by the Bombay High Court.<sup>200</sup> The defendants appointed the plaintiff, a broker, to obtain a loan on the mortgage of his premises. He introduced the manager of a bank who would have made an advance if the security offered had not proved to be insufficient. Ultimately, the bank did make an advance, but through another broker. The plaintiff was held entitled to his commission.

Where the agent's services are only remotely connected with the transaction, his remuneration is not earned. *Tribe v Taylor*<sup>201</sup> is an apt illustration.

The defendant requested the plaintiffs to introduce a purchaser of his premises or a source of capital. The plaintiff introduced one Wood who advanced a sum of money by way of loan. The agreed commission was paid to the plaintiffs. Subsequently Wood entered into partnership with the defendant and advanced a further sum. The plaintiff's action to claim commission on this second advance failed.

The judge said: "The question which arose was... whether the subsequent advance was the result of any act of the plaintiffs. If... the plaintiffs had introduced any new person, who had advanced the money, I should have thought the defendant would have been bound to pay the commission claimed. If they had induced Wood to become a partner and to introduce

196. *Sheikh Farid Baksh v Hargulal Singh*, AIR 1937 All 46.

197. See also *Saraswati Devi v Motilal*, AIR 1982 Raj 108: (1982) Raj LR 251. Where commission was payable to an estate agent as and when he introduced a ready and willing customer but the principal refused to sign the agreement, held, the agent entitled to commission. Following *Abdulla Ahmad v Animendra Kissen Mitter*, AIR 1950 SC 15: 1950 SCR 30.

198. See, for example, *Bray v Chandler*, (1856) 18 CB 718; *Gibson v Crick*, (1862) 31 LJ Ex 304; it need not necessarily be the immediate cause of the transaction, but it must be shown that it was brought about as the direct result of his intervention. *Burton v Hughes*, (1885) 1 TLR 205. It is not sufficient for the agent to show that it would not have been entered into but for his services, if it resulted therefrom only as a casual or remote consequence: *Tribe v Taylor*, (1876) LR 1 CPD 505 and *Jordon v Ram Chandra Gupta*, (1903–04) 8 Cal WN 831.

199. (1863) 14 CBNS 681: 8 LT 503: 11 WR 834: 32 LJCP 261. Approved by the Privy Council in *Burchell v Gowrie*, 1910 AC 614.

200. *Vasanji Moolji v Karsondas Tejpal*, AIR 1928 Bom 270.

201. (1876) LR 1 CPD 505.

further capital, I should have thought they would have been entitled to commission on that.... Was the subsequent partnership the result of the introduction or of an independent negotiation? *Causa proxima* is not the question; the plaintiffs must show that the act of theirs was the *causa causans*. It is true that (second) advance might not, and probably would not have been made by Wood, but for the original introduction by the plaintiffs. But that is not enough."

The principal is, of course, under a duty not to prevent the agent from earning his commission.<sup>202</sup> But this does not prevent the principal from selling the property himself or from refusing to sell at all. A well-known case is *Luxor (Eastbourne) Ltd v Cooper*.<sup>203</sup>

An agent was promised his commission if he brought about the sale of the defendant's cinemas. The agent introduced a customer but the company refused to sell. The agent brought an action for his commission.

The House of Lords held against him: "There was no implied term that the principal would not dispose of the property himself, or through other channels or otherwise act so as to prevent the agent from earning his commission." Viscount SIMON LC said:<sup>204</sup> "The agent necessarily incurs certain risks, e.g. the risk that his nominee cannot find the purchase price and will not consent to terms reasonably proposed to be inserted in the contract of sale.... The agent also takes the risk of his principal not being willing to conclude the bargain with the agent's nominee. The last risk is ordinarily a slight one for the owner's reason for approaching the agent is that he wants to sell."

Where an agent of a foreign company entered into a contract for sale of machinery to the defendant and one of the terms of the contract was that payment of commission to be payable by the defendant would be subject to installation of the machinery, but the defendant could not make the site for installation ready and, therefore, there could be no installation. The agent, being not responsible for the same, was entitled to his commission.<sup>205</sup> The terms of the arrangement showed sufficient privity of contract between the defendant buyer and the agent of the foreign principal, e.g. provision for payment of commission to the agent directly by deducting it from price.<sup>206</sup>

### *Jurisdiction*

Where the contract was entered into at Calcutta and communicated to the plaintiff at Delhi and payment of commission was also made at Delhi,

202. Where the transaction fell through because of the defective title of the principal, the broker was allowed his commission. *Ellas v Govind Chander*, ILR (1903) 30 Cal 202.

203. 1941 AC 108 (HL).

204. At p. 117, *ibid*. For the purposes of his remuneration the agent has the right to demand accounts from the principal though there is no statutory provision on it, *Narandas Morardas Gajiwala v S.P.A.M. Papammal*, AIR 1967 SC 333, 335.

205. *Continental and Eastern Agencies v Coal India Ltd*, AIR 2003 Del 387.

206. *Ibid*.

it was held that the courts at Delhi had jurisdiction to enforce the contract since a part of the cause of action had arisen there.<sup>207</sup>

*Effect of misconduct [S. 220]*

**S. 220. Agent not entitled to remuneration for business misconduct.**—An agent who is guilty of misconduct in the business of the agency is not entitled to any remuneration in respect of that part of the business which he has misconducted.

*Illustrations*

- (a) A employs B to recover 1,00,000 rupees from C, and to lay it out on good security. B recovers the 1,00,000 rupees and lays out 90,000 rupees on good security, but lays out 10,000 rupees on security which he ought to have known to be bad, whereby A loses 2000 rupees. B is entitled to remuneration for recovering the 1,00,000 rupees and for investing the 90,000 rupees. He is not entitled to any remuneration for investing the 10,000 rupees and he must make good the 2000 rupees to B.
- (b) A employs B to recover 1000 rupees from C. Through B's misconduct the money is not recovered. B is entitled to no remuneration for his services, and must make good the loss.

An agent is not entitled to any commission in respect of that part of the business which he has misconducted.<sup>208</sup> Section 220 accordingly provides that an agent who is guilty of misconduct in the business of agency, is not entitled to any remuneration in respect of that part of the business which he has misconducted.

The effect of misconduct is twofold. Firstly, the agent forfeits his right to commission. This is irrespective of any loss suffered by the principal. "The principle underlying the rule is that 'a principal is entitled to have an honest agent and it is only the honest agent who is entitled to any commission'."<sup>209</sup> The commission is forfeited only in respect of that part of the agency business which has been misconducted.<sup>210</sup> An agent was employed to sell leasehold premises. Great many tailors were interested in acquiring the premises. The agent, being afraid that the original landlord would not permit lease to tailors, obtained his permission in advance. This considerably increased the price. The agent, however, kept this fact from his principal and induced him

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207. *Ibid.*

208. There is no misconduct where commercial practices of a trade allow the broker commission from both parties, or where the principal leaves the agent to look for remuneration to a third party or where he knows that the agent will get remuneration from third party. *Bow's Emporium Ltd v A. R. Brett & Co*, (1927) 44 TLR 194 (HC); *Baring v Stanton*, (1876) LR 3 Ch D 502 (CA); *Municipal Corpn of Bombay v Cuverji Hirji*, ILR (1895) 20 Bom 124, a custom or knowledge of that kind would have to be proved by the agent. But otherwise commission from the other party is a misconduct. *Andrews v Ramsay & Co*, (1903) 2 KB 635. Discount money retained in the honest belief that the agent is entitled to it is not a misconduct though the amount may have to be handed over.

209. *Sirdhar Vasanta Rao Ananda Rao v Gopal Rao Sethu Rao Peshwai*, AIR 1940 Mad 299, 301.

210. See *Purushottam Haridas v Amruth Ghee Co Ltd*, AIR 1961 AP 143.

to accept lower price. This was a misconduct and breach of duty on the part of the agent. He was not allowed to recover his commission.<sup>211</sup>

Secondly, the principal is entitled to recover compensation for any loss caused by the misconduct. The illustrations to the section make it clear that payment of damages caused by the misconduct is in addition to the forfeiture of commission or remuneration.

## 2. Right of retainer [S. 217]

**S. 217. Agent's right of retainer out of sums received on principal's account.**—An agent may retain, out of any sums received on account of the principal in the business of the agency, all moneys due to himself in respect of advances made or expenses properly incurred by him in conducting such business, and also such remuneration as may be payable to him for acting as agent.

The agent has the right to retain his principal's money until his claims, if any, in respect of his remuneration or advances made or expenses incurred in conducting the business of agency are paid. The right can be exercised on "any sums received on account of the principal in the business of the agency". He can retain only such money as is in his possession. He is not entitled to an equitable lien, that is, the right to have his claims satisfied in preference to other creditors out of the principal's money not in his possession. But a solicitor or vakil is entitled to an equitable lien on the proceeds of an action conducted by him till his costs are paid. His fee is first charge on the proceeds even if they are not in his possession. He is also entitled, for this purpose, to have the proceeds pass through his hands.<sup>212</sup>

## 3. Right of lien [S. 221]

**S. 221. Agent's lien on principal's property.**—In the absence of any contract to the contrary, an agent is entitled to retain goods, papers and other property, whether movable, or immovable, of the principal received by him, until the amount due to himself for commission, disbursements and services in respect of the same has been paid or accounted for to him.

In addition to the above right of retainer, the "agent has the right to retain goods, papers and other property, whether movable or immovable, of the principal received by him, until the amount due to himself for commission, disbursements and services in respect of the same has been paid or accounted for to him".<sup>213</sup>

211. *Heath v Parkinson*, (1926) 42 TLR 693; *E.I.D. Parry (India) Ltd v Far Eastern Marine Transport Co Ltd*, 1983 SCC OnLine Mad 61: (1988) 1 LW 320, short delivery of goods by carrier: *E.I.D. Parry (India) Ltd v Far Eastern Marine Transport Co Ltd*, (1988) 2 TAC 387.

212. *Menon v Cochine Mercantiles Ltd*, (1962) 32 Comp Cas 378.

213. Lord ELLENBOROUGH in *Houghton v Mathew*, (1803) 3 Bos & P 485, 494, described lien "to be the right in one man to retain that which is in his possession belonging to another until certain demands of the person who is in possession are satisfied". Cited by A.H. KHAN J in *Gopaldas v Thakurdas*, AIR 1957 MB 20, 22. *Bharat Petroleum Corp Ltd v Chembur Service Station*, (2011) 3 SCC 710: (2011) 2 SCC (Civ) 49 and *Bharat Petroleum Corp Ltd v*

The conditions of this right are:

- (1) The agent should be lawfully entitled to receive from the principal a sum of money by way of commission earned or disbursements made or services rendered in the proper execution of the business of agency.
- (2) The property over which the lien is to be exercised should belong to the principal and it should have been received by the agent in his capacity and during the course of his ordinary duties as agent.<sup>214</sup> The property is considered to be sufficiently in the possession of the agent where he has been dealing with it. Thus where an auctioneer was engaged to sell furniture at the owner's house, he was held to be sufficiently in possession to exercise lien for his commission. The property held by an agent for a special purpose cannot be subjected to lien. The existence of a special purpose implicitly excludes the right.<sup>215</sup> Similarly, where possession is obtained without the principal's authority or by fraud or misrepresentation, there is no lien. Briefly, the agent's possession must be lawful.
- (3) The agent has only a particular lien. A particular lien attaches only to that specific subject-matter in respect of which the charges<sup>216</sup> are due. No other property can be retained.

For example, in *Bombay Saw Mills Co, re*,<sup>217</sup> the secretaries and treasurers<sup>218</sup> of a company claimed lien over the company's property for their advances. SCOTT J rejected the claim "because the sums advanced and expended were not, as required (by S. 221) 'disbursements and services in respect of' the property on which the lien was claimed, but were loans made on behalf of the company generally and for the purpose of the whole concern".<sup>219</sup>

#### *Effect of lien*

The effect of lien as between the principal and the agent has been thus stated by A.H. KHAN J in *Gopaldas v Thakurdas*<sup>220</sup>: "The agent's lien does not give unrestricted authority to the agent to deal with the property in any manner the agent may like. The right is limited in nature. It enables

*Chembur Service Station*, (2011) 3 SCC 710: (2011) 2 SCC (Civ) 49, certain railway premises were in possession of a businessman for his business for over 40 years. His licence was terminated and he was told to handover vacant possession. He claimed compensation for sudden termination and lien on premises till payment. The court said that he deserved a notice and hearing so that the court could consider what were the terms of the licence.

214. See MEHTA AJC in *Pestonji Bhimji v Ravji Javerchand*, (1934) 150 IC 483 (Sind), 447.

215. *Williams v Millington*, (1788) 1 Hy Bl 81: 2 RR 724.

216. S. 171 confines general lien only to bankers, factors, wharfingers, attorneys and policy brokers. A general agent is not covered by any one of these categories.

217. ILR (1888) 13 Bom 314.

218. Who were a sort of managing agents, now banned.

219. At p. 321. *Rocklines Constructions v Trupti K. Patel*, (2003) 1 CLT 414 (Kant), an order can be issued for delivery of property where the right does not exist or payment has been made.

220. AIR 1957 MB 20, 22.

the agent to retain the property till his dues are paid. But this confers no authority on the agent to sell or otherwise dispose of the property without the consent of the owner".

A partnership firm acting as the clearing and forwarding agents of the principal detained the goods of the principal because of a dispute about their commission amount and had the goods sold on an interim court order. The firm was held to be in the wrong. It had no right to sell because lien does not give that right. An agent can no doubt dispose of the goods with the consent of the principal or with court order, but in this case the order of the court was not valid because the firm being not registered could not have filed a suit. The sale was wrongful. The court directed the firm to keep intact the money equivalent of the value of the goods so that the remedy of accounts would be effectively available to the principal.<sup>221</sup>

Where, however, in terms of his agreement with the principal, the agent has become a pledgee of the goods, he may sell them after giving a reasonable notice to the principal of his intention to sell.<sup>222</sup>

As against third parties the lien is effective only to the extent of the principal's rights on the property. If the principal has limited rights, the lien will be equally limited. If the property is already subject to some rights or equities in favour of third persons, the lien will also be subject to them. But where the property on which lien is being exercised is a negotiable instrument, the agent will become a holder for value to the extent of his lien and will acquire a title free of prior equities if he acts in good faith and without notice of them.<sup>223</sup>

If the principal creates any charge on the property subsequently to the attachment of the lien, that will be subject to the lien.

### *Loss of lien*

The agent's lien is lost in the following cases:

- (1) Lien, being a possessory right, is lost as soon as possession is lost. Possession is lost when the agent delivers the goods to the principal himself or to a carrier for the purpose of transmission to the principal. In the latter case, the agent cannot revive his lien by stopping the goods in transit.<sup>224</sup> But where the property has been delivered for a special purpose, like safe custody, which is inconsistent with lien, the lien is not lost.

As long as the agent remains in possession, his lien is effective, and is not affected by the fact that the company to which the

221. *Kavita Trehan v Balsara Hygiene Products Ltd*, AIR 1992 Del 92.

222. *Gopaldas v Thakurdas*, AIR 1957 MB 20, 22.

223. *London Joint Stock Bank v Simmons*, 1892 AC 201 (HL).

224. *Kishun Das v Ganesh Ram*, AIR 1950 Pat 481; *Sweet v Pym*, (1860) 1 East 4: 102 ER 2: 5 RR 497.

goods belonged has been ordered to be wound up,<sup>225</sup> or that the principal has become insolvent. The agent's possession is not terminated where property has been obtained from him by unlawful means or by fraud or misrepresentation.

- (2) The lien is lost, when the agent waives his right. Waiver may arise out of an agreement express or implied or may be inferred from conduct inconsistent with the right.
- (3) The agent's lien is subject to a contract to the contrary and, therefore, does not exist where the agent has by his agreement with the principal excluded it.<sup>226</sup>

#### 4. Right to indemnity [Ss. 222–223]

**S. 222. Agent to be indemnified against consequences of lawful acts.**—The employer of an agent is bound to indemnify him against the consequences of all lawful acts done by such agent in exercise of the authority conferred upon him:

##### *Illustrations*

- (a) *B*, at Singapore, under instructions from *A* of Calcutta, contracts with *C* to deliver certain goods to him. *A* does not send the goods to *B*, and *C* sues *B* for breach of contract. *B* informs *A* of the suit, and *A* authorises him to defend the suit. *B* defends the suit, and is compelled to pay damages and costs, and incurs expenses. *A* is liable to *B* for such damages, costs and expenses.
- (b) *B*, a broker at Calcutta, by the orders of *A*, a merchant there, contracts with *C* for the purchase of 10 casks of oil for *A*. Afterwards *A* refuses to receive the oil, and *C* sues *B*. *B* informs *A*, who repudiates the contract altogether. *B* defends, but unsuccessfully, and has to pay damages and costs and incurs expenses. *A* is liable to *B* for such damages, costs and expenses.

The right to indemnity extends to all losses and expenses incurred by the agent in the conduct of the business. Where, for example, a stockbroker, on the instructions of a solicitor, contracted to sell certain shares and had to incur liability to the purchaser by reason of the owner's refusal to complete the sale, the stockbroker was held entitled to recover indemnity from the principal.<sup>227</sup>

The agent must have been indemnified in the lawful conduct of the business of agency. A wagering agreement is not unlawful. It is only void. Accordingly, the Supreme Court in *Kishanlal v Bhanwar Lal*,<sup>228</sup> allowed an agent to recover indemnity for losses incurred by him in wagering transactions entered into on instructions of his principal.

Where the act done by the agent on instructions from his principal is apparently lawful, but it turns out to be unlawful or injurious to a third

225. *Chidambaran Chettiar v Tinnevelly Sarangapani Sugar Mills Co Ltd*, ILR (1906–08) 31 Mad 123.

226. *Ram Prasad v State of M.P.*, (1969) 3 SCC 24, 27: AIR 1970 SC 1818, the right is excluded where the property is accepted for a special purpose.

227. *Hicens Harrison, Woolston & Co v Jackson & Sons*, 1943 AC 266 (HL).

228. AIR 1954 SC 500 (1955).

person, the agent is entitled to indemnity against the consequences of the act.

### Liability of agent under dishonoured cheque

The contract was for supply of goods. The petitioner was working as a commission agent transacting business on behalf of the company. The court said that once the cheque was issued duly signed by the petitioner, he became liable to be prosecuted against. There was failure on the part of the agent to reply to the notice to inform the complainant that the primary liability was that of the principal for the amount due, if any. This estopped him from subsequently saying that only the principal was liable. He was also not able to prove that there was no real transaction under which the cheque was issued.<sup>229</sup>

**S. 223. Agent to be indemnified against consequences of acts done in good faith.**—Where one person employs another to do an act, and the agent does the act in good faith, the employer is liable to indemnify the agent against the consequences of that act, though it causes an injury to the rights of third persons.

#### *Illustrations*

- (a) A, a decree-holder and entitled to execution of B's goods, requires the officer of the Court to seize certain goods representing them to be the goods of B. The officer seizes the goods, and is sued by C, the true owner of the goods. A is liable to indemnify the officer for the sum which he is compelled to pay to C, in consequence of obeying A's directions.
- (b) B, at the request of A, sells goods in the possession of A, but which A had no right to dispose of. B does not know this, and hands over the proceeds of the sale to A. Afterwards C, the true owner of the goods, sues B and recovers the value of the goods and costs. A is liable to indemnify B for what he has been compelled to pay to C and for B's own expenses.

One of the illustrations appended to Section 223 seems to be based upon the facts of *Adamson v Jarvis*:<sup>230</sup>

An auctioneer sold certain cattle on instructions from the defendant and was held liable to the true owner for conversion. He recovered indemnity from the principal because the act in question was apparently lawful.

Where, however, the act in question is apparently unlawful or criminal, such as beating a person or publication of a libel, the principal will not be liable upon an express or implied promise to indemnify the agent against the consequences of such act. For example, an agent, appointed to import adulterated mustard oil, suffered loss and punishment, but he could not recover

229. *J. Ramaraj v Iliyaz Khan*, AIR 2007 NOC 2031 (Kant).

230. (1827) 4 Bing 66: 29 RR 503. The Supreme Court held in *A. Thangal Kunju Musaiar v M. Venkatachalam Potti*, AIR 1956 SC 246: (1955) 2 SCR 1196, 1211, that there can be no agency for the commission of a crime. The wrongdoer would be personally liable.

indemnity.<sup>231</sup> Where, however, the plaintiff on instruction, from the defendant, paid a sum of money to the caste panchayat to have the defendant's caste disqualifications removed, he was allowed to recover the money from the defendant.<sup>232</sup>

**S. 224. Non-liability of employer of agent to do a criminal act.**—Where one person employs another to do an act which is criminal, the employer is not liable to the agent, either upon an express or an implied promise, to indemnify him against the consequences of that act.

*Illustrations*

- (a) A employs B to beat C, and agrees to indemnify him against all consequences of the act. B thereupon beats C, and has to pay damages to C for so doing. A is not liable to indemnify B for those damages.
- (b) B, the proprietor of a newspaper, publishes, at A's request, a libel upon C in the paper, and A agrees to indemnify B against the consequences of the publication, and all costs and damages of any action in respect thereof. B is sued by C and has to pay damages, and also incurs expenses. A is not liable to B upon the indemnity.

Where the act in question is apparently tortious, the agent, who has been held liable on it, may recover contribution from the principal (not indemnity) under the Law Reform (Married Women's and Tortfeasors) Act, 1955.<sup>233</sup>

## 5. Right to compensation [S. 225]

**S. 225. Compensation to agent for injury caused by principal's neglect.**—The principal must make compensation to his agent in respect of injury caused to such agent by the principal's neglect or want of skill.

Thus every principal owes to his agent the duty of care not to expose him to unreasonable risks.<sup>234</sup> The illustration appended to the section makes the point clear:

A employs B as a bricklayer in building a house, and puts up the scaffolding himself. The scaffolding is unskillfully put up, and B is in consequence hurt. A must make compensation to B.

## Relations of principal with third parties

### AGENT'S AUTHORITY

The acts of the agent within the scope of his authority bind the principal.<sup>235</sup> Section 226 of the Contract Act gives statutory effect to the principle by declaring that:

231. *Ram Kumar Agarwala v Lakshmi Narayan Agarwala*, AIR 1947 Cal 157.

232. *Hazarimal Kochnaji v Khemchand Maggaji*, AIR 1962 Raj 86.

233. S. 6(1)(c), (2). "Contribution" is different from "indemnity" because indemnity covers the whole of the loss suffered by the agent.

234. *Federal Insurance Co v Nakano Singapore (P) Ltd*, (1992) 1 Curr LJ 539 (CA Singapore), liability for weak scaffolding.

235. See *Polestar Electronics (P) Ltd v CST*, (1978) 1 SCC 636, where it was held that sales made by a taxpayer through his branches run by his agents would be regarded as sales made by

**S. 226. Enforcement and consequences of agent's contracts.—**

Contracts entered into through an agent, and obligations arising from acts done by an agent, may be enforced in the same manner, and will have the same legal consequences, as if the contracts had been entered into and the acts done by the principal in person.

*Illustrations*

- (a) *A buys goods from B, knowing that he is an agent for their sale, but not knowing who is the principal. B's principal is the person entitled to claim from A the price of the goods, and A cannot, in a suit by the principal, set-off against that claim a debt due to himself from B.*
- (b) *A, being B's agent, with authority to receive money on his behalf, receives from C a sum of money due to B. C is discharged of his obligation to pay the sum in question to B.*

It is necessary for this effect to follow that the agent must have done the act within the scope of his authority. The authority of an agent and more particularly its scope are subjects of some controversy.<sup>236</sup> The uncertainty is largely due to the fact that the authority of an agent does not depend upon one source. It emanates from the principal, but its dimensions depend upon legal inferences, which, in turn, depend upon the purpose of the agency, the surrounding circumstances and a desire to protect *bona fide* commercial transactions. For, agency came into being to promote and not to hinder commerce.<sup>237</sup>

The authority of an agent means his capacity to bind the principal. It refers to the sum total of the acts it has been agreed between principal and agent that the agent should do on behalf of the principal. When the agent does any of such acts, it is said he has acted within his authority.<sup>238</sup>

him. *V. Ramesh v Convenor, EAMCET*, AIR 1997 AP 79, a candidate who was entitled to a reserve seat for admission to engineering college was invited by telegram for interview. Telegraph Department delayed message. Taking the Telegraph Department to be the agent of the sender, its lapse was the lapse of the principal which the principal must rectify. Direction for admission. *A. Arul Latha Gold v Govt of T.N.*, (1994) 2 LW 686 (Mad), principle of agency attracted when post office is selected as a carrier of message.

236. The varying viewpoints have been presented by J.L. Montrose in *The Basis of the Power of an Agent in Cases of Actual and Apparent Authority*, (1938) 16 Can BR 757. The following articles are there considered: Cook, *Agency by Estoppel*, (1905) 5 Col LR 35; Ewart, *Agency of Estoppel*, (1905) 5 Col 354; Cook, *Agency of Estoppel—A Reply*, (1906) 6 Colum LR 34; Cook, *Estoppel as Applied to Agency*, (1903) 16 Harv LR 324. He who does an act through another is deemed in law to do it himself. See *MCD v Jagdish Lal*, (1969) 3 SCC 389: AIR 1970 SC 7: (1970) 1 SCR 579. *Sardar Gurcharan Singh v Mahendra Singh*, (2004) 1 MPLJ 252, plaintiff's father cancelled the purchase of land made by his son because there was encroachment. In that respect he acted as an agent of his son. The latter became bound by that act.

237. See, for example, Stoljor, *THE LAW OF AGENCY: ITS HISTORY AND PRESENT PRINCIPLES* (1961). *Kamlesh v Jasbir Singh*, AIR 2004 P&H 216: (2004) 4 ICC 39, the owner authorised his brother-in-law to manage his property in his absence. He inducted a licensee on the premises. This was held to be valid. It was also ratified by the owner. It did not require a registered power of attorney because there was no transfer of interest in it. The owner could terminate the licence and sue for possession.

238. *Nand Lal Thanvi v Legal Representatives of Goswami Brij Bhushan*, (2004) 2 ICC 103 (Raj), acknowledgement of liability by agent binding the principal with extension of time of limitation.

## Actual authority

Actual authority of an agent is the authority conferred on him by the principal. It is of two kinds, namely, express or implied. Sections 186 and 187 provide this:

**S. 186. Agent's authority may be expressed or implied.**—The authority of an agent may be expressed or implied.

**S. 187. Definitions of express and implied authority.**—An authority is said to be express when it is given by words spoken or written. An authority is said to be implied when it is to be inferred from the circumstances of the case; and things spoken or written, or the ordinary course of dealing, may be accounted circumstances of the case.

### *Illustration*

A owns a shop in Serampore, living himself in Calcutta, and visiting the shop occasionally. The shop is managed by B, and he is in the habit of ordering goods from C in the name of A for the purposes of the shop, and of paying for them out of A's funds with A's knowledge. B has an implied authority from A to order goods from C in the name of A for the purposes of the shop.

## Express authority

Where the authority is conferred by words, spoken or written, it is called express authority. A power of attorney, for example, which is a kind of deed and authorises the agent to do certain acts, is an illustration of express authority. But, however precisely the authority of an agent may be drawn, disputes as to its scope are likely to arise. The scope of express authority is worked out by construction of the words used in the documents. For example, where a principal, while going abroad, authorised his agent and partner to carry on the business, and his wife to accept bills on his behalf for his personal business, he was held not bound when his wife accepted bills for the business, which the agent was conducting and which was different from his personal business.<sup>239</sup> The decision has been criticised, particularly because the agent and the third party had acted in good faith to meet the principal's genuine business needs. Accordingly, in a subsequent case of agency by power of attorney, where the agent obtained a loan outside his authority by signing a cheque on behalf of his principal to pay the principal's workmen, the principal was held bound.<sup>240</sup> Where the appointment was for "fixing" a steamer, intention being to let it out, the principal was held liable when the agent instead hired a steamer.<sup>241</sup>

239. *Attwood v Munnings*, (1827) 7 B&C 278: 108 ER 727. The decision has been criticised in Stoljar, THE LAW OF AGENCY (1961) 94.

240. *Reid v Rigby*, (1894) 2 QB 40.

241. *Weigall S. & Co v Runciman & Co*, (1916) 85 LJKB 187 (CA). *Forysthe Trading Services Ltd v M.V. Niizuru*, (2004) 5 Bom CR 806, contract made through agency process, the principal accepted liability to pay for the supply could not subsequently escape by saying that there was no privity of contract.

But where the third party has knowledge of the limitation on the agent's authority or could have discovered it by reasonable examination, he would be bound by it.<sup>242</sup> Thus, where an agent was given very wide power of withdrawing the principal's money "without restriction", the principal was held not bound when the agent gave a cheque to a car dealer to purchase a car for himself,<sup>243</sup> and paid a few cheques into his banking account to wipe out his overdraft.<sup>244</sup> In either case it was the duty of the third party to make a reasonable inquiry whether the agent had the authority to use the principal's money for his personal purposes.<sup>245</sup>

An agent cannot borrow on behalf of his principal unless he has clear authority to do so. The power to draw or endorse bills or notes does not include the power to borrow.<sup>246</sup> Where the agent has the power to borrow, the fact that he borrowed beyond the authorised limit, does not prevent the third party from holding the principal liable,<sup>247</sup> because the third party has no means of ascertaining that fact. Similarly, the fact that an agent has acted from improper motive does not take the case beyond the scope of authority. Thus in *Hambro v Burnard*:<sup>248</sup>

An agent was appointed to underwrite policies. He underwrote a policy which in fact amounted to a guarantee of a company's debts. He knew the precarious condition of the company, but being interested in it, wanted to help it. The principal was held liable because the third party could not have known with what motive the agent was underwriting a particular policy.

### Implied authority

"An authority is said to be implied when it is to be inferred from the circumstances of the case; and things spoken or written or the ordinary course of dealing, may be accounted circumstances of the case." [See illustration to S. 187]

Implied authority is an instance of real or actual authority for it is conferred upon the agent by the conduct of the principal as interpreted in the circumstances of the case.

242. *Ferguson v Um Chand Boid*, ILR (1906) 33 Cal 343, the power of attorney expressly restricting borrowing.

243. *Reckitt v Barnet, Pembroke & Slater Ltd*, 1929 AC 176 (HL).

244. *Midland Bank Ltd v Reckitt*, 1933 AC 1 HL.

245. *United Province Govt v Church Missionary Trust Assn Ltd*, ILR (1948) 22 Luck 93: AIR 1948 Oudh 54, the third party knew that the agent was acting under power of attorney, but did not bother to acquaint himself with its terms.

246. *Jacobs v Morris*, (1902) 1 Ch 816 (CA). *Raymond Woollen Mills Ltd v Coal India Ltd*, (1998) 1 CHN 53, an agent cannot initiate legal proceedings on behalf of principal without express authorisation. To the same effect is the decision in *State of Karnataka v M. Muniraju*, (2003) 1 Kant LJ 291.

247. *Withington v Herring*, (1829) 5 Bing 442.

248. (1904) 2 KB 10 (CA). *Albright and Wilson U K Ltd v Biochem Ltd*, 2002 UKHL 37 (HL), a chemical supplier company whose agent failed to provide the correct documentation with the delivery was held to be in breach of its contract with the buyer.

The distinction between express and implied authority is not fundamental, but depends merely on whether the authority is delimited by words or by conduct. If *P* tells *A* that he is to act as manager, this is really a compendious way of stating that he is to do all the acts as manager would ordinarily do. Those acts might well be termed as express authority. However, it is often said that if an agent is placed in a certain position he has implied authority to do all the acts a person in that position ordinarily does.<sup>249</sup>

An illustration of implied authority is to be found in *Ryan v Pilkington*.<sup>250</sup> An estate agent was appointed to find a purchaser for certain property. He accepted a deposit from a prospective customer and misappropriated it. The principal was held liable, because an estate agent has an implied authority to take a deposit. He cannot, however, receive payment or give any warranty unless actually authorised.<sup>251</sup>

Thus the extent of an agent's authority, whether express or implied, depends upon—

- (1) the nature of the act or business he is appointed to do;
- (2) things which are incidental to the business or are usually done in carrying it out;<sup>252</sup>
- (3) the usual customs and usages of the trade.

This is the essence of Section 188 which defines the extent of the agent's authority in the following words:

249. J.L. Montrose, *Actual and Apparent Authority*, (1938) 16 Can 764. The American Restatement refers to this kind of authority as "incidental". Art. 35 says: "Unless otherwise agreed, authority to conduct a transaction includes authority to do acts which are incidental to it, usually accompany it, or are reasonably necessary to accomplish it."

250. (1959) 1 WLR 403; (1959) 1 All ER 689 (CA).

251. See *BOWSTEAD ON AGENCY* (13th Edn by Reynolds and Davenport, 1968) 73. See also *Foujdar Kameshwar Dutt Singh v Ghanshyamdas*, 1987 Supp SCC 689, where the elder brother sold property and was held to be impliedly authorised by long acquiescence with open knowledge; *Banarsee Das v Ghulam Hossein*, (1869–70) 13 MIA 358, drawing and accepting of bills, implied authority if incidental to business. *Bank of Bengal v Ramanathan*, (1915–16) 43 IA 48; 43 Cal 527, authority to borrow implies authority to create a charge, pledge or mortgage. *Malukchand v Sham Mohan*, ILR (1890) 14 Bom 590; *Bank of Bengal v Fagan*, (1849) 5 MIA 27; 18 ER 804, authority to sell does not include authority to mortgage; *Pestonji Nesserwanjee Bottlewallah v Gool Mohd Sahib*, (1874) 7 Mad HCR 369, authority of a firm of merchants to run their ordinary business does not imply authority to accept bills, etc; *Satyanarayanan v Vithal*, AIR 1959 Bom 452, authority to sell present goods does not include authority to sell future goods.

252. Things necessary means things necessary for carrying out the purposes of agency. *Murugesu v Province of Madras*, AIR 1947 Mad 74, an agent appointed to take possession of land on expiry of lease cannot accept rent; *Phonographic Performance Ltd v Hotel Gold Regency*, AIR 2009 Del 11, a copyright-society cannot be authorised by the owner of copyright to institute proceedings on the owner's behalf. Such authorisation is not enforceable under the Copyright Act or Contract Act.

### Scope of authority

**S. 188. Extent of agent's authority.**—An agent, having an authority to do an act, has authority to do every lawful thing which is necessary in order to do such act.

An agent having an authority to carry on a business, has authority to do every lawful thing necessary for the purpose, or usually done in the course, of conducting such business.

#### *Illustrations*

- (a) *A* is employed by *B*, residing in London, to recover at Bombay a debt due to *B*. *A* may adopt any legal process necessary for purpose of recovering the debt, and may give a valid discharge for the same.
- (b) *A* constitutes *B*, his agent to carry on his business of a shipbuilder. *B* may purchase timber and other materials, and hire workmen, for the purpose of carrying on the business.

A well-known illustration is the case of *Dingle v Hare*.<sup>253</sup>

An agent was authorised to sell artificial manure. He had no authority to give any warranty about the goods. Yet he warranted to the buyer that the manure contained 30 per cent phosphate of lime.

The warranty turned out to be false and the principal was sued for its breach. He was held liable, because it was usual in the artificial manure trade to give a warranty of this kind. BYLES J said:

“When the jury found that it was usual to sell these artificial manures with a warranty, the nice distinction as to the extent of the agent’s authority became quite immaterial. An agent to sell has general authority to do all that is usual and necessary in the course of such employment.”

Thus every agent has the implied authority to act according to the customs and usages of a particular market or trade.<sup>254</sup> The principal is bound by such usages even if he is unaware of them<sup>255</sup> or even if they conflict with his instructions. Thus, where a bill-broker in London was entrusted with certain bills for discounting, and he pledged them, the principal was held bound as it was usual for bill-brokers in London to raise money by depositing their customers’ bills *en bloc*.<sup>256</sup>

But the custom or usage must not be unlawful or unreasonable. Whether a custom or usage is unlawful is a question of law. Any custom which changes

253. (1859) 7 CB (NS) 145: 29 LJ (CP) 143: 1 LT 38.

254. *Sutton v Tatham*, (1839) 10 Ad & E 27: 113 ER 11: 8 LJ QB 210; *Harker v Edwards*, (1887) 57 LJ QB 147 (CA). *Mahmud-Un-Nissa v Barkat Ullah*, AIR 1927 All 44, authority to carry on business, to receive and to spend moneys includes authority to borrow. *Murugan v G. Ramamurthy*, (2006) 1 AIR Kant 196, the driver of a motor lorry who was appointed by the owner appointed a cleaner, the insurance company was not permitted to deny the validity of the appointment and to say that his presence at the lorry was that of a stranger.

255. *Scott & Harton v Godfrey*, (1901) 2 KB 726.

256. *Foster v Pearson*, (1835) 1 CM & R 489: 4 IJ Ex 120.

the very nature of the agency, as for example, which converts the agent into a principal is unreasonable. *Robinson v Mollett*<sup>257</sup> is an illustration in point.

R authorised a broker M to purchase for him 50 tons of tallow. M supplied his own tallow as there was a custom in his trade to buy large quantities of tallow in his own name and then to allocate it to his principals.

The House of Lords held the custom to be unreasonable. It made M a wholesaler rather than an agent. It also created a conflict between his duty to the principal and his personal interest.

Similarly, a custom which gives the agent liberty to adjust his personal account by way of set-off or otherwise for the claims of the principal is unreasonable. Thus, where an agent was authorised to collect from the underwriters a sum of money due under a policy of insurance, he was not allowed to set-off his personal debts to the underwriters against that money although a custom to that effect was alleged.<sup>258</sup> The principal would, however, have been bound by this custom if he were aware of it.

The principle of *Dingle v Hare*<sup>259</sup> applies to all cases where the agent acts as a seller. For example, an agent appointed to sell a horse may warrant it as good if the principal is a horse dealer,<sup>260</sup> or if the sale is being held at a market place,<sup>261</sup> but not if it is a private sale.<sup>262</sup> Similarly, an agent to sell a property has authority to state the condition and value of the property to a proposed purchaser<sup>263</sup> and an agent to discount a bill may warrant it as a good bill, but he cannot endorse it.<sup>264</sup>

### Authority of special agents

#### Factor

A factor is a mercantile agent who is put in possession of the goods of his principal for sale. He has the authority to sell them in his own name,<sup>265</sup> to warrant them if it is usual to do so,<sup>266</sup> to fix the selling price and to receive payment.<sup>267</sup>

#### Broker

A broker is a mercantile agent appointed to sell the goods of his principal, but he is not given possession thereof. He may sell the goods in his own

257. (1874) LR 7 HL 802.

258. *Blackburn v Mason*, (1893) 68 LT 510; (1893) 9 TLR 286 (CA).

259. (1859) 7 CB (NS) 145.

260. *Howard v Sheward*, (1866) LR 2 CP 148.

261. *Brooks v Hassal*, (1883) 49 LT 569.

262. *Brady v Todd*, (1861) 9 CB (NS) 592; 127 RR 797.

263. *Mullens v Miller*, (1882) LR 22 Ch D 194.

264. *Fenn v Harrison*, (1791) 3 TR 757. *Amali English Medium High School v Govt of A.P.*, AIR 1993 AP 338, concession made by the Advocate General on behalf of the State, binding.

265. *Baring v Corrie*, (1818) 2 B & Ald 137; *Dixon, ex p.*, (1876) LR 4 Ch D 133.

266. *Dingle v Hare*, (1859) 7 CB (NS) 145; 29 LJ (CP) 143; 1 LT 38.

267. *Drinkwater v Goodwin*, 1775 Cowp 251.

name, and may receive payment.<sup>268</sup> But if he discloses the name of the principal, he cannot receive payment.<sup>269</sup> He may act according to the usual course of business except where a usage is unreasonable or unlawful. He may sell on reasonable credit.<sup>270</sup>

### *Estate or House Agent*

"A house or estate agent is in a different position from a broker at the stock exchange owing to the peculiarities of the property with which he has to deal and which does not pass by a short instrument as stocks and shares do, but has to be transferred after investigation of title as to which various stipulations, which might be of particular concern to the owner, may have to be inserted in a concluded contract relating to such property. The parties, therefore, do not ordinarily contemplate that the agent should have the authority to complete the transaction in such cases. That is why it has been held both in England and here, that authority given to a broker to negotiate a sale and find a purchaser, without furnishing him with all the terms means 'to find a man willing to become a purchaser and not to bind him and make him a purchaser'." This passage occurs in the judgment of the Supreme Court in *Abdulla Ahmed v Animendra Kissen Mitter*.<sup>271</sup>



CASE PILOT

The facts of the case were that an estate broker was appointed with an authority for one month to negotiate the sale of a property on certain terms as to price and with which his commission was also linked. Before the expiry of the month he found a customer ready and willing to purchase and communicated the fact to the principal. The principal terminated the authority of the agent and directly entered into account with a nominee of the person found by the agent. The agent claimed his commission.

It was held that the agent having negotiated the sale and secured a buyer who made a firm offer acquired the right to commission on the basis of the preferred price subject to the condition that the buyer should complete the transaction, and as this condition was fulfilled, the agent's right to commission became absolute and could not be affected by the circumstances that the principal for some reason of his own sold the property at a lower price.

A general power of attorney was constituted for dealing with existing properties of the principal as well as properties acquired after the appointment of the attorney. A contract made by him in the exercise of the power could not be cancelled. The purchaser had himself cancelled the agreement to buy. He claimed refund of the consideration. The vendor wanted to set-off his claim for damages for breach. The court said that this could be possible only on showing that he remained ready and willing to perform his part.

268. *Campbell v Hassell*, (1816) 1 Stark 233.

269. *Linck, Mocller & Co v Jameson & Co*, (1885) 2 TLR 206 (CA).

270. *Boorman v Brown*, (1842) 3 QB 511: 61 RR 287.

271. AIR 1950 SC 15: 1950 SCR 30, 36; see also *John v Philip*, (1987) 2 KLT 50 (SN).

The purchaser had justification in cancelling because the vendor's title was defective. The court said that this right of refund is available also to a person who had prior knowledge of the defect.<sup>272</sup>

#### *Auctioneer*

An auctioneer is an agent appointed to sell goods at a public auction. He, therefore, does not have the authority to sell by private contract.<sup>273</sup> He cannot sell on credit,<sup>274</sup> or accept any payment other than cash, or warrant the goods.<sup>275</sup> He acts both for seller and buyer and, therefore, can sign the contract for both.<sup>276</sup>

#### *Power of attorney holder*

Except where a matter is required to be done personally, acts and statements of a power of attorney are attributable to the principal. The principal was a non-resident landlord. He wanted to evict the tenant. The statement made by the attorney to the effect that his principal was in personal need of the premises was held to be receivable in evidence for ordering eviction.<sup>277</sup>

#### *Agent of Life Insurance Corporation*

An agent of the Life Insurance Corporation did not perform his duty to deposit the premium amount with LIC. It was held that LIC could not shirk its responsibility to pay the amount assured under the policy.<sup>278</sup>

#### *Ostensible or apparent authority*

The apparent authority of an agent is thus explained by DENNING LJ:<sup>279</sup> "Ostensible or apparent authority is the authority of an agent as it appears to others. It often coincides with actual authority. Thus, when the board (of directors) appoint one of their members to be a managing director they invest him not only with implied authority, but also with ostensible authority to do all such things as fall within the usual scope of that office. Other people who see him acting as managing director are entitled to assume that he has the usual authority of a managing director. But sometimes ostensible authority exceeds actual authority. For instance, when the board appoint the managing director, they may expressly limit his authority by saying he is not to order goods worth more than £ 500 without sanction of the board. In that case his actual authority is subject to the £ 500 limitation, but his *ostensible* authority includes all the usual authority of a managing director.

272. *R.L. Pinto v F.F. Menzes*, AIR 2001 Kant 141.

273. *Mews v Carr*, (1856) 1 H&N 484: 108 RR 683.

274. Payment by cheque, etc. may be accepted if there is a custom to that effect, *Bharat Survodaya Mills Co Ltd v Shree Ram Mills*, AIR 1959 Bom 309.

275. *Payne v Leconfield*, (1882) 51 LJ QB 642.

276. *Emerson v Heclis*, (1809) 11 RR 520.

277. *Satnam Channan v Darshan Singh*, AIR 2007 DOC 216 (P&H).

278. *Kota Central Coop Bank Ltd v District Legal Service Authority*, AIR 2016 Raj 1.

279. *Hely-Hutchinson v Brayhead Ltd*, (1968) 1 QB 549: (1967) 3 WLR 1408 (CA).

The company is bound by his *ostensible* authority in his dealings with those who do not know of the limitation. Thus, if he orders goods worth £1000, the company is bound to the other party who does not know of the £500 limitation.”

“When it is said that an agent’s act was within the scope of his apparent authority all that is meant is that the act appeared to be authorised”.<sup>280</sup> A leading authority is *Watteau v Fenwick*.<sup>281</sup>

The defendants had forbidden the manager of their hotel from buying cigars on credit. The plaintiff gave cigars to the manager on credit, which were used in business. The manager’s name appeared over the board, the plaintiff trusted him and had never heard of the defendants. Being unable to recover the price from the manager, the plaintiff sued the defendants.

The court found that “cigars were... such as would naturally be supplied to and dealt in such an establishment”. WILLS J, therefore, held that “once it is established that the defendant was the real principal, the ordinary doctrine as to principal and agent applied, that the principal is liable for all the acts of the agent which are within the authority usually confided to an agent of that character, notwithstanding limitations, as between the principal and the agent, put upon that authority”.<sup>282</sup> In another similar case, the manager of a public house was authorised to buy spirits only from A, but he bought them from another person telling him that he was a manager. The principal was held not liable, because the fact of agency was disclosed and it was well known that such managers had authority to buy only from authorised sources.<sup>283</sup> But if in the above case the fact of agency had not been disclosed, the principal would have been liable in the manner of a dormant partner.

Similarly, in a case before the Kerala High Court,<sup>284</sup> it was held that a person having responsibility to carry on the business of the store of a cooperative society must be deemed to have authority to purchase goods on credit notwithstanding that the society had advanced him enough money for the purpose.

A decision of the Allahabad High Court furnishes another illustration.<sup>285</sup>

In pursuance of an agreement the plaintiff despatched a wagonload of potatoes to the defendant. The latter refused to take delivery. The plaintiff then sent his agent to take delivery and to sell them at the available

280. J.L. Montrose, *Actual and Apparent Authority*, (1938) Can BR 757, 765.

281. (1893) 1 QB 346.

282. See also *Edmunds v Bushell and Jones*, (1865) LR 1 QB 97 where at p. 99 COCKBURN CJ observed: “[A] well-established principle is that if a person employs another as an agent in a character which involves a particular authority, he cannot by secret reservation divest him of that authority.”

283. *Daun v Simmins*, (1879) 41 LT 783.

284. *Valapad Coop Stores Ltd v Srinivasa Iyer*, AIR 1964 Ker 176.

285. *Ishaq Abdul Karim v Madan Lal*, AIR 1965 All 34. See, where Lord BLACKBURN observed that once an agent is clothed with ostensible authority, no private instructions can prevent his acts within the scope of that authority from binding his principal.

price. The defendant offered to the agent a less sum of money in full payment, which the agent accepted. The plaintiff received the money but brought an action for the balance.

It was held that the defendant could presume that the agent who was sent to sell at the available price had the ostensible authority to settle with the defendant at a less price.

In the above-cited Kerala case the court adopted from Smith and Watt's MERCANTILE LAW<sup>286</sup> the following statement on the distinction between "implied" and "ostensible authority": "Implied authority is real authority, the exercise of which is binding not only as between the principal and the third party, but also between principal and agent. It differs only from an express authority in that it is conferred by no express words, but is to be gathered from surrounding circumstances. The term "ostensible authority", on the other hand, denotes no authority at all. It is a phrase conveniently used to describe the position which arises when one person has clothed another, or allowed him to assume an appearance of authority to act on his behalf, without actually giving him any authority either express or implied, by which appearance of authority a third party is misled into believing that a real authority exists."<sup>287</sup>

#### *Apparent authority is real authority*

The statement portrays the truth in Lord ELLENBOROUGH's observation that "apparent authority is the real authority".<sup>288</sup> Whether there is appearance of authority in a particular case depends upon the facts of the case. An appearance of authority may, for example, arise from the course of business. A well-known authority is *Humbro v Burnard*.<sup>289</sup> Here an agent was authorised to underwrite insurance policies. The principal was held liable when he underwrote a guarantee policy because underwriting of guarantee policies was within the ordinary course of business of a Lloyd's underwriter.

#### *Appearance of authority arising from course of dealing*

An appearance of authority may arise from the course of dealing adopted in a particular case. Thus, where a principal once authorised his servant to purchase iron on credit and paid for it, he was liable when on a subsequent occasion he sent the servant with ready cash, but the servant again incurred credit.<sup>290</sup> But if the original act had been unauthorised, the principal would not have been liable for the second, even if he had paid for the first. "Thus in *Barrett v Irvine*,<sup>291</sup> it was laid down that a mother who has once paid for

286. (8th Edn, 1924) 177. *Valapad Coop Stores Ltd v Srinivasa Iyer*, AIR 1964 Ker 176.

287. Cited by MATHEW J in *Valapad Coop Stores Ltd v Srinivasa Iyer*, AIR 1964 Ker 176, 177.

288. *Pickering v Busk*, (1812) 15 East 38.

289. (1904) 2 KB 10.

290. *Hazard v Tredwell*, (1722) 1 Stra 506.

291. (1907) 2 ILR 462 (CA).

a horse for her infant son does not thereby raise an inference of a general authorisation to him to pledge her credit for his future equine purchases.”<sup>292</sup>

#### *Representation of authority by conduct*

A representation of apparent authority has to emanate from some conduct of the principal. There must be some conduct on his part which enables the agent to occupy a position of apparent authority. The representation which creates “apparent” authority may take a variety of forms of which the commonest is representation by conduct, that is, by permitting the agent to act in some way in the conduct of the principal’s business with other persons”.<sup>293</sup> For example, a principal used to order goods from the plaintiff. He had a servant whom he never authorised nor ever sent out for buying goods. The servant was dismissed and after that on two occasions he bought goods from the plaintiff in the principal’s name. Each time the principal paid the account in ignorance. He was held entitled to recover back the money, for he had done nothing to enable his servant to acquire an appearance of authority.<sup>294</sup> Where a Crown agent without ever having been so authorised, sold steel plates belonging to the Crown, the latter was not bound by the sale. The agent’s own representations could not create an apparent authority.<sup>295</sup> On the other hand, in the American case of *Kannelles v Locke*,<sup>296</sup> the principal was held liable for the act of a complete imposter. The plaintiff arrived at night at a small hotel. She was greeted by a man in the corridor. He booked a room for her and took charge of her valuable articles and issued a receipt in the principal’s name. He disappeared with the articles. The hotel-keeper was held liable because the imposter could not have occupied that position of apparent authority without the hotel-keeper’s negligence. In *Panorama Development (Guildford) Ltd v Fidelis Furnishing Fabrics*<sup>297</sup> the facts were:

The plaintiff ran a cars-on-hire business. The defendant company’s secretary hired cars from the plaintiff ostensibly for the company’s business, telling him that the cars were wanted to carry important customers of the company. He wrote on the company’s paper ordering the cars, signing himself “Company Secretary”. In fact, he used the cars himself and not for the company’s purposes.

It was held that the secretary had ostensible authority to enter into contracts for hiring cars for which the company must pay.

292. Borrowed from Hanbury, THE PRINCIPLES OF AGENCY (1952) 28, Irish reports being not available here. See also *Gillman v Robinson*, (1825) 1 C&P 642, where BEST CJ said (at p. 643): “I agree that one transaction is not enough to raise the presumption of a general authority, but several instances are sufficient.”

293. *Lateefa Begum v B.G. Kirloskar*, (2005) 11 SCC 515, the person in question was openly acting as agent in property matters. The principal not allowed to deny it. Specific recovery of property granted.

294. *Bailey & Whites Ltd v House*, (1915) 31 TLR 583.

295. *Attorney-General for Ceylone v Silva*, 1953 AC 461: (1953) 2 WLR 1185 (PC).

296. (1919) 12 Ohio App 210.

297. (1971) 2 QB 711: (1971) 3 WLR 440 (CA).

### *Continuance of apparent authority till termination*

An apparent authority once created continues to exist unless it is terminated by a notice to the third party. It cannot be terminated or restricted privately. Thus a principal who had terminated the authority of his agent who had occasionally bought wool for him was nevertheless held liable for the agent's further purchases as the supplier had no notice of the termination.<sup>298</sup> Similarly, where a man lived with his mistress as husband and wife and used to pay for the mistress's purchases, he was held liable for the purchases made after he had left her, because the supplier did not know of that fact.<sup>299</sup>

### *Agent's possession*

The possession of servant or agent is that of his master or principal for all purposes. A suit against servant or agent cannot be maintained on the basis of such possession.<sup>300</sup> "It is well settled that the possession of the agent is the possession of the principal and in view of the fiduciary relationship the defendant cannot be permitted to claim his own possession. This aspect was well emphasised in *David Lyell v John Lawson Kennedy*,<sup>301</sup> where the agent who was collecting the rents from the tenants on behalf of the owner and depositing it in a separate earmarked account continued to do so even after the death of the owner. After more than 12 years of the owner's death his heir's assignee brought the action against the agent for possession and the agent defendant pleaded adverse possession and limitation. The plaintiff succeeded in the first court. But the action was dismissed by the Court of Appeal. The House of Lords reversed the decision of the Court of Appeal and remarked, "For whom, and on whose behalf were those rents received after Ann Duncan's death? Not by the respondent for himself, or on his own behalf, anymore than during her lifetime". Emphasising the fiduciary character of the agent his possession was likened to that of trustee, a solicitor or an agent, receiving the rent under a power of attorney.

### *Employer's undertaking to pay insurance premia*

Where an employer, in a group savings linked insurance scheme, undertook to pay monthly premiums to the insurer from wages or salaries of employees, but when a worker died, it came to light that the premiums were in default, it was held that the insurer was bound to pay the insurance money to employee's family. The employer had become the agent of the insurer for the agreed purpose. Lack of consideration between the insurer and employer

298. *Dodsley v Varley*, (1840) 12 A&E 632.

299. *Ryan v Sams*, (1848) 12 QB 460. In *Summers v Solomon*, (1857) 7 E&B 879, the principal became responsible to a supplier who supplied jewellery to the shop manager as usual not knowing that he had been removed.

300. *Mahabir Prasad Jain v Ganga Singh*, (1999) 8 SCC 274: AIR 1999 SC 3873.

301. (1989) LR 14 AC 437. Cited in *Kamlesh v Jasbir Singh*, AIR 2004 P&H 216. Another case on matters of rent, *Corpn of Calicut v K. Sreenivasan*, (2002) 5 SCC 361: (2002) 1 RCR (Rent) 614.

was immaterial because no consideration is necessary at the time creation of agency. Consideration in such cases is promotion of business.<sup>302</sup> This line of decisions has found Supreme Court approval in *Life Insurance Corp v Rajiv Kumar Bhaskar*.<sup>303</sup> The employer became the agent of LIC for collection and payment of premia on the account of employees covered by the scheme. The insurer had to bear responsibility. After noting the contents of the scheme, the court said:

“The employers in terms of this tripartite arrangement accepted the responsibility of deducting the premium from the salaries of the same and send the same to the Corporation by one cheque. The concerned employees would have no knowledge about the contents of correspondence passed between the Corporation and their employers.”

“The employer’s letter to the Corporation indicates that no form of individual premium due notice or receipt would be issued by the Corporation which clearly shows that the entire responsibility was thrust upon the employer by the Corporation.”

Dealing with the arguments as to creation of agency the court said:

An agency can be created expressly or by necessary implication. It may be true that the employers in response to the proposal made by the Corporation stated that they would act as agents of their employees and not that of the Corporation, but, the expression “agent” in such circumstances may not mean to be one within the meaning of the Life Insurance Corporation of India (Agents) Regulation, 1972, made in terms of Section 49 of the Act: but would mean an agent in ordinary sense of the term. An employer would not be an agent in terms of the said Regulation on the premise that it was not appointed by the Corporation to solicit or procure life insurance business. The employers had no duty to discharge to the Corporation either under the Act or the rules and regulations framed thereunder but keeping in view the fact that the Corporation did not make any offer to the employees nor would directly make any communication with them regarding payment or non-payment of the premium or any other matter in relation thereto or connected therewith including the lapse of the policy, if any, it cannot be said that the employer had no role to play on behalf of the Corporation.

The Scheme clearly and unequivocally demonstrates that not only the contract of insurance was entered into by and between the employee and the insurer through the employer but even the terms and conditions of the policy were to be performed only through the employer. In that limited sense, the employers would be the agents of the insurer. In *BOWSTEAD & REYNOLDS*

302. *LIC v K. Rama Iyer*, 2004 AIR Kant 594: (2004) 1 Kant LJ 216 (DB), the premiums in respect of the employee were in default for four months up to the time of his death, the insurer was held liable. It was the default of the employer who was LIC’s agent.

303. (2005) 6 SCC 188: AIR 2005 SC 3087: (2005) 126 Comp Cas 809. *H.B. Gowramma v LIC*, 2006 SCC OnLine Kar 365: 2007 ACJ 1087 delay by school in sending payment under the scheme, even so LIC accepted, not allowed to say that the policy had lapsed.

ON AGENCY,<sup>304</sup> it is stated: "Where a person, by words or conduct, represents or permits it to be represented that another person has authority to act on his behalf, he is bound by the acts of that other person with respect to anyone dealing with him as an agent on the faith of any such representation, to the same extent as if such other person had the authority that he was represented to have even though he had no such actual authority."

In a scheme of group insurance of policemen, premium amounts were sent by the Police Department after deducting from respective salaries. The department failed to communicate to the insurer the fact of death of a policeman within the time stipulated in the policy and after which the insurer was not to be liable. It was held that in all matters in respect of the group policy, the Department was acting as an agent of the insurer. The information of the Department amounted to information of the insurer. Thus the insurer had attributed knowledge within time.<sup>305</sup>

### Statutory provision about apparent authority

The doctrine of ostensible authority is given statutory shape in Section 237 of the Contract Act.

**S. 237. Liability of principal inducing belief that agent's unauthorised acts were authorised.**—When an agent has, without authority, done acts or incurred obligations to third persons on behalf of his principal, the principal is bound by such acts or obligations if he has by his words or conduct induced such third persons to believe that such acts and obligations were within the scope of the agent's authority.

#### Illustrations

- A consigns goods to B for sale, and gives him instructions not to sell under a fixed price. C being ignorant of B's instructions, enters into a contract with B to buy the goods at a price lower than the reserved price. A is bound by the contract.
- A entrusts B with negotiable instruments endorsed in blank. B sells them to C in violation of private orders from A. The sale is good.

The provision has been used in quite a few cases to fix the principal with liability for unauthorised acts of his agent.<sup>306</sup> The prominent among them

304. (7th Edn) 307.

305. *Sushila Devi v State of Bihar*, 2005 AIHC 1514 (Pat); *LJC v Rajiv Kumar Bhaskar*, (2005) 6 SCC 188; AIR 2005 SC 3087; (2005) 126 Comp Cas 809.

306. See, for example, *Moosa Bhoy v V. Kristiah*, AIR 1952 Hyd 79, where a petty contractor was held liable for the money misappropriated by his agent put by him in charge of the work. See also *Dinabandhu Saha v Abdul Latif Molla*, ILR (1922) 50 Cal 258; *Vurdhman Bros v Radhakishan Jai Kishan*, AIR 1924 Nag 79; *K.S. Ramachandran v Coop Societies*, AIR 1963 Mad 105, where a clerk of the society was held to be authorised to receive payments. Representation of authority should have been towards the particular plaintiff and not to the world unless the plaintiff acted on that wider representation. *Phonographic Performance Ltd v Hotel Gold Regency*, AIR 2009 Del 11, a copyright society cannot be authorised by the owner of copyright to institute proceedings on the owner's behalf. Such authorisation is not enforceable under the Copyright Act or Contract Act.

seems to be a decision of the Nagpur High Court,<sup>307</sup> where a banking firm was held liable for the misappropriation of the funds of a customer by a person who, to the knowledge of the firm, was accepting deposits from customers. The court said:

“Their Lordships of the Judicial Committee of the Privy Council ruled in *Ram Pertab v Marshall*<sup>308</sup> that the right of a third party against the principal on the contract of his agent though made in excess of agent’s actual authority was nevertheless to be enforced when the evidence showed that the contracting party had been led into an honest belief in the existence of the authority to the extent apparent to him.”

#### *Actual or constructive notice of lack of authority*

Where, however, a person contracting with the agent has actual or constructive notice of any restriction on the agent’s ostensible authority, he is bound by the restriction. Thus where an agent, authorised by a power of attorney to operate a business, but not to borrow money, produced the power of attorney to a lender whom he asked for a loan, but the lender did not read it and advanced a loan, he could not recover it from the principal as he had constructive notice that the agent had no power to borrow.<sup>309</sup> Where a broker was permitted to receive payment for his principal’s goods by drawing upon the seller a bill of exchange and securing his acceptance to it, a payment made in that manner became binding upon the principal. But where the broker was authorised to receive payment only in respect of one previous contract, that was held to be not sufficient to create an apparent authority to receive such payments in the future also.<sup>310</sup> Once an ostensible authority is created, the principal becomes bound by agent’s acts within the scope of such authority. He cannot rely upon any private restrictions upon the agent’s authority.<sup>311</sup>

#### *Just and reasonable solution*

The ultimate question is whether the circumstances under which a servant has made a fraudulent misrepresentation which has caused loss to an

307. *Bisssessardas v Kabulchand*, AIR 1945 Nag 121: ILR 1945 Nag 204. An agent authorised to borrow on exceptional terms in an emergent situation, borrowed on exceptional terms without any emergency, yet the principal was held liable for the loan. *Montaignac v Shitta*, (1890) LR 15 AC 357. *Clifford George Pinto v M.R. Shenava*, (2005) 3 CCC 498 (Kant): AIR 2005 Kant HCR 316: (2005) 1 Kant LJ 458, power of attorney for sale of only one property, the other included by the attorney by forgery, neither the buyer was aware of it nor the power document created any such doubt, principal bound by the sale.

308. ILR (1898) 26 Cal 701.

309. *Jacobs v Morris*, (1902) 1 Ch 816 (CA).

310. *Kamal Singh Dugar v Corporated Engineers (India) (P) Ltd*, AIR 1963 Cal 464.

311. *Sarshar Ali v Roberts Cotton Assn*, (1963) 1 SC 244 (Pak); *Ram Pertab v Marshall*, ILR (1898) 26 Cal 701, where their Lordships of the Privy Council ruled that the rights of a third party against the principal on the contracts of his agent though made in excess of the agent’s actual authority were nevertheless to be enforced when the evidence showed that the contracting party had been led into an honest belief in the existence of the authority to the extent apparent to him.

innocent party contracting with him are such as to make it just for the employer to bear the loss. Such circumstances exist where the employer by words or conduct has induced the injured party to believe that the servant was acting in the lawful course of the employer's business. They do not exist where such belief, although it is present, has been brought about through misguided reliance on the servant himself, when the servant is not authorised to do what he is purporting to do, when what he is purporting to do is not within the class of acts that an employee in his position is usually authorised to do and when the employer has done nothing to represent that he is authorised to do it. Applying these principles to the facts of a case before it, the House of Lords held that where an agent was authorised to dispose of a ship, a charter-party granted by him did not bind the principal. The sale of a ship backed by a three-year charter-party is a transaction of wholly different character from a straightforward sale.<sup>312</sup>

Rule 8 of the Life Insurance Corporation (Agents) Rules, 1981 framed under Section 48(2)(cc) of the Life Insurance Corporation Act, 1956 prohibits agents from collecting premium on behalf of LIC. Accordingly, an implied or apparent authority could not be inferred for that purpose. The fact that LIC accepted the premium amount from him, which he had taken from his client, would not create an apparent authority in favour of the agent.<sup>313</sup>

#### *Agent's authority in emergency [S. 189]*

**S. 189. Agent's authority in an emergency.**—An agent has authority, in an emergency, to do all such acts for the purpose of protecting his principal from loss as would be done by a person of ordinary prudence, in his own case, under similar circumstances.

#### *Illustrations*

- (a) An agent for sale may have goods repaired if it be necessary.
- (b) A consigns provisions to B at Calcutta, with directions to send them immediately to C, at Cuttack. B may sell the provisions at Calcutta, if they will not bear journey to Cuttack without spoiling.

This section creates a special authority in emergency. It constitutes the agent into an agent of necessity to counteract the emergent situation. An act done in the exercise of this extended authority would bind the principal if the agent was not able to communicate with his principal and the course he took was necessary in the sense that it was the only reasonably prudent course left open to him and that he acted in good faith in the interest of the parties concerned.

312. *Armagas Ltd v Mundogas S.A.*, 1986 AC 717; (1985) 3 WLR 640 (CA).

313. *Harshad J. Shah v LIC*, (1997) 5 SCC 64: AIR 1997 SC 2459. The policy lapsed because of delay in payment by the agent. The Supreme Court ordered on compassionate grounds the insurer to pay back the total deposit amount with interest.

### Where agent exceeds authority

**S. 227. Principal how far bound, when agent exceeds authority.**—When an agent does more than he is authorised to do, and when the part of what he does, which is within his authority, can be separated from the part which is beyond his authority, so much only of what he does as is within his authority is binding as between him and his principal.

#### *Illustration*

A, being owner of a ship and cargo authorises B to procure an insurance for 4000 rupees on the ship. B procures a policy for 4000 rupees on the ship, and another for the like sum on the cargo. A is bound to pay the premium for the policy on the ship, but not the premium for the policy on the cargo.

**S. 228. Principal not bound when excess of agent's authority is not separable.**—When an agent does more than he is authorised to do, and what he does beyond the scope of his authority cannot be separated from what is within it, the principal is not bound to recognize the transaction.

#### *Illustration*

A authorises B to buy 500 sheep for him. B buys 500 sheep and 200 lambs for one sum of 6000 rupees. A may repudiate the whole transaction.

Where an agent exceeds his authority, actual or apparent, the principal is not bound by the excess work, but where it is separable from the authorised work the principal is bound to that extent. [S. 227] For example, an agent is authorised to insure a ship. He insures the ship as well as the goods under separate policies. The principal is bound only by the policy on the ship. If he had taken out only one policy in excess of instructions, the principal would not have been bound.<sup>314</sup> Where the agent was authorised to sell half a right over a property and he contracted to sell all the rights, the principal was held to be bound to the extent of half rights, they being separable from the rest.<sup>315</sup>

Where the authorised work is not separable from the rest, the principal may repudiate the whole of the transaction. [S. 228] For example, an agent is authorised to buy 500 sheep. He buys 500 sheep and 200 lambs for one sum of 6000 rupees. The principal may repudiate the whole transaction.<sup>316</sup> Where an agent was authorised to draw bills up to Rs 200 each, the principal was held not liable when the agent drew up to Rs 1000 each.<sup>317</sup> Similarly, where an agent was instructed to contract for the purchase of cotton to be delivered at the end of January, the principal was held not liable when the agent contracted for delivery in the middle of that month.<sup>318</sup>

314. *Brains v Ewing*, (1866) LR 1 Ex 320.

315. *Ahammed v Mammad Kunbi*, AIR 1987 Ker 228.

316. Illustration to S. 228.

317. *Premabhai Hemabhai v Brown*, (1873) 10 BHCR 319.

318. *Avlapa Nayak v Narsi Keshawji*, (1871) 8 Bom HC App Cas 19.

### Effect of notice to agent

**S. 229. Consequences of notice given to agent.**—Any notice given to or information obtained by the agent, provided it be given or obtained in the course of the business transacted by him for the principal, shall, as between the principal and third parties, have the same legal consequences as if it had been given to or obtained by the principal.

#### Illustrations

- (a) A is employed by B to buy from C certain goods, of which C is the apparent owner, and buys them accordingly. In the course of the treaty for the sale, A learns that the goods really belonged to D, but B is ignorant of that fact. B is not entitled to set-off a debt owing to him from C against the price of the goods.
- (b) A is employed by B to buy from C goods of which C is the apparent owner. A was, before he was so employed, a servant of C, and then learned that the goods really belonged to D, but B is ignorant of that fact. In spite of the knowledge of his agent, B may set-off against the price of the goods a debt owing to him from C.

The effect of the provision is that notice given to or information obtained by an agent in the course of the business transacted by him on behalf of his principal, shall, as between the principal and third parties have the same legal consequences as if it had been given to or obtained by the principal. Acting on the principle of the section the Calcutta High Court held that where the secretary of a society was *de facto* as well as *de jure* incharge of the affairs of the society, a notice given to him of the fact that a partner of a firm with which the society had dealings had retired, operated as a notice to the society.<sup>319</sup>

### Knowledge of broker

Whether a broker is acting as an agent of the assured or the insurer, depends upon the facts of each case. It has been held that when a broker has the power to bind the insurer, popularly known as "binder", he will be an agent of the insurer and his knowledge will be deemed to be the knowledge of the insurer. Thus, where a member of the broker's firm knew of the criminal past of the assured, the insurer was not permitted to deny liability on the ground that the past had not been disclosed.<sup>320</sup>

In such circumstances an assurance given by the broker would bind the insurer. In one such case the broker orally assured that the new car purchased by the assured would be substituted under the same policy for the old. The insurer was held liable though he was not in a position to give such substitution.<sup>321</sup>

### Liability for agent's wrongful acts [S. 238]

Section 238 of the Contract Act lays down the principle by which the liability of the principal for the wrongful acts of the agent is to be determined.

319. *Jani Nautamal Venishanker v Vivekanand Coop Housing Society Ltd*, AIR 1986 Guj 162.

320. *Woolcott v Excess Insurance Co Ltd*, (1978) 1 Lloyd's Rep 633 (CA).

321. *Stockton v Mason*, (1978) 2 Lloyd's Rep 430.

**S. 238. Effect, on agreement, of misrepresentation or fraud by agent.—**

Misrepresentations made, or frauds committed, by agents acting in the course of their business for their principals, have the same effect on agreements made by such agents as if such misrepresentations or frauds had been made or committed by the principals; but misrepresentations made, or frauds committed, by agents, in matters which do not fall within their authority, do not affect their principals.

*Illustrations*

- (a) *A*, being *B*'s agent for the sale of goods, induces *C* to buy them by a misrepresentation, which he was not authorized by *B* to make. The contract is voidable, as between *B* and *C*, at the option of *C*.
- (b) *A*, the captain of *B*'s ship signs bills of lading without having received on board the goods mentioned therein. The bills of lading are void as between *B* and the pretended consignor.

To fix the principal with vicarious liability for the wrongs of his agent it is necessary that the wrong must have been committed in the course of the principal's business. Although the particular act may not be authorised but if it is done in the course of carrying on the authorised business, the principal is liable.<sup>322</sup>

A master is liable for the wrongs of his servant committed in the course of the servant's employment, whereas a principal is liable for wrongs done by the agent in the course of business. The expression "course of business" has been generally taken to mean the same thing as "course of employment". Accordingly, the principles governing the master and servant relationship have been applied to that of principal and agent and also to partners. To quote Professor Street: "There has never been a time when cases on master and servant were not cited as authority in the law of principal and agent."<sup>323</sup>

Secondly, although Section 238 speaks of "misrepresentations" and "frauds" in reference to "agreements made by agents" the principle is applicable to all cases whether an agreement is involved or not.

322. For example, Lord LINDLEY in *Citizens' Life Assurance Co v Brown*, 1904 AC 423, 427, stated the principle of vicarious liability in the following words: "Although the particular act which gives the cause of action may not be authorised, still, if the act is done in the course of employment which is authorised then the master is liable for the act of his servant." This doctrine has been approved and acted upon by this Board in *Mackay v Commercial Bank of New Brunswick*, (1874) LR 5 PC 94; *Swire v Francis*, (1877) LR 3 AC 106 (PC), and the doctrine is as applicable to incorporated companies as to individuals. All doubt on this question was removed by the decision of the Court of Exchequer Chamber in *Barwick v English Joint Stock Bank*, (1867) LR 2 Ex 259, which is the leading case on this subject. It was distinctly *approved* by Lord SELBORNE in the House of Lords, in *Houldsworth v City of Glasgow Bank*, (1880) 5 AC 317, 326, and has been followed in numerous other cases. There can be no agency for doing wrongful acts. *A. Thangal Kunju Musaiar v M. Venkatachalam Potti*, AIR 1956 SC 246: (1955) 2 SCR 1196. The agent would be personally liable.

323. Street, FOUNDATIONS OF LEGAL LIABILITY, Vol 2, 454.

## Misrepresentations and frauds

An agent appointed to sell his principal's goods or property has often to make statements concerning the nature and quality of the property and, in his enthusiasm to find a customer, may make exaggerated statements. The law does not like to hold the principal liable for the agent's extravagant statements unless it finds some fault with the principal himself. If, for example, the principal has authorised a false statement to be made, or knows that it is being made by the agent or keeps the real facts from the agent, obviously the principal is liable. The liability of the principal is enforced, at the option of the third party, by avoiding the contract if it is still executory or by holding the principal liable in damages. Such liability came to the principal in the following three cases:

*Fuller v Wilson*:<sup>324</sup> An estate agent stated to the purchaser that the house under sale was free from rates and taxes. The principal was aware, but the agent was not, that the house was subject to taxes and taxes were levied soon after the plaintiff purchased the house. The principal would have been held liable if the plaintiff had relied on the representation. DENMAN CJ said "...if the purchaser was actually deceived in his bargain, the law will relieve him from it. We think the principal and his agent are for this purpose completely identified, and that the question is, not what was passing in the mind of either, but whether the purchaser was in fact deceived by them or either of them."

*London County Freehold & Leasehold Properties Ltd v Berkely Property & Investment Co Ltd*:<sup>325</sup> Negotiations were afoot for the sale of a block of flats by the defendant company to the plaintiff company. The solicitors of the plaintiff company, while going through the draft agreement, put a marginal note inquiring whether all the tenants were paying their rents regularly. The solicitors of the defendant company consulted the property manager of the company and then informed the plaintiffs, also by way of marginal note to the draft, that the tenants were paying rents regularly with immaterial exceptions. The statement turned out to be false. The defendant company was held liable in fraud because one of its agents (property manager) who knew the real facts had made a false statement, and the company has necessarily to act through its agents.

*Briess v Wooley*:<sup>326</sup> A director of a company started negotiations for a contract without any authority and made fraudulent misrepresentations. Subsequently he was authorised to complete the contract, but did nothing to correct the misrepresentations. The company was held liable.

In the following case the principals were held not liable:

*Cornfoot v Fowke*:<sup>327</sup> The plaintiff had employed an agent to let a house. The defendant was in contact with the agent for a house. The defendant asked

324. (1842) 3 CB 58.

325. (1936) 2 All ER 1039.

326. 1954 AC 333: (1954) 2 WLR 832 (HL).

327. (1840) 6 M&W 358: 55 RR 655.

the agent: "if there was any objection to the house", to which he answered that there was not; the defendant entered into and signed the agreement, but afterwards discovered that the adjoining house was a brothel, and on that ground declined to fulfil the agreement. He claimed the right to avoid the agreement as there was fraudulent concealment of a material fact. But he was held bound by the agreement. There was no guilt in the principal because he neither knew nor had authorised the statement to be made. There was no guilt in the agent because he did not know that there was a brothel.

This decision has been criticised.<sup>328</sup> It should be the duty of the principal to apprise the agent of the whole situation, otherwise he creates the risk of innocent misrepresentation being made by the agent. Moreover, rescission is allowed even for innocent misrepresentation and there was no reason why this should not have been attributed to the principal. If the principal had himself said "there was no objection to the house" he would have been guilty of fraud, and when he gives an ostensible position to his agent to make this statement, the elementary principle that "he who acts through another is deemed to act himself" should have been followed.

Despite criticism, the decision was followed in *Armstrong v Strain*.<sup>329</sup>

One Mr Strain, a retired practitioner, "owned a bungalow in an area notoriously prone to produce settlements because of the heavy clay sub soil. The bungalow had suffered severely from this scourge and had already been underpinned three times". He was naturally anxious to dispose it of and entrusted it to his partners for this purpose. His partners arranged it with another firm, which found Armstrongs as buyers. The bungalow was described to be "in a very nice condition" and one of the partners of the latter firm valued it at £2000 for mortgage purposes. The agents knew of the last underpinning but not of the two earlier ones. Within two months of the transaction the bungalow collapsed finally. But Armstrong's action to hold the principal liable in damages for the fraud failed. The court found no conscious falsehood and, therefore, acquitted the principal "and the unfortunate Armstrongs were left with the ruins of a bungalow".

The decision has been described by L.C.B. Gower as one that is socially undesirable and logically unsatisfying.<sup>330</sup> The learned writer has stated the position of English law in the following words:

The law is that a principal is not liable for fraud in respect of his agent's acts unless—

- (a) he intends or knowingly permits the agent to make a false statement, or

328. For critical analysis of this and contrary decisions see Patrick Devlin, *Fraudulent Misrepresentation: Division of Responsibility between Principal and Agent*, (1937) 53 LQR 344.

329. (1952) 1 KB 232; (1952) 1 KB 232 (CA).

330. L.C.B. Gower, *Agency and Fraud*, (1952) 15 Mod LR 232 at p. 234.

- (b) his agent acting within the actual or apparent scope of his authority makes a statement with knowledge of its falsity or recklessly not caring whether it be true or false.

### Agent's torts

"One who chooses to do business through an agent may in certain situations be liable for a tort committed by the agent. The doctrine of *respondeat superior* (let the superior answer) will be applied to make the principal liable where the agent commits a tort while engaged in the business of the principal, or, as it is commonly said, when the tort is committed by the agent while acting in the course of and within the scope of his agency."<sup>331</sup>

"An agent kicked a boy from a moving streetcar. The principal was held liable for assault and battery.<sup>332</sup> An agent, employed to collect evidence for his principal in a pending lawsuit, offered to bribe a witness. It was held that the act was within the course of the employment of the agent and that the principal was bound by it."<sup>333</sup>

It was at one time said, on the authority of *Barwick v English Joint Stock Bank*<sup>334</sup> that the principal would not be liable where the agent committed a tort for his personal benefit and not for the benefit of the principal. But the House of Lords in their decision in *Lloyd v Grace Smith & Co*<sup>335</sup> clearly ruled that the *Barwick* case was not an authority for any such principle and that the only condition of the principal's liability is that the act in question must be within the course of the agency business. The facts of the case were as follows:

Grace Smith & Co were a firm of solicitors of some repute and respectability. Mrs Lloyd, a widow, being dissatisfied with the income of her two cottages, consulted the firm's clerk, who was incharge of the conveyancing business, as to how to improve the income. He advised her to dispose of the cottages. He asked her to bring the title deeds which she did and obtained her signature on two papers. He converted these papers into a sale deed to himself and subsequently disposed of the property and misappropriated the proceeds. It was held "that the firm were responsible for the fraud committed by their representative in the course of his employment".<sup>336</sup>

Where the premium was to be deducted by the employer from the salary of the employee and for forwarding it to the insurer and this arrangement

331. *Atlantic Die Casting Co v Whiting Tubular Products Inc*, 337 Mich 414, reported in Stimson and Lazar, RECENT CASES AND MATERIALS ON BUSINESS LAW (1955) 131.

332. *Schultz v La Crosse City Rly Co*, (1907) 133 Wis 420.

333. *Chicago City Rly Co v McMahan*, 1882 ILJ 485. The statement is borrowed from Spencer and Gillam, A TEXT BOOK OF LAW AND BUSINESS, 280 (3rd Edn, 1952).

334. (1867) LR 2 Ex 259.

335. 1912 AC 716 (HL).

336. The relationship of a locker-holder with the bank is that of bailee and bailor and not that of landlord and tenant. The bank will be liable if an employee fraudulently tampers with a locker. *National Bank of Lahore Ltd v Sohan Lal*, AIR 1962 Punj 534: ILR (1962) 1 Punj 566.

was in terms of an agreement between the insurer and employer, it was held that the employer had become an agent of the insurer for this purpose. Failure of the employer to send two instalments by reason of which the policy was in a state of lapse at the time of the employee's death was not to go against the employee. It was the failure of the insurer's agent and not that of the employee.<sup>337</sup>

### RIGHTS AND LIABILITIES OF UNDISCLOSED PRINCIPAL

The rights and liabilities of a principal under contracts made by his agent depend upon whether—

- (a) The principal's existence and name were disclosed by the agent;
- (b) The principal's existence was disclosed but not his name;
- (c) Neither existence nor name of the principal was disclosed.

#### Where the principal is disclosed

Where the existence of the principal is disclosed, Section 226 applies, according to which the agent's acts and contracts "will have the same legal consequence as if the contracts had been entered into and the acts done by the principal in person". The principal may sue the third party upon the contract and *vice versa*. For example, where the agent is authorised to receive payment, a payment to him discharges the third party from his liability to the principal.

The agent can neither sue nor be sued upon a contract made by him on behalf of his principal. "The contract is the contract of the principal, not that of the agent, and *prima facie* at common law the only person who can sue is the principal and the only person who can be sued is the principal."<sup>338</sup>

#### Unnamed principal

Even where the agent does not disclose the name of his principal, but discloses his own representative character, the contract will be the contract of the principal, unless there is something in its form or signature to show that the agent intended to be personally liable. Where an agent signed the contract as a broker, "to my principals", but did not disclose who the principals were, he was not personally liable.<sup>339</sup> "There is nothing whatever on the contract to show that the defendant intended to act otherwise than as a broker."

#### Undisclosed principal

The doctrine of undisclosed principal comes into play when the agent neither discloses the existence of his principal nor his representative character.

337. *LIC v Mukesh Devi*, AIR 2002 Raj 404. Another similar ruling is *LIC v K. Rama Iyer*, 2004 AIR Kant 594: (2004) 1 Kant LJ 216 (DB), LIC not allowed to deny liability.

338. *Montgomerie v United Kingdom Mutual SS Assn*, (1891) 1 QB 370, 371, *per* WRIGHT J.

339. *Southwell v Bowditch*, (1875) LR 1 CPD 374.

In such circumstances the question arises what are the mutual rights and liabilities of the principal, the agent and the third party.

There is nothing unusual in this doctrine insofar as the relations between the agent and the third party are concerned. Since the agent has contracted in his own name, he is bound by the contract. He may be sued on it and he has the right to sue the third party, and the principal is not liable in such a case.<sup>340</sup>

But the principal too has the right to intervene and assert his position as an undisclosed party to the contract. This right of the principal is protected by the Contract Act itself. Section 231 declares:

If an agent makes a contract with a person who neither knows, nor has reason to suspect that he is an agent, his principal may require the performance of the contract;....

This right of the principal has been described as “anomalous” because it does not fit in any of the established principles of the law of contract.<sup>341</sup> “The rule which permits an undisclosed principal to sue and be sued on a contract to which he is not a party, though well-established, is itself an anomaly.”<sup>342</sup>

Similarly, in BOWSTEAD’S LAW OF AGENCY<sup>343</sup> the doctrine is described as “surprising but well-established by the cases.” Yet the doctrine has business convenience to recommend itself. But for this doctrine, the property or money of one person would have gone to enrich the estate of another person.<sup>344</sup> If, for example, an agent sells his principal’s property in his own name and receives the price, the principal is obviously entitled to trace his money and recover it, even if the agent has gone bankrupt. An action of this kind was allowed as early as 1710 in *Gurratt v Cullum*.<sup>345</sup>

But the principal’s right to sue the third party was established with an initial setback. In what has been considered to be the very first case, namely, *Scrimshire v Alderton*:<sup>346</sup>

A farmer’s oats were sold by a *del credere* factor without disclosing the name or existence of the farmer. The factor became bankrupt. The farmer discovered the buyer and informed him not to pay the factor. Even so the buyer paid him.

LEE CJ was of opinion that the buyer should be responsible to the undisclosed principal in such cases. “Here being notice before actual payment, there could be no harm done.” But the jury obstinately held for the defendant.

340. *J. Thomas (P) Ltd & Co v Bengal Jute Baling Co Ltd*, AIR 1979 Cal 20.

341. Cheshire and Fifoot, THE LAW OF CONTRACT (6th Edn, 1964) 418.

342. Lord DAVEY in *Keighley Maxseted & Co v Durant*, 1901 AC 240, 256 (HL).

343. (13th Edn by Reynolds & Davenport, 1968) 273.

344. The historical foundation of the doctrine is traced in Stoljar, THE LAW OF AGENCY (1961) 204–11.

345. 1710 Bull NP 42: Willes 400, 405–06.

346. (1743) 2 Stra 1182: 93 ER 1114.

The right of the undisclosed principal to intervene and sue the third party is, however, subject to the following qualifications. They are laid down in Sections 231 and 232.

**S. 231. Rights of parties to a contract made by agent not disclosed.**—If an agent makes a contract with a person who neither knows, nor has reason to suspect that he is an agent, his principal may require the performance of the contract; but the other contracting party has, as against the principal, the same rights as he would have had as against the agent if the agent had been principal.

If the principal discloses himself before the contract is completed, the other contracting party may refuse to fulfil the contract, if he can show that, if he had known who was the principal in the contract or if he had known that the agent was not a principal, he would not have entered into the contract.

**S. 232. Performance of contract with agent supposed to be principal.**—Where one man makes a contract with another, neither knowing nor having reasonable ground to suspect that the other is an agent the principal, if he requires the performance of the contract, can only obtain such performance subject to the rights and obligations subsisting between the agent and the other party to the contract.

#### *Illustration*

*A*, who owes 500 rupees to *B*, sells 1000 rupees worth of rice to *B*. *A* is acting as agent for *C* in the transaction, but *B* has no knowledge nor reasonable ground of suspicion that such is the case. *C* cannot compel *B* to take the rice without allowing him to set-off *A*'s debt.

#### *Subject to equities*

Firstly, the other contracting party would have against the principal “the same rights which he would have had against the agent if the agent had been principal”. This declaration of Section 231 is further supplemented by Section 232 which says that “the principal, if he requires the performance of the contract, can only obtain such performance subject to the rights and obligations subsisting between the agent and the other party to the contract”. The main concern of these sections is to ensure that the third party is not put to any disadvantage by the intervention of the principal. If, for example, the agent owes some money to the third party, which the latter could have set-off against the price of the goods sold to him, he would have the same right if the principal sues him for the price.<sup>347</sup> *Montagu v Forwood*<sup>348</sup> is an illustration in point.

The plaintiffs, who were acting for the owners of a cargo, employed *B & Co* as their agents to collect from underwriters contributions in respect of general average loss. *B & Co* not being brokers, employed the

347. See *Greer v Downs Supply Co*, (1927) 2 KB 28 (CA), where timber was purchased under the impression that the buyer would have set-off against the seller and the undisclosed principal of the seller was not allowed to intervene.

348. (1893) 2 QB 350 (CA).

defendants, who were brokers at Lloyd's, to collect the money, and they did so. At the time when the defendants received the money there was a debt due to them from *B & Co*. The defendants did not know and there was nothing to lead them to suppose, that *B & Co* were not acting as principals in the matter and the defendants believed that *B & Co* were acting as principals.

It was held that the defendants were entitled to stand in the position in which they would have stood if *B & Co* had really been principals; and that consequently, the defendants were entitled to set-off against the demand of the plaintiffs for the money which they had collected the debt due to them from *B & Co*.

The illustration appended to Section 232 is more or less to the same effect.

*A*, who owes 500 rupees to *B*, sells 1000 rupees worth of rice to *B*. *A* is acting as agent for *C* in the transaction, but *B* has no knowledge nor reasonable grounds of suspicion that such is the case. *C* cannot compel *B* to take the rice without allowing him to set-off *A*'s debt.

A contract to underwrite the shares of a company, i.e., to take up that portion of the shares which is not applied for by the public, was not allowed to be enforced by the undisclosed principal of the underwriter because an engagement of this kind proceeds upon the personal reputation and integrity of the underwriter.<sup>349</sup>

But where the third party does not believe the agent to be a principal or there are suspicious circumstances he may not be able to claim a set-off. Thus, for example, in *Isaac Cooke v Henry Douglas Eshelby*:<sup>350</sup>

*L & Co* sold cotton to *C*, in their own names, but really on behalf of an undisclosed principal. *C* knew that *L & Co* were in the habit of dealing both for principals and on their own account and had no belief on the subject whether they made this contract on their own account or for a principal.

It was held that *C* could not, in an action brought by the principal for the price of cotton, set-off a debt due from *L & Co*.

#### *Third party's right to repudiate executory contract*

Secondly, if the principal discloses himself before the contract is completed, the third party may repudiate the contract if he can show that if he had known who the principal was or that the agent was not the principal, he would not have contracted.<sup>351</sup> The right of the third party to repudiate the contract arises only when the identity of the undisclosed principal would

349. *Collins v Associated Greyhound Racecourses Ltd*, (1930) 1 Ch 1 (CA).

350. (1887) LR 12 AC 271 (HL).

351. S. 231. *Govt of Goa v Goa Urban Co-operative Bank Ltd*, (2011) 2 Mah LJ 37 (Bom), the act should be within the scope of the agent's authority.

have been so material to him that if he had known the true facts, he would not have contracted. Thus in *Said v Butt*.<sup>352</sup>

A theatre ticket was purchased by a person through an undisclosed agent knowing full well that a ticket would not have been issued to him on personal grounds. It was held that the theatre-owner had the right to repudiate the contract and exclude him from admission.

It means that an undisclosed principal cannot intervene when he knows that the other party would not have dealt with him. This principle will apply only when “some personal consideration (forms) a material ingredient”.<sup>353</sup> In *Dyster v Randall and Sons*<sup>354</sup> a piece of land was purchased by somebody for an undisclosed principal. The owner would not have sold the land to him, yet he was allowed to intervene and enforce the contract.<sup>355</sup>

#### *Undisclosed principal cannot intervene against express terms*

Lastly, an undisclosed principal cannot intervene if some express or implied term of the contract excludes him from doing so. Where, for example, an agent described himself in the contract as “owner”,<sup>356</sup> “proprietor”,<sup>357</sup> it shows an intention to make a personal contract and consequently precludes the undisclosed principal from intervening. But where, in a contract of letting out, the agent described himself as the “landlord”, evidence was allowed to show that he was only an agent. Similarly, “the description in a charter-party of one of the contracting parties as ‘charterer’ does not, of itself, designate him as the only person to fill that position”, and the undisclosed principal was allowed to sue for the breach of the charter-party.<sup>358</sup>

#### *Third party’s right against undisclosed principal*

Just as the undisclosed principal has the right to sue the third party, the latter has the right to sue the principal. Difficult questions in this connection have arisen where the principal has already paid the agent, trusting that he has paid or will pay the third party, but the agent has defaulted or has gone bankrupt before payment. This happened in *Davison v Donaldson*.<sup>359</sup>

The managing owner and the ship’s husband purchased goods on credit from the plaintiff for the purposes of the ship. The undisclosed partner settled his account with the husband believing that the latter had paid the

352. (1920) 3 KB 497.

353. *Dyster v Randall and Sons*, 1926 Ch 932, 939.

354. 1926 Ch 932.

355. Even where no personal considerations are involved and the third party was told that the agent was not acting for any principal, the third party can avoid the contract for fraud. *Archer v Stone*, (1898) 78 LT 34, cf *Berg v Sadler & Moore*, (1937) 2 KB 158 (CA).

356. *Humble v Hunter*, (1848) 12 QB 310, 317.

357. *Formby Bros v Formby*, (1910) 102 LT 116.

358. *Fred Drughorn Ltd v Rederiaktiebolaget Transatlantic*, 1919 AC 203.

359. (1882) LR 9 QBD 623.

plaintiff. But he had not done so and had gone bankrupt. The plaintiff sued the principal.

The court said: "Where a person is supplied with goods it is his duty to see that the seller is paid....Partners ought not to settle with their co-partners without satisfying themselves that the payments have been actually made."

#### PERSONAL LIABILITY OF AGENT [S. 230]

**S. 230. Agent cannot personally enforce, nor be bound by, contracts on behalf of principal.**—In the absence of any contract to that effect, an agent cannot personally enforce contract entered into by him on behalf of his principal, nor is he personally bound by them.

**Presumption of contract to contrary.**—Such a contract shall be presumed to exist in the following cases—

- (1) where the contract is made by an agent for the sale or purchase of goods for a merchant resident abroad;
- (2) where the agent does not disclose the name of his principal;
- (3) where the principal, though disclosed, cannot be sued.

#### Agent cannot sue or be sued unless contrary contract

It has already been seen that the chief function of an agent is to establish contractual relationship between his principal and third parties. The agent then drops out. He can neither sue nor be sued on contracts made by him on his principal's behalf. Section 230 accordingly provides: In the absence of any contract to that effect, an agent cannot personally enforce contracts entered into by him on behalf of his principal, nor is he personally bound by them.<sup>360</sup> Where a consignment was landed from a ship but the consignee did not take delivery and the question arose as to who was liable to pay demurrage, it was held that the liability was solely that of the consignee and not that of the shipping agent.<sup>361</sup> Similarly, in a case before the Calcutta High Court<sup>362</sup> it was apparent from the bill of lading that the document was signed by the agent of a principal who was named in the document. There was no contract to the effect that the agent would be bound by the contract. Thus, unless it is shown that there is a contract to the effect of binding the agent, entered into on behalf of the named principal, the agent cannot be bound

360. See *Marine Container Services South (P) Ltd v Go Go Garments*, (1998) 3 SCC 247: AIR 1999 SC 80, an agent of a contractor against whom there was a complaint under the Consumer Protection Act, 1986 for deficient services was held to be entitled to raise the defence of immunity and that defence could not be brushed aside without due consideration. *Tropic Shipping Co Ltd v Kothari Global Ltd*, (2002) 2 Bom CR 93, an agent not allowed to enforce an arbitration award.

361. *Port of Madras v Southern Shipping Corpn (P) Ltd*, AIR 2001 Mad 413 at p. 417. *Tashi Delek Gaming Solutions Ltd v State of Karnataka*, (2006) 1 SCC 442: AIR 2006 SC 661, advertising and other agents had the right to challenge the validity by means of a writ the ban on their work without the principal joining as a party.

362. *Jaytee Exports v Natvar Parekh Industries Ltd*, AIR 2001 Cal 150.

by it. The attachment of the bank account of the agent was not allowed to be continued. Earning of commission by the agent cannot make his agency as one coupled with interest. The mere fact that some of the persons were directors in the principal company as well as in the agency company was not a material fact when the principal was fully disclosed.<sup>363</sup>

This is known as the principle of the agent's immunity from personal liability. This rule applies even where the agent has contracted beyond his authority and the principal would not be liable. Even then the agent cannot be sued on the contract if he professed to act for the principal,<sup>364</sup> though he will then be liable to compensate the third party for his loss.<sup>365</sup>

But there are certain circumstances in which the agent incurs personal liability. Section 230, which incorporates the principle of agent's immunity for personal liability, says that there may be a contract to the contrary. In other words, the agent may contract to undertake personal liability. The section further goes on to provide that such contract is presumed in the following cases:

### Presumption of contrary contract

In the following cases there is presumption of a contract to the contrary:

#### 1. Foreign principal

When an agent contracts for "a merchant resident abroad" there is the presumption that the agent undertakes personal liability. [S. 230(1)] The original presumption of English law was that the agent alone was liable and he had no right to pledge the credit of a foreign principal. The presumption still stands, but it has declined in importance. The presumption was needed at a time when it was difficult to sue foreign principals and for the convenience of merchants a usage came into existence that the agent of a

363. Another case to the same effect *Midland Overseas v C.M.B.T. Tana*, AIR 1999 Bom 401, the contract of carriage was entered into by agent on behalf of foreign principal who was named and disclosed. The agent did not undertake any personal liability. The agent could not be sued personally for the alleged breach of contract. *K.M. Sankaran v DC*, (2004) 2 CTC 101, a power of attorney holder agent working as a disclosed agent was not allowed to be sued personally for dues against the principal. The judgment in the case of *Mackinnon Mackenzie & Co v Lang, Moir & Co*, ILR (1881) 5 Bom 584 an admitted position that the company was aware of the fact that the other contracting party was acting as an agent for a third party whose name was already known to the contracting party. *Prem Nath Motors Ltd v Anurag Mittal*, (2009) 16 SCC 274: AIR 2009 SC 567, the principal called applications for booking cars. The agent received applications with cheques drawn in favour of the principal. The claim of the petitioner was that he filed an application alongwith the cheque, but neither he received the car nor refund. The plea of the agent that the liability was of the principal and not his was held to be proper. *National Textile Corp v Nareshkumar Badrikumar Jagad*, (2011) 12 SCC 695: AIR 2012 SC 264, agent sued when principal known, the agent challenged it before the Supreme Court for the first time. It being a question of fact, the challenge was not entertained.

364. *Lewis v Nicholson*, (1852) 18 QB 503. Where the matter is doubtful as to who between the two is sueable, both should be sued. (1989) Malaysian LJ 187, SC Kuala Lumpur.

365. This liability arises under S. 235 as that of a pretended agent. He may be also sued for deceit.

foreign principal incurs personal liability. But now on account of changed conditions of international trade, merchants trust each other and agents do not like to incur personal liability. The resulting position has been summed up by SCRUTTON LJ in the following words: "While I think that one cannot at the present day attach the importance which used to be attached forty or fifty years ago to the fact that the supposed principal is a foreigner, it is still a matter to be taken into account in deciding whether the person said to be an English agent has or has not made himself personally liable."<sup>366</sup>

The presumption being still a part of the law, an agent can only overthrow it by contracting in a manner showing an intention not to incur personal liability. Thus, where a contract was signed "by the authority of our principals;...as agents", or "Greenwich Marine Incorporated as agents for Trader Export S.A."<sup>367</sup> it was held that this was sufficient manifestation of the intention to exclude personal liability.<sup>368</sup> Where a charter-party contract was signed by agents "for and on behalf of J.M. & Co (as agents), J.A.M." they were held to be not personally liable under the charter-party, although they were described as charterers.<sup>369</sup> Where a contract made through an agent for the import of metallic recovery expressly provided that the obligations of the principal or seller were not enforceable against the agent, a claim for shortage in metallic recovery against the agent was held to be not maintainable.<sup>370</sup>

Where there was a short landing of goods and a suit for damages was filed against the foreign principal, the carrier, it was held that the Indian agent was automatically discharged of liability. The court said that both the principal and agent could not be sued together.<sup>371</sup>

366. *H.O. Brandt & Co v H.N. Morris & Co Ltd*, (1917) 2 KB 784, 797, in some of the cases, however, it has been stated that the presumption has ceased to exist altogether and the whole question turns upon the intention of the parties. See, for example, PRITCHARD J in *Holt & Mosley Ltd v Cunningham & Partners*, (1949) 83 LIL Reports 141; quoted in Powell, THE LAW OF AGENCY, 252 (1961). A.H. Hudson in his three contributions, namely, *Agent of a Foreign Principal*, (1960) 23 Mod LR 695, and (1957) 35 Can BR 336; *Agents for Foreign Principals*, (1966) 29 Mod LR 353 has argued that the presumption still exists as part of the law. See also *Tehran Europe Co Ltd v S.T. Belton (Tractors) Ltd*, (1968) 2 QB 545. The matter depends upon as to whom the third party gave credit or may be presumed to have given credit. He cannot be presumed to have given credit to a foreign principal about whom he knows nothing. *James Machintosh & Co v Sree Yamuna Mills Co Ltd*, (1990) 2 KLJ 141.

367. *Tudor Marine Ltd v Tradax Export S.A.*, (1976) 2 Lloyd's Rep 135.

368. *Miller, Gibb & Co v Smith & Tyre Ltd*, (1917) 2 KB 141. See also *Lilly, Wilson & Co v Smales, Eeles & Co*, (1892) 1 QB 456, where also the mode of signature excluded liability of the agent who mistakenly quoted a wrong rate of freight.

369. *Universal Steam Navigation Co v James McElvie & Co*, 1923 AC 492 (HL). *MV X-press Annapurna v Gitanjali Woolens (P) Ltd*, AIR 2011 Bom 105, agent sued under a contract for carriage of goods by sea for non-delivery of goods. It was not a contract for sale or purchase of goods with a merchant resident abroad. Agent acted on behalf of a disclosed principal. No decree for damages could be passed against him.

370. *Nandan Iron and Metal Industries v Fenestry Inc*, AIR 1992 Del 364.

371. *W.B. Essential Commodities Supply Corpn Ltd v Koren Foreign Transportation Corpn*, AIR 2002 Cal 211.

By virtue of the provision in Section 230 the presumption has statutory force in India. A company registered in England, and having a place of business in India, has been held to be a foreign principal for the purposes of this presumption and the Indian agent acting for it was held personally liable.<sup>372</sup>

## 2. Principal unnamed

The presumption of agent's personal liability arises when he "does not disclose the name of his principal". Where an agent contracts for an undisclosed principal, he definitely is personally liable, being a party to the contract.<sup>373</sup> But when he contracts for an unnamed principal, there is only a presumption of his personal liability. The presumption may arise even where the agent discloses his representative character, but not the name of his principal. Accordingly, the honorary secretary of a school was held personally liable for the rent of a house hired by him in his own name though for purposes of the school.<sup>374</sup> But where an agent disclosed his character as the secretary of a club, personal liability could not be imposed on him.<sup>375</sup> The same result would follow where the representative character is already known to the third party.<sup>376</sup> But in every such case the form of contract will be the deciding factor. In an English case, a broker signed a contract in his own name, but had added: "Messrs Southwell, to my principal, etc." It was held that he was not personally liable.<sup>377</sup> "There is nothing whatever in the contract to show that the defendant intended to act otherwise than as broker." Where an order was placed over telephone by a broker to another broker for the supply of bunkers, the ordering broker was held to be not personally liable. The general practice in placing orders by telephone was not to disclose the name of the principal and, moreover, the supplier already knew that the order was sent by a broker.<sup>378</sup> Where, on the other hand, the usual mode of operation over telex of a forwarding agent was to remark, without disclosing the name of the principal, "We can do this for you", he was held

372. *Tutika Basavraju v Parry & Co*, ILR (1904) 27 Mad 315. *Shaw Wallace & Co Ltd v Union of India*, (2004) 5 CTC 308, where the agent was the first party liable for damage to the goods in transit and the second defendant was the owner of the vessel and, therefore, both being jointly liable invocation of S. 230 was not necessary. *Girish Chander v American Consolidation Services Ltd*, 2004 All LJ 3098; *Cochin Frozen Food Exports (P) Ltd v Vanchinad Agencies*, (2004) 13 SCC 434, disclosure or non-disclosure of principal, so far as S. 230 Exception (1) is concerned, is immaterial, the only requirement being that the principal should be resident abroad. See Ian Brown, *The significance of General and Special Authority in the Development of the Agent's Authority External Authority in English Law*, 2004 JBL 391.

373. *Castrol Ltd v Admiral Shipping Ltd*, (2005) 3 Bom CR 507, orders placed by agent without disclosing that he was acting for a principal and accepting all bills and invoices without any protest, nothing to show that he was acting for a foreign principal, the agent himself liable as a principal.

374. *Bhojabhai v Hayen Samuel*, ILR (1898) 22 Bom 754.

375. *NWP Club v Sadullah*, ILR (1898) 20 All 497.

376. *Mackinnon Mackenzie & Co v Lang, Moir & Co*, ILR (1881) 5 Bom 584.

377. *Southwell v Bowditch*, (1875) LR 1 CPD 374.

378. (N&J) *Vlassopoulos Ltd v Ney Shipping Ltd*, (1977) 1 Lloyd's Rep 478 (CA).

personally liable, though in that case he indicated the name of the liner to whom he was forwarding the goods.<sup>379</sup>

### *Liability of dealer under the Consumer Protection Act*

A dealer of motor vehicles was held personally liable under the Consumer Protection Act, 1986 for passing a defective vehicle to a consumer buyer. His defence was that the real liability should be that of the manufacturer. The National Commission said that the dealer may have his reimbursement from his principal against any such liability but so far as the consumer is concerned he was bound either to rectify the defect or take back the vehicle and refund the price.<sup>380</sup>

### **3. Non-existent or incompetent principal**

An agent is presumed to incur personal liability where he contracts on behalf of a principal who, "though disclosed cannot be sued". An agent who contracts for a minor, the minor being not liable, the agent becomes personally liable. This result may not, however, follow where the other party already knows that the principal is minor.<sup>381</sup> Similarly, where promoters buy goods on behalf of a projected company they become personally liable to pay for them. The company, being not in existence at the time of the contract, cannot be sued.<sup>382</sup> Now, by virtue of the provision in Section 9(2) of the European Communities Act, 1972, an agent of an unformed principal will be deemed to be contracting personally so as to entitle him to sue and be also sued on the contract. The Calcutta High Court did not permit an agent of the Russian Government to be sued personally because it was neither averred nor proved that the Government of Russia could not be sued in India or elsewhere. The mere fact that such a suit required permission of the Government of India could not be taken to mean that no suit was possible.<sup>383</sup>

### *Directors of company*

Directors of a company are not agents of the company in the conventional sense of the principal-agent relationship ordinarily, therefore, they are not liable in damages for breach of contract committed by their company. Even if they are agents, Section 230 confers immunity on an agent against personal liability provided only that the contract has been made in the representative capacity for and on behalf of the principal. There are no doubt some exceptions. But it is a general principal and not an exception that an

379. *Salsi v Jetspeed Air Services Ltd*, (1977) 2 Lloyd's Rep 57. *Shriniwas Shankar Potnis v Raghubul Sahakari Griharachana Sanstha Maryadit*, (2010) 1 Mah LJ 368, third party can refuse to perform contract made by agent without disclosing for whom he was contracting.

380. *Marikar (Motors) Ltd v Lalan Carmu*, (2004) 1 All LJ 522 (NC).

381. *Shet Manibhai v Bai Rupaliba*, ILR (1899) 24 Bom 160.

382. *Kelner v Baxter*, (1866) LR 2 CP 174. By virtue of S. 9(2) of the European Communities Act, an agent of an unformed company becomes personally liable. See *Phonogram Ltd v Lane*, 1982 QB 938; (1981) 3 WLR 736 (CA).

383. *Union of India v Chinoy Chablani & Co*, AIR 1976 Cal 467.

agent committing tort or some other wrong, for example, inducing a person to make a loan to the company by making a fraudulent representation, the director would be personally liable.<sup>384</sup>

*Election by third party [S. 233]*

**S. 233. Right of person dealing with agent personally liable.**—In cases where the agent is personally liable, a person dealing with him may hold either him or his principal, or both of them liable.

In all the above situations “where the agent is personally liable, a person dealing with him may hold either him or his principal, or both of them, liable.” The only illustration given in the section says:

*A enters into a contract with B to sell him 100 bales of cotton and afterwards discovers that B was acting as agent for C. A may sue either B or C, or both, for the price of the cotton.*

This seems to be a departure from the English law, where the third party has to elect between the liability of the principal or agent and the election once made is final and binding on him.<sup>385</sup> If, for example, he has obtained judgment against the agent, he cannot afterwards sue the principal even if the judgment against the agent has remained unsatisfied.<sup>386</sup> But this rule has been criticised.<sup>387</sup> Clearly it is contrary to justice that *T* should not be able to sue *P* if his judgment against *A* is unsatisfied. The rule works particularly harshly where *T* does not even know of *P*’s existence until after he has obtained judgment against *A*.<sup>388</sup>

It is perhaps for this reason that the Indian Legislature marked a departure from the English rule and allowed the third party to sue the agent and the principal jointly. COUTTS-TROTTER CJ of the Madras High Court doubted whether this was the intention of the Legislature and opined that the English rule should be followed.<sup>389</sup> But a subsequent Division Bench of the same High Court disagreed with him. LEACH CJ said: “There is no ambiguity in the language used in the section and I am unable to see anything unreasonable in the rule, which it embodies. What would be the position if a suit is brought against the principal after judgment had been obtained against the agent in an earlier suit is another matter, but we are not called upon to consider that question here.”<sup>390</sup> Earlier the Bombay High Court had also held that the section plainly intends to create joint liability.<sup>391</sup>

384. *Tristar Consultants v Customer Service India (P) Ltd*, AIR 2007 Del 157.

385. *Kendall v Hamilton*, (1879) LR 4 AC 504 (HL).

386. Mere commencement of proceedings constitutes evidence of election but that is rebuttable. *Clarkson Booker Ltd v Andjel*, (1964) 2 QB 775: (1964) 3 WLR 466 (CA).

387. See the dissenting judgment of Lord PENZANCE in *Kendall v Hamilton*, (1879) LR 4 AC 504 (HL), where he described it as “unbending and indiscriminate”.

388. Powell, THE LAW OF AGENCY (2nd Edn, 1961) 270.

389. *Kuttikrishnan Nair v Appa Nair*, ILR (1926) 49 Mad 900, 902: AIR 1926 Mad 1213.

390. *Shamsuddin v Shaw Wallace & Co*, ILR 1939 Mad 282: AIR 1939 Mad 520.

391. *Shivlal Motilal v Birdichand Jivraj*, 1917 SCC OnLine Bom 68: AIR 1917 Bom 268.

But it seems that even under this section some kind of election is likely to be involved. The third party has to choose between the liability of the agent, or the principal or both and the choice once made shall bind him.

Election may be express or implied from conduct. An implied election takes place when the third party debits the account of the principal or the agent,<sup>392</sup> receives a negotiable instrument from one or the other in payment of the price, or sues one or the other. Filing of a suit is a strong *prima facie* evidence of election, but is not conclusive.<sup>393</sup>

#### *Estoppel of third party [S. 234]*

**S. 234. Consequence of inducing agent or principal to act on belief that principal or agent will be held exclusively liable.**—When a person who has made a contract with an agent induces the agent to act upon the belief that the principal only will be held liable, or induces the principal to act upon the belief that the agent only will be held liable, he cannot afterwards hold liable the agent or principal respectively.

One method of electing between the principal and the agent is indicated by Section 234. If the third party leads the agent to believe that only the principal will be held liable or the principal to believe that only the agent will be held liable, he cannot afterwards change his stance. He would have to confine himself to the liability of a person whom he has selected by that process. Thus where a purchaser of goods gave notice to the seller's agent that the agent alone would be held responsible if the goods did not turn out to be of contract quality, he could not proceed against the principal.<sup>394</sup>

#### 4. Pretended agent [S. 235]

**S. 235. Liability of pretended agent.**—A person untruly representing himself to be the authorised agent of another, and thereby inducing a third person to deal with him as such agent, is liable, if his alleged employer does not ratify his acts, to make compensation to the other in respect of any loss or damage which he has incurred by so dealing.

Thus where a person pretends to act as the agent of another, he may be saved by the principal by ratifying his act. But if no ratification is forthcoming the pretended agent becomes personally liable to the third party for any loss that he may have suffered by relying upon the representation of authority. It would make no difference to his liability that he honestly believed that he had the authority in question or that, even if he did not have it, his principal would ratify his act.<sup>395</sup> The false representation must be the cause of the

392. *Addison v Gandasequi*, (1812) 4 Taunt 574.

393. *Scarf v Jardine*, (1882) LR 7 AC 345; *Clarkson Booker Ltd v Andjel*, (1964) 2 QB 775: (1964) 3 WLR 466 (CA).

394. *Madhadev Ganga Prasad v Gouri Shankar Sanganaria*, ILR (1949) 1 Cut 453: AIR 1950 Ori 42.

395. *Collins v Wright*, Collins v Wright, (1857) 8 E&B 647, approved in *Starkey v Bank of England*, 1903 AC 114 (HL).

contract. A person who acknowledged the liability of a firm pretending to be one of its partners was held to have incurred personal liability under the acknowledgment.<sup>396</sup> Since the action in such cases is under the tort of deceit, tort principles as to damages would apply rather than those applicable to breach of contract.<sup>397</sup> If the truth is already known to the other party, no liability arises.<sup>398</sup>

Where the pretension is as to a matter of law, the agent would not be liable. For example, the borrowing power of a company is a matter of interpretation of its constitutional documents and governing statutes. A misrepresentation as to this will not create liability.<sup>399</sup> But whether borrowing powers have been exhausted, is a question of fact. Liability would follow if this fact is misrepresented.<sup>400</sup>

The agent himself cannot sue on a contract which he has made pretending to be an agent. This disability is clinched upon him by Section 236.

**S. 236. Person falsely contracting as agent, not entitled to performance.**—A person with whom a contract has been entered into the character of agent is not entitled to require the performance of it, if he was in reality acting, not as agent, but on his own account.

When a person has, in fact, no principal, yet persuades the other to contract with him as an agent of another, he is estopped from saying that he had no principal, and since the contract was with his principal and not with him he has no locus standi to sue under that right. This will be so whether he feigns a named or unnamed principal.<sup>401</sup> Where a shipping agent gave a personal commitment of issuing a bill of lading after mate's receipt but did not do so, he was held personally liable to the principal for the tort of conversion and for breach of contract under Section 73 of the Contract Act.<sup>402</sup>

## 5. Breach of warranty of authority

Closely allied to the liability of a pretended agent is the liability of an agent for breach of warranty of authority. Where a person is in fact an agent, but exceeds his authority, or represents to have a kind of authority which he in fact does not have, he commits breach of warranty of authority and is personally liable to the third party for any loss caused to him by reason of acting on the false representation.<sup>403</sup> This is the principle of *Collins v Wright*.<sup>404</sup>

396. *Bheek Chand v Parbhaji*, AIR 1963 Raj 84: ILR (1963) 13 Raj 84.

397. *Vairavan Chettiar v Avicha Chettiar*, ILR (1915) 38 Mad 275.

398. *Shet Manibhai v Bai Rupaliba*, ILR (1899) 24 Bom 160, a mother representing herself to be the agent of her minor son, was held not liable as the other party already knew the principal's minority.

399. *Saffron Walden Benefit Building Society v Rayner*, (1880) LR 14 Ch D 406 (CA).

400. *Oliver v Bank of England*, (1901) 1 Ch 652, 660 (CA).

401. *Gopal Sridhar v Sashi Bhushan*, ILR (1933) 60 Cal 111: AIR 1933 Cal 109.

402. *Nepal Food Corpn v U.P.T. Import and Export Ltd*, AIR 1988 Cal 283.

403. *Ganpat Prasad v Sarju*, (1912) 9 All LJ 8.

404. (1857) 8 E&B 647: 27 LJ QB 215: 30 LT 209.

W was land agent for one G. W agreed to grant to the plaintiff a lease of G's farm for 12½ years. He honestly believed that he had the authority to do so. But G refused to execute the lease and he proved that he had given no such authority to the agent. W, having died in the meantime, the plaintiff sued his executors for the loss he had suffered in entering upon the farm, and they were held liable.

WILLES J said:<sup>405</sup> "The fact that the professed agent honestly thinks that he has authority that affects the moral character of his act; but his moral innocence, so far as the person whom he has induced to contract is concerned, in no way aids such person, or alleviates the inconvenience and damage which he sustains. The obligation arising in such a case is well expressed by saying that a person, professing to contract as agent for another, impliedly, if not expressly, undertakes to or promises the person who enters into such contract, upon the faith to the professed agent being duly authorised, that the authority which he professes to have does in point of fact exist."<sup>406</sup>

Similarly, in *Yonge v Toynbee*<sup>407</sup> an agent was held liable for prosecuting an action even after his principal, though unknown to him, had become insane, for the insanity had determined the agent's authority at once. An agent was held liable to a person to whom he chartered his principal's ship without authority of the principal who repudiated the transaction.<sup>408</sup> An agent gives warranty of his authority; he does not guarantee that, if the contract is within authority, the principal would not commit breach.

## RATIFICATION

The doctrine of ratification comes into play when a person has done an act on behalf of another without his knowledge or consent. The doctrine gives the person on whose behalf the act is done an option either to adopt the act by ratification or to disown it. Ratification is thus a kind of affirmation of unauthorised acts. It is thus explained in Section 196:

**S. 196. Right of person as to acts done for him without his authority: Effect of ratification.**—Where acts are done by one person on behalf of another, but without his knowledge or authority, he may elect to ratify or to disown such acts. If he ratify them, the same effects will follow as if they had been performed by his authority.

405. *Collins v Wright*, (1857) 8 E&B 647 (657): 27 LJ QB 215: 30 LT 209.

406. The principle of this case applies to all cases where a person induces another to do an act on the faith of his representation. See, for example, *Starkey v Bank of England*, 1903 AC 114 (HL), transfer to consols by the bank on the faith of the defendant's representation that he had the power of attorney to authorise the transfer; *Sheffield Corpn v Barclay*, 1905 AC 392, a banker innocently inducing a corporation to act on the basis of a forged deed; *Bank of England v Cutler*, (1908) 2 KB 208 (CA), the agent innocently introducing certain person as the owner of stock, when he was not so in fact.

407. (1910) 1 KB 215 (CA).

408. *Weigall S. & Co v Runciman & Co*, (1916) 85 LJKB 187 (CA), the agent was authorised to hire a ship but he mistook the instruction and let out a ship.

Where, for example, a person insures the goods of another without his authority, the owner may ratify the policy and then the policy will be as valid as if the agent had been authorised to insure the goods.<sup>409</sup>

Ratification may be expressed or implied. Section 197 provides:

**S. 197. Ratification may be expressed or implied.**—Ratification may be expressed or may be implied in the conduct of the person on whose behalf the acts are done.

#### *Illustrations*

- (a) *A, without authority, buys goods for B. Afterwards B sells them to C on his own account; B's conduct implies a ratification of the purchase made for him by A.*
- (b) *A, without B's authority, lends B's money to C. Afterwards B accepts interest on the money from C. B's conduct implies a ratification of the loan.*

Where the manager of an insurance company effected an assurance which he had no authority to do, but the company accepted the money which was received under the policy, that was held to be a sufficient ratification.<sup>410</sup> “Ratification will be implied from any act showing an intention to adopt the transaction, even silence or mere acquiescence<sup>411</sup> and if an act is adopted at all, it will be held to have been adopted throughout.” Ratification of a contract required to be in writing need not be in writing, but ratification of a contract made by deed must be by deed.<sup>412</sup>

#### **Requirements of ratification**

A valid ratification has to fulfil certain conditions. Some of them are as follows:—

##### *1. On behalf of another*

In the first place, it is necessary that the act in question must have been done on behalf of the person who wants to ratify it. The agent must profess to act as an agent and on behalf of an identifiable principal. “It is not necessary that he should be named, but there must be such a description of him as shall amount to a reasonable designation of the person intended to be

409. *Secy of State in Council for India v Kamachee Boye*, 7 MIA 476, unauthorised act of an agent ratified by the Government.

410. *Hukumchand Insurance Co Ltd v Bank of Baroda*, AIR 1977 Kant 204. A mere participation in arbitration proceedings has been held to be no ratification. *Union of India v A.L. Rallia Ram*, AIR 1963 SC 1685: (1964) 3 SCR 164. *T. R. Bhavani Shankar Joshi v Gordhandas Jamnadas*, (1942-43) 70 IA 50: AIR 1943 PC 66, 68. Ratification becomes effective when it is communicated. *Raja Gopalacharyulu v Secy of State*, ILR 38 Mad 997.

411. *Bank of Melli Iren v Barclays Bank*, (1951) 2 TLR 1057, silence of landlord as to repairs by tenant. *Ashok Kumar J. Pandya v Suyog Coop Housing Society Ltd*, AIR 2003 NOC 118 (Guj): 2002 AIHC 3401, ratification is affirmation of a contract already made and as on the date on which it was made. It is not the making of a new contract to the effect that the parties would be bound by the old contract, nor is it the making of new contract in terms of the old one. A contract which has no legal validity cannot, therefore, be ratified.

412. CHITTY ON CONTRACTS (24th Edn, 1977) 9, para 2019, citing *Commercial Banking Co of Sydney Ltd v Mann*, 1961 AC 1: (1960) 3 WLR 726.

bound by the contract.”<sup>413</sup> If the agent acts in his own name and “makes no allusion to agency”<sup>414</sup> his act cannot be ratified by any other person, even if the agent in his secret mind intended to act for another. This is the principle of the famous case of *Keighley Maxseted & Co v Durant*.<sup>415</sup>

K.M. & Co, authorised their agent to buy Karachi wheat at specified rates on their joint account. Wheat was not obtainable at those rates. He bought wheat from Durant at a higher rate. He did so in the hope and confidence that his act would be adopted by the principals, but he never mentioned the principals and contracted in his own name. The principals approved the purchase, but, when the price of wheat fell, refused to take delivery. Durant sued the agent and the principals for breach of contract.

But the principals were held not liable. The agent, having contracted in his own name, his act was not open to anybody's ratification and, therefore, the purported ratification was ineffective. Lord MACNAGHTEN said: “[B]y a wholesome and convenient fiction, a person ratifying the act of another, who, without authority, has made a contract openly and avowedly on his behalf, is deemed to be a party to the contract. Does the fiction cover the case of a person who makes no avowal at all, but assumes to act for himself and for no one else? On principle I should say certainly not.... [O]bligations are not to be created by, or founded upon, undisclosed intentions.”<sup>416</sup>

Similarly Lord JAMES said: [at p. 251] “To establish that a man's thoughts unexpressed and unrecorded can form the basis of a contract so as to bind other persons and make them liable on a contract they never made with persons they never heard of, seems a somewhat difficult task.”

The words “on behalf of another” as used in Section 196 expressly recognise this rule.<sup>417</sup> The section, however, does not insist upon the name of the principal being disclosed. Marine insurance policies are often effected on behalf of anybody interested and are, therefore, open to anybody's ratification.<sup>418</sup> Where the act is purported to be done on behalf of another, that other may ratify even if the agent used his name to commit a fraud upon the third party.<sup>419</sup>

413. WILLES J: *Watson v Swann*, (1862) 11 CB (NS) 756, 771: 142 ER 993.

414. Cheshire and Fifoot, THE LAW OF CONTRACT, 405 (6th Edn, 1964).

415. 1901 AC 240, 256 (HL).

416. *Keighley, Maxeted & Co v Durant*, 1901 AC 240 at p. 247.

417. *Raja Rai Bhagwat Dayal Singh v Debi Dayal Sahu*, (1907–08) 35 IA 48; *R. Raghavachari v M.A. Pakkiri Mahomed*, 1916 SCC OnLine Mad 403: AIR 1917 Mad 250, an agent buying in his own name against the directions of his principal a property at a court auction, the principal's subsequent ratification of no effect.

418. *Hagedorn v Oliverson*, (1814) 2 M&S 485; Arnold, MARINE INSURANCE. In other cases, there is a general insistence that the principal should be named and disclosed. *Boston Fruit Co v British & Foreign Marine Insurance Co*, 1906 AC 336, 338–39 (HL).

419. *Tiedemann & Ledermann Freres, re*, (1899) 2 QB 66. After ratification, the principal is bound by the act whether it is to his advantage or detriment and whether liability therefor is founded in contract or in tort, to the same extent and with all the same consequences as if it has been done by his previous authority.

## 2. *Competence of principal*

Since ratification relates back to the date when the contract was originally made by the agent, it is necessary that the principal who purports to ratify must be in existence at the time of the contract and should also be competent. It is this principle which prevents a person from ratifying a contract made by him during his minority. Similarly, a company cannot ratify a contract made in its name before its incorporation.<sup>420</sup> But this is subject to the provisions of the Specific Relief Act, 1963. Section 15 of the Act provides that where the promoters of a public company have made a contract before its incorporation, for the purposes of the company, and if the contract is warranted by the terms of incorporation, the company may enforce it. "Warranted by the terms of incorporation" means within the scope of the company's objects as stated in the memorandum. The contract should be for the purposes of the company. A contract to allot shares after the company is incorporated is not for the purposes of the company so that the company cannot enforce it against the other party.<sup>421</sup>

Section 19 of the same Act provides that the other party can also enforce the contract if the company has adopted it after incorporation and the contract is within the terms of incorporation.

## 3. *What acts can be ratified (Act should be lawful) [S. 200]*

**S. 200. Ratification of unauthorised act cannot injure third person.**—An act done by one person on behalf of another, without such other person's authority, which, if done with authority, would have the effect of subjecting a third person to damages, or of terminating any right or interest of a third person, cannot by ratification, be made to have such effect.

### *Illustrations*

- (a) *A*, not being authorized thereto by *B*, demands, on behalf of *B*, the delivery of a chattel, the property of *B*, from *C*, who is in possession of it. This demand cannot be ratified by *B*, so as to make *C* liable for damages for his refusal to deliver.
- (b) *A* holds a lease from *B*, terminable on three months' notice. *C*, an unauthorized person, gives notice of termination to *A*. The notice cannot be ratified by *B*, so as to be binding on *A*.

**ONLY LAWFUL ACTS CAN BE RATIFIED.**—Only lawful acts are open to ratification. An act which is void from the very beginning cannot be ratified. The Privy Council observed in a case<sup>422</sup> that ratification "must be in relation

420. Except as provided in Specific Relief Act, 1963, an unincorporated company is not able to act before incorporation. *Kelner v Baxter*, (1866) LR 2 CP 174; *Ganesh Flour Mills Co v Puran Mal*, 1905 Punj Rec No 2. An unauthorised act once ratified does not create an authority for such future acts. *Irvine v Union Bank of Australia*, ILR (1875-78) 3 Cal 280, 285-86.

421. *Imperial Ice Mfg Co v Munchershaw Barjorji Wadia*, ILR (1889) 13 Bom 415.

422. *La Banque Jacques-Cartier v La Banque d'Epargne*, (1887) LR 13 AC 111 (PC), an appeal from the Province of Quebec. Void acts cannot be ratified. *Mulamchand v State of M.P.*, AIR 1968 SC 1218: (1968) 3 SCR 214; *State of U.P. v Murari Lal & Bros Ltd*, (1971) 2 SCC 449: AIR 1971 SC 2210. No ratification of a Government contract made in contravention

to a transaction which may be valid in itself and not illegal". Where money was entrusted to a person for investment and he put it to his own use, it was held by the Privy Council that the doctrine of ratification could not be used to validate this breach of fiduciary obligation.<sup>423</sup> Where the managing director of a corporation removed an employee belonging to a category of employees whom he was not authorised to remove, it was held that the act was an illegal termination of employment and could not be cured by ratification.<sup>424</sup>

Subject to this, any act may be ratified "whether it is founded on a tort or on a contract". A forgery of signatures, being a crime, cannot be ratified.<sup>425</sup> A minor's agreement being void cannot be ratified by him on attaining majority.

**ACTS WHICH WOULD BECOME INJURIOUS BY RATIFICATION.**—Similarly, acts which would become injurious to others by ratification cannot be ratified. This principle is incorporated in Section 200 which says that an act cannot be ratified which by ratification "would have the effect of subjecting a third person to damages".<sup>426</sup> The illustrations to the section are that an unauthorised notice terminating a lease cannot be ratified.<sup>427</sup>

**ACTS DONE ON BEHALF OF GOVERNMENT.**—Such acts are ratifiable in the same way in which private acts can be. In one of the cases it was observed:<sup>428</sup> "If there had been any doubt about the original intention of the Government, it has clearly ratified and adopted the acts of its agents which according to the principle in *Buron v Denman*<sup>429</sup> is equivalent to previous authority." Thus acts of public servants in excess of their authority may be ratified by the Government.

Where public officers exceed their authority the State will be liable only to the extent it has expressly or impliedly ratified or approved the acts of such officers. This was laid down specifically as early as 1861 in *Collector of*

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of Article 299(1) of the Constitution. Their Lordships observed: "There can in truth be no notification without an intention to ratify and there can be no intention to ratify an illegal act without knowledge of illegality."

423. *M.P.M. Murugappa Chetti v Official Assignee of Madras*, (1936–37) 64 IA 343: AIR 1937 PC 296.

424. *Sunil v Maharashtra State Mining Corpn*, (2006) 1 Mah LJ 495. *Krishna Kumar v Electrical Engineer*, (1979) 4 SCC 289: AIR 1979 SC 1912, appointing authority is Board of directors.

425. *Brook v Hook*, (1871) LR 6 Exch 89. There may, however, be estoppel against forgery, i.e., the principal may by prior or subsequent conduct be deprived of his right to say that there was forgery of signature. *Greenwood v Martins Bank Ltd*, 1933 AC 51 (HL).

426. For example, ratification of a contract after its breach by the third party. *Kidderminster Corp v Hardwick*, (1873) LR 9 Exch 13.

427. Facts of this kind were involved in *Cassim Ahmed v Eusuf Haji Azam*, (1916) 23 Cal LJ 453, where notice to quit was given by one of joint lessors and the other joint lessor was not allowed to ratify it. *Sucharita Pradhan v U.P. Twiga Fibreglass Ltd*, AIR 2002 Del 1, an unauthorised notice served by only some of the owners for termination of tenancy was not allowed to be made regular by ratification by others.

428. *Secy of State in Council for India v Kamachee Boye*, 7 MIA 476, 539.

429. (1848) 2 Exch 167.

*Masulipatam v Cavalry Vencata Narrianpah*,<sup>430</sup> where the court said: “The acts of a Government officer bind the Government only when he is acting in the discharge of certain duty within the limits of the authority or if he exceeds that authority, when the Government in fact or in law directly or by implication ratifies the excess.”

#### 4. Knowledge of facts [S. 198]

**S. 198. Knowledge requisite for valid ratification.**—No valid ratification can be made by a person whose knowledge of the facts of the case is materially defective.

“To constitute a binding adoption of acts *a priori* unauthorised these conditions must exist: (1) the acts must have been done for and in the name of the supposed principal, and (2) there must be full knowledge of what those acts were, or such an unqualified adoption that the inference may properly be drawn that the principal intended to take upon himself the responsibility for such acts, whatever they were.”<sup>431</sup>

#### 5. Whole transaction [S. 199]

**S. 199. Effect of ratifying unauthorised act forming part of a transaction.**—A person ratifying any unauthorised act done on his behalf, ratifies the whole of the transaction of which such act formed a part.

A person cannot ratify a part of the transaction which is beneficial to him and repudiate the rest. So a ratification of a part of a transaction operates as a ratification of the whole of the transaction.<sup>432</sup>

#### 6. Within reasonable time

A ratification to be effective must come within reasonable time.<sup>433</sup> If a time is fixed for performance of the contract, ratification must come before that time otherwise it will be too late.<sup>434</sup> For example, a tender for supply of eggs was approved by a board, but not formally. The time for commencement

430. (1861) 8 MIA 529, 554 PC. *Buron v Denman*, (1848) 2 Exch 167 ratification of the acts of a British Naval Commander and thereby making them sovereign acts and therefore entitled to sovereign immunity. *Chatturbhuj Vithaldas Jasani v Moreshwar Parashram*, AIR 1954 SC 236: 1954 SCR 817, ratification of contracts made without complying with Art. 299 of the Constitution.

431. See *Fitzmaurice v Bayley*, (1856) 6 E&B 868 where the principal without knowledge of the fact whether the agent had exceeded authority, stood by his acts whatever they were. Followed in *Gauri Shankar Rao v Jwala Prasad*, AIR 1930 Oudh 312; *Tukaram Ramji Shendre v Madhorao Manaji Bhange*, AIR 1948 Nag 293, ratification of contract made on behalf of a minor without the knowledge of facts.

432. *Commercial Banking Co of Sydney Ltd v Mann*, 1961 AC 1: (1960) 3 WLR 726; *Bristow v Whitmore*, (1861) 9 HL Cas 391, principal bound to perform the contract in its entirety.

433. *Portuguese Consolidated Copper Mines Ltd, re*, (1890) LR 45 Ch D 16 (CA).

434. *Dibbins v Dibbins*, (1896) 2 Ch 348. It is observed in POLLOCK ON CONTRACTS that ratification must in every case be within a reasonable time and where a time is expressly delimited within which an act must be done, ratification after the time has expired will not serve.

of performance was September. Before this date the tender was withdrawn. The board ratified its approval of the tender on October 6. It was held this was too late as it was done after the date fixed for performance.<sup>435</sup> Similarly, a policy of fire insurance was not allowed to be ratified after the occurrence of the loss, because the owner himself could not have insured at that time.<sup>436</sup> The only exception is marine insurance, where a policy can be ratified even after the owner has come to know of the loss.<sup>437</sup> "The principal has no right to pause and wait for the fluctuation of the market, in order to ascertain whether the purchase is likely to be beneficial. He is bound if he decides to notify his determination in a reasonable time provided he has an opportunity of doing it."<sup>438</sup>

### Effects of ratification

Ratification has the following effects:

- (1) It establishes the relationship of principal and agent insofar as the act ratified is concerned between the person ratifying and the person doing the act.
- (2) Ratification establishes the relationship of contract between the principal and the third party.

### *Doctrine of relation back*

Ratification relates back to the date on which the agent first contracted. Section 196 declares that if an unauthorised act is ratified by the person on whose behalf it was done, "the same effects will follow as if they had been performed by his authority". Thus there is a contract between the principal and the third party, not from the date of ratification, but from the date when the agent first contracted. One of the effects of relation back is demonstrated by *Bolton Partners v Lambert*.<sup>439</sup>

The defendant made an offer to the managing director of a company who, having no authority to do so, accepted it. That gave the company an option to ratify the contract. But the company ratified only after the defendant had withdrawn his offer. The company sued the defendant for specific performance.

The company was held entitled to it. The company's ratification related back to the date on which the managing director first accepted the offer. Thus there was a contract between the company and the defendant from that date. The defendant's revocation of his offer was ineffective. LINDLEY LJ believed that it was not a question of withdrawal of offer, but withdrawal

435. *Metropolitan Asylums Board of Manager v Kingham & Sons*, (1890) 6 TLR 217.

436. *Grover & Grover Ltd v Mathews*, (1910) 2 KB 401.

437. *Williams v North China Insurance Co*, (1876) LR 1 CPD 757 (CA).

438. *Prince v Clarke*, (1823) 1 B&C 186: 107 ER 70. Followed, *Madura Municipality v K. Alagirisami Naidu*, AIR 1939 Mad 957, 960.

439. (1889) LR 41 Ch D 295 at pp. 308–09.

from contract. The managing director having accepted the offer, though without authority, there was contract, and it was not an offer, but a contract that was ratified. He said:

“I can find no authority in the books to warrant the contention that an offer made, and in fact accepted by a principal through an agent or otherwise, can be withdrawn. The true view on the contrary appears to be that the doctrine as to retrospective action of ratification is applicable.”

The decision has been criticised on the ground that it leaves the third party in a worse position than he would have been in if he had contracted with the principal, for then he could have revoked his offer until the principal had accepted it. But if he contracts through an unauthorised agent, he neither has a contract (until ratified) nor can he withdraw from it. The *American Restatement* suggests a different rule: “To constitute a ratification, the affirmation of a transaction must occur before the other party has manifested his withdrawal from it either to the purported principal or to the agent, and before the offer or agreement has been otherwise terminated or been discharged.” [S. 88, Restatement]

The decision has also been justified. The defendant had contracted to sell the property for certain price and was given the same terms. The ratification had not caused him any prejudice.<sup>440</sup>

But the general trend of opinion is against the decision. That is why it is not to be extended and was not followed in *Watson v Davies*.<sup>441</sup>

The defendant offered to sell his property to a charitable institution. The offer was accepted by a few members of the board “subject to approval by full members of the board”. The day on which the board was to meet, the defendant withdrew his offer. The board ratified it and brought an action for specific performance.

The ratification was held to be too late, and the revocation effective. MAUGHAM J said: “An acceptance by an agent... subject in express terms to ratification by his principal is legally a nullity until ratified, and is no more binding on the other party than an unaccepted offer which can, of course, be withdrawn before acceptance.”

The above decision may be said to constitute an exception to the principle in *Bolton Partners v Lambert*.<sup>442</sup> Another exception is where ratification would prejudice the interests acquired by others. For example, an unauthorised stoppage of goods in transit cannot be ratified after the transit has ended.<sup>443</sup>

The doctrine of relation back does not come into play where the contract made by the agent says that it is “subject to approval or ratification”. In such

440. See Stoljar, THE LAW OF AGENCY (1961) 190–91; Powell, THE LAW OF AGENCY (2nd Edn, 1961) 143.

441. (1931) 1 Ch 455, at pp. 468–69.

442. (1889) LR 41 Ch D 295.

443. *Bird v Brown*, (1850) 4 Exch 786; also note where third parties have in the meantime acquired property rights. *Whitehead v Taylor*, (1839) 10 Ad&El 210.

cases the other party would have the option to withdraw until ratification.<sup>444</sup> Retrospective ratification also becomes ruled out where the agent and third party have already by mutual consent cancelled the contract.<sup>445</sup>

## DETERMINATION OF AGENCY

The relationship of principal and agent may end in any of the ways mentioned in Section 201.<sup>446</sup>

**S. 201. Termination of agency.**—An agency is terminated by the principal revoking his authority; or by the agent renouncing the business of the agency; or by the business of the agency being completed; or by either the principal or agent dying or becoming of unsound mind; or by the principal being adjudicated an insolvent under the provisions of any Act for the time being in force for the relief of insolvent debtors.

The section provides for the following modes of termination:

1. Revocation<sup>447</sup>;
2. Renunciation by agents;
3. Completion of business;
4. Principal or agent's death;
5. Principal or agent becoming person of unsound mind;
6. Insolvency of principal;
7. Expiry of time.

These modes are considered below:

### By revocation [S. 203]

The principal may revoke his agent's authority and that puts an end to the agency.

**S. 203. When principal may revoke agent's authority.**—The principal may, save as is otherwise provided by the last preceding section, revoke the authority given to his agent at any time before the authority has been exercised so as to bind the principal.

444. *Warehousing and Forwarding Co of East Africa Ltd v Jafferali & Sons Ltd*, 1964 AC 1: (1963) 3 WLR 489 (PC).

445. *Walter v James*, (1871) LR 6 Exch 124.

446. See generally *Khila Dhish v Mool Chand*, (1969) 3 SCC 411, 413–14.

447. *U.P. Purva Sainik Kalyan Nigam Ltd v State of Uttaranchal*, AIR 2005 Utt 33: 2006 All LJ 1622 (Utt), provision for termination of security service by one month notice, notice effective. *Ashish Gupta v I.B.P. Co Ltd*, (2005) 125 DLT 298, termination of Government dealership would require show-cause notice, opportunity of being heard and reasoned decision, there can be interference under writ jurisdiction if natural justice is not observed. It is immaterial that the relationship is that of contractual nature. *Dirghayu Mahavir Diagnostic v State of Bihar*, 2015 SCC OnLine Pat 299: AIR 2015 Pat 110, an agency was created to run and operate regional diagnostic centres. The Authority had the right to terminate the agency either on establishing its own diagnostic centres or by following the procedure prescribed by law. There was no clarity about power of termination. The Authority had not established its own centres. Yet it terminated the agency that too by not giving any prior notice of show cause, arbitration was also not accepted because work was of emergency nature. Termination was held to be not proper.

Section 207 further provides that revocation may be expressed or implied in the conduct of the principal. An illustration appended to the section says:

A empowers B to let A's house. Afterwards A lets it himself. This is an implied revocation of B's authority.

Thus where the owner of a colliery appointed a sole selling agent for his coal for seven years, it was held that the owner could sell the colliery even before the expiry of this period and thus terminate the agency. He was not bound to keep his colliery.<sup>448</sup>

Lord PENZANCE said:<sup>449</sup> "Upon such an agreement as that... unless there is some special term in the contract that the principal shall continue to carry on business, it cannot for a moment be implied as a matter of obligation on his part that, whether the business is a profitable one or not, and whether for his own sake he wishes to carry it or not, he shall be bound to carry it on for the benefit of the agent and the commission that he may receive."

Similarly, an agent had provided a charter-party to the owner of a ship to run for a period of 18 months, the agent receiving commission on hire paid and earned. The owner sold the ship to the charterers within four months. The charter-party ended and so did the agency. The agent could not recover any damages, for the principal was not bound to keep the ship for the period of the charter-party.<sup>450</sup> An agent was appointed by a shirt manufacturer as a canvasser and traveller for five-year period to sell such goods as may be forwarded to him. The principal's factory was burned down by a chance fire while there were still three years for the agency to go. The principal never resumed business and ended the agency. He was held liable in damages as the agency seemed to have been created for a definite term.<sup>451</sup>

There was an agreement for allotment of distributorship of Gas. The allottee fulfilled the terms and conditions of the letter of allotment. The company failed to send its standard agreement to the allottee. It was held that the terms and conditions of the standard agreement could not legally

448. *Rhodes v Forwood*, (1876) LR 1 AC 256 (HL). The principle laid down in *Llanelli Rly & Dock Co v London and North Western Rly Co*, (1875) LR 7 HL 550 that there would be a presumption of perpetual duration in contracts specifying no time-limit, does not apply to agency. See Carnegie, 85 LQR 392 and Treitel, THE LAW OF CONTRACT (5th Edn, 1979) 570.

449. At p. 272, *Rhodes v Forwood*, (1876) LR 1 AC 256 (HL).

450. *L. French & Co Ltd v Leeston Shipping Co Ltd*, (1922) 1 AC 451.

451. *TCB Ltd v Gray*, 1987 Ch 458 (CA). See also *M.S. Desai & Co v Hindustan Petroleum Corp Ltd*, AIR 1987 Guj 19 where it was held that the termination of the dealership by an instrumentality of the State raises wider questions than mere breach of contract. *Madhabananda Nayak v State of Orissa*, AIR 1998 Ori 1, an agency under the public distribution system was held to have been wrongfully terminated when the alleged points of misconduct on the part of the agent were not proved. A similar matter, *Ashok Agarwal v State of Orissa*, (1996) 82 Cut LT 239. Declaration of Government policy that agencies for National Savings Certificates should not be given to relatives of employees was held to be not a good ground for termination of existing agencies, *Union of India v V.P. Parukutty*, (1997) 2 SCC 252: AIR 1997 SC 1903.

bind the allottee. The termination of the agency on the violation of such terms was not proper.<sup>452</sup>

An agency was deemed to have ended automatically by operation of law when a war broke out between the two countries to which the principal and agent respectively belonged.<sup>453</sup> This is so because “agency as a contract is determined by any event which terminates a contract”.<sup>454</sup>

### *Withdrawal of vakalatnama*

It has been held that a contract of *Vakalatnama* can be withdrawn by the client at any time. There is no such thing as an irrevocable *Vakalatnama*. After collecting the case papers, the advocate was trying to blackmail the client. The client lost faith in him. He terminated the *vakalatnama* and sought return of his file. It was immaterial that he was working without his professional fee. Corresponding to the right of the client, he was under professional duty to handover papers to the client.<sup>455</sup>

Revocation may be express or implied. Section 207 given below so provides:<sup>456</sup>

**S. 207. Revocation and renunciation may be expressed or implied.—** Revocation and renunciation may be expressed or may be implied in the conduct of the principal or agent respectively.

#### *Illustration*

A empowers B to let A's house. Afterwards A lets it himself. This is an implied revocation of B's authority.

An example of implied revocation was found in a case in which a father, after executing a power of attorney in favour of his son, fell into strained relations with him so that the son became an adversary and was, therefore, no more capable of acting as an agent.<sup>457</sup>

Execution of power of attorney does not denude the principal of his power to act independently of the attorney. The principal is not required to take attorney's consent for so acting. He was not bound to consult his attorney before signing a compromise petition. Such act on the part of the principal was held to have operated as an implied revocation of the power of attorney.<sup>458</sup>

452. *Niloufer Siddiqui v Indian Oil Corp Ltd*, AIR 2008 Pat 5.

453. *Stevenson (Hugh) & Sons Ltd v Ag Fur Cartonnagen Industrie*, (1917) 1 KB 842 (CA). Another justified termination, *G.L. Kilikar v State of Kerala*, (1971) 3 SCC 751: AIR 1971 SC 1196.

454. *English v Dedham Vale Properties Ltd*, (1978) 1 WLR 93.

455. *C. V. Sudhindra v Divine Light School for Blind*, AIR 2009 Kant 5.

456. *U.P. Purva Sainik Kalyan Nigam Ltd v State of Uttarakhand*, AIR 2005 Utt 33, notice terminating security service, as per the contract by giving one month notice. *Amina Begum v Mohd Ramzan*, AIR 2005 Raj 41, a written power of attorney could not be orally cancelled.

457. *Amrik Singh v Sohan Singh*, (1988-91) 93 PLR 541. *Kamlesh Aggarwal v Union of India*, AIR 2003 Del 88, agency of National Savings Organisation schemes, the agent was absent and remained unavailable due to detention in a criminal case. Termination of agency proper.

458. *Deb Ratan Biswas v Anand Moyi Devi*, AIR 2011 SC 1653.

An agreement entered into by virtue of the power of attorney before it was revoked retains its binding effect. If anything is done in relation to such a transaction, the agent can recover compensation for loss, if any caused to him.<sup>459</sup>

Revocation is subject to the following conditions:

Revocation operates prospectively [S. 204]

**S. 204. Revocation where authority has been partly exercised.**—The principal cannot revoke the authority given to his agent after the authority has been partly exercised, so far as regards such acts and obligations as arise from acts already done in the agency.

*Illustrations*

- (a) A authorises B to buy 1000 bales of cotton on account of A, and to pay for it out of A's money remaining in B's hands. B buys 1000 bales of cotton in his own name, so as to make himself personally liable for the price. A cannot revoke B's authority so far as regards payment for the cotton.
- (b) A authorises B to buy 1000 bales of cotton on account of A, and to pay for it out of A's money remaining in B's hands. B buys 1000 bales of cotton in A's name, and so as not to render himself personally liable for the price. A can revoke B's authority to pay for the cotton.

Even where the agent has partly exercised his authority, the principal may revoke it for the future. But it is irrevocable "as regards such acts and obligations as arise from acts already done in the agency". Where, for example, an agent has been appointed to buy something for the principal and he has purchased it by involving his personal liability, his authority cannot be revoked. Where a sale deed was executed by an agent under his power of attorney before his power was revoked by a newspaper notification, it was held that it could not upset the deed already executed and the registration of the deed could not have been refused because of the revocation.<sup>460</sup>

Where the agent carries on business even after his authority has been revoked by the principal, the latter cannot recover profits, if any, made by the agent in that business.<sup>461</sup> The agent cannot have any claim to remuneration for a period after the revocation.<sup>462</sup> He can, however, recover compensation for wrongful dismissal. He may even restrain his principal from appointing any other person in his place if there was a restrictive covenant to that effect.<sup>463</sup>

459. *Shamli Das v Swadesh Ghose*, (2010) 2 ICC 40 (Cal).

460. *Kishni Devi v State of Rajasthan*, AIR 1992 Raj 24. An auctioneer's authority is revocable before he knocks down but not afterwards, *Hare and O'More, re*, (1901) 1 Ch 93.

461. *Haribar Prasad Singh v Kesho Prasad Singh*, AIR 1925 Pat 68.

462. *Denmark Productions Ltd v Boscobel Productions Ltd*, (1969) 1 QB 699: (1968) 3 WLR 841; *Roberts v Elwells Engineers Ltd*, (1972) 3 WLR 1 (CA); remuneration earned up to the date of revocation remains recoverable. *Madhusudan Sen v Rakhal Chandra Das Basak*, AIR 1916 Cal 698, if the agent continues to work for the legal heirs, a new agency is created.

463. *Decro-Wall International SA v Practitioners in Mktg Ltd*, (1971) 1 WLR 361 (CA).

### Notice precedent to revocation [S. 206]

**S. 206. Notice of revocation or renunciation.**—Reasonable notice must be given of such revocation or renunciation; otherwise the damage thereby resulting to the principal or the agent, as the case may be, must be made good to the one by the other.

Where an agency has been created for a fixed period, a reasonable notice would be necessary to terminate it.<sup>464</sup> The length of notice will depend, among other things, upon the length for which the agency has continued. Thus the Privy Council held that “the notice of 3½ months given by the respondents was inadequate to determine an agency which had lasted for nearly 50 years, under which a very large business had been built up, and great expense incurred by the agents”.<sup>465</sup> Their Lordships would have accepted without question that two years was a reasonable notice.

### Liability to compensate [Ss. 205–206]

**S. 205. Compensation of revocation by principal, or renunciation by agent.**—Where there is an express or implied contract that the agency should be continued for any period of time, the principal must make compensation to the agent, or the agent to the principal, as the case may be, for any previous revocation or renunciation of the agency without sufficient cause.

**S. 206. Notice of revocation or renunciation.**—Reasonable notice must be given of such revocation or renunciation; otherwise the damage thereby resulting to the principal or the agent, as the case may be, must be made good to the one by the other.

If the agency is determined without reasonable notice, “the damages thereby resulting to the agent must be made good” by the principal. Where an agency has been created for a fixed period, compensation would have to be paid for its premature termination, if the termination is without sufficient cause. Reasonable notice for premature determination of an agency was not given. The agent was earning Rs 4000 per month. The court was of the view that at least three months’ notice should have been given. A compensation of Rs 12,000 was accordingly allowed.<sup>466</sup> The liability to pay compensation does not arise where the agency is not for a fixed period. The Madras High Court did not allow any compensation to the agent for the unilateral termination of an agency, which though created without any stipulation for its

464. A termination without notice is ineffective. *Om Prakash Pariwal v Union of India*, AIR 1988 Cal 143, FCI terminating the agency of a storing agent without notice. The requirement of notice is mandatory. *Popular Shoe Mart v K. Srinivasa Rao*, (1989) 2 An LT 541: AIR 1990 NOC 87 (AP).

465. *Sohrabji v Oriental Govt Security Assurance Co*, (1944–45) 72 IA 315: AIR 1946 PC 9. See *Shipping Corp of India Ltd v Machado Bros*, 1996 AIHC 3869, termination of agency held bad because on the reorganisation of the firm, the agency was continued, subsequent termination on that ground not proper; notice was necessary before termination, which was not given.

466. *J.R. Sayani v Bright Bros (P) Ltd*, AIR 1980 Mad 162.

duration, had lasted from 1952 to 1964.<sup>467</sup> Thus no compensation is payable in the following cases: (1) Where the agency has not been created for any definite period; (2) Where, though created for a specified length of time, reasonable notice for its termination has been given or the termination is otherwise based upon a sufficient cause.

#### *Power of attorney executed on consideration*

A power of attorney was executed in favour of the agent (defendant) after receiving consideration from him. Its execution was duly made by a number of conscious signatures on several papers. It was subsequently revoked without giving the agent any compensation or repayment of the loan amount. Such cancellation was held to be *non-est* in the eyes of law.<sup>468</sup>

#### **Agency coupled with interest [S. 202]**

In certain circumstances, however, an agency becomes irrevocable. This happens when the agent is personally interested in the subject-matter of agency. Section 202 provides:

**S. 202. Termination of agency, where agent has an interest in subject-matter.**—Where the agent has himself an interest in the property which forms the subject-matter of the agency, the agency cannot, in the absence of an express contract, be terminated to the prejudice of such interest.

#### *Illustrations*

- (a) A gives authority to B to sell A's land, and to pay himself, out of the proceeds, the debts due to him from A. A cannot revoke this authority, nor can it be terminated by his insanity or death.
- (b) A consigns 1000 bales of cotton to B, who has made advances to him on such cotton, and desires B to sell the cotton, and to repay himself, out of the price, the amount of his own advances. A cannot revoke this authority, nor is it terminated by his insanity or death.

In the well-known case of *Smart v Sanders*<sup>469</sup> WILDE CJ stated the rule thus:

“Where an agreement is entered into on a sufficient consideration, whereby an authority is given for the purpose of securing some benefit to the donee of the authority, such an authority is irrevocable. This is what is usually meant by an authority coupled with an interest, and which is commonly said to be irrevocable.”<sup>470</sup> The simplest case of such agency occurs when the principal owes something to the agent and authorises him to sell the

467. *Bright Bros (P) Ltd v J.K. Sayani*, AIR 1976 Mad 55.

468. *Subhadra v M. Narasimha Murthy*, AIR 2012 Kant 19.

469. (1848) 5 CB 895.

470. *Ibid.* At p. 917. Citing from *Clerk v Laurie, Public Officer*, (1857) 2 H&N 199: 157 ER 83. The agency is irrevocable during the subsistence of such security or interest. *Reginald Charles Frith v Josiah Alexander Frith*, 1906 AC 254.

principal's goods and pay himself out of the sale proceeds.<sup>471</sup> But an authority to pay debts which the principal owes to some third person does not make the agency irrevocable.<sup>472</sup> In a case before the Madras High Court, a person was entitled to be maintained out of the income of a property, known as *tarwad* property. He was subsequently given the authority to collect rents of the property. The authority was held to be not revocable.<sup>473</sup> In another case before the same High Court, in consideration of advances made by the plaintiff, all the properties of a *devason* were given over to him on lease for 18 years with authority to receive rents. That was held to be an authority coupled with interest and, therefore, irrevocable.<sup>474</sup> Thus the essence of the matter is that “[t]he agent has, as it were, bought his authority in order to ensure the payment of a debt due from the principal”.<sup>475</sup> Where an agent was authorised to do all acts in connection with the performance of a contract and to receive running payments, it was held to be an equitable assignment of the contract for a consideration making the arrangement irreversible.<sup>476</sup> The amounts payable to the agent were not permitted to be attached for the debts of the principal, but the rest of the amounts, such as security deposits and retention money, which were not assigned, remained attachable.

An agency of this kind is not even terminated by the principal's death.<sup>477</sup> A principal owed a sum of money to his agent and gave him an accepted bill of exchange with an authority to fill in the drawer's name. The principal died before the agent could complete the bill. His authority to fill in the drawer's name was held to be not terminated.<sup>478</sup> But the matter is not free from controversy. For, in *Watson v R.*,<sup>479</sup> Lord ELLENBOROUGH said: “How can a valid act be done in the name of a dead man?” Commenting upon the decision, Powell says: “The decision overlooks the fact that an authority coupled with an interest is really a transfer of property.”<sup>480</sup> An authority coupled with interest is also not determined by the principal's insolvency.<sup>481</sup>

471. *Pestonji v Matchett*, (1870) 7 BHC App Cas 10; *Subba Rao v Varadaiah*, AIR 1943 Mad 482, buyer authorised to pay off mortgage out of sale proceeds in his hands. *Jogabhai v Rustomji Nasarvanji*, (1885) 9 Bom 311, an assignment of a debt is not revocable.

472. *Clerk v Laurie, Public Officer*, (1857) 2 H&C 199: 157 ER 83.

473. *Chatbu Kuttu Nair v Kundan Appa*, AIR 1932 Mad 70.

474. *Ibid.*

475. Powell, THE LAW OF AGENCY (2nd Edn, 1961) 392.

476. *Joseph George v Cochin Sanitary Wares*, (1991) 2 KLT 447.

477. *Shantadevi v Savjibhai H. Patel*, (1999) 4 GCD 3190, in the absence of express contract for termination, even death of the principal would not result in termination of such an agency. The agency in this case was for the development and construction activity on land for weaker sections of society.

478. *Carter v White*, (1883) LR 25 Ch D 666 (CA).

479. (1815) 4 Camp 272.

480. THE LAW OF AGENCY (2nd Edn, 1961) 388, f.n. 5.

481. *Alley v Hotsan*, (1815) 4 Camp 325. The Supreme Court has held in *Loonkaran Sethiya v Ivon E. John*, (1977) 1 SCC 379: AIR 1977 SC 336 that where an agency is created for valuable consideration and the agent is given authority to secure his interest, the authority cannot be revoked.

*Interest existing at the time of creation of agency*

But the doctrine of agency coupled with interest is not without qualification. In the first place, the interest of the agent must exist at the time of the creation of the agency.<sup>482</sup> “[T]his doctrine applies only to cases where the authority is given for the purpose of being a security, or ... as a part of the security: not to cases where the authority is given independently, and the interest of the donee of the authority arises afterwards, and incidentally only.”<sup>483</sup> This statement of the law occurs in *Smart v Sanders*.<sup>484</sup> In this case goods were consigned to a factor for sale and he subsequently made advances to his principal on the credit of the goods. It was held that the subsequent advance could not convert the agency into one coupled with interest. “The making of such an advance may be a good consideration for an agreement that the authority to sell shall be no longer revocable, but such an effect will not arise independently of agreement.” An agency created by an irrevocable power of attorney for enabling the agent to construct houses on the land of the principal for sale was held to be an agency coupled with interest. The court said that the interest of the agent need not be a pre-existing interest. Such interest may be created simultaneously with the agreement. The agent had to seek approval of the building plan. His agency was not allowed to be revoked.<sup>485</sup> An agency created through power of attorney authorising the agent to apply for renewal of permits of the vehicles and, if necessary, to replace the vehicles by transferring them and spend money for this purpose, the agency was held to be one coupled with interest and, therefore, not revocable to the prejudice of the interest. The acts done by the agent within the scope of his authority were held to be binding on the principal.<sup>486</sup> An irrevocable power of attorney was created for working a mine. The intention was to transfer the leasehold interest in the mine in favour of the power

482. *Kondayya Chetti v Narasimhalu Chetti*, ILR (1897) 20 Mad 97 (1893), advance given for the purpose of getting agency and to recoup from proceeds, irrevocable.

483. WILDE CJ in *Smart v Sanders*, (1848) 5 CB 895. See *M. John Kotaiah v A. Divakar*, AIR 1985 AP 30, it was a power of attorney to manage an estate, the agent was to receive commission at the rate of 5 per cent of the market value of the property. Held, this was not an agency coupled with interest.

484. *Ibid.*

485. *Shantidevi Pratap Singh Rao Gaekwad v Savjibhai S. Patel*, (1998) 2 Guj LR 1521, investment by the agent on the basis of the promise creates an interest.

486. *Goutham Surana & Sons v K. Kesavakrishnan*, 1995 SCC OnLine Mad 5: (1998) 3 LW 809. The court considered *Board of Revenue v Annamalai & Co (P) Ltd*, AIR 1968 Mad 50, debtor authorising the creditor-banker to sell his properties to pay himself, held, agency coupled with interest. *Bhagwanbhai Karamanbhai Bharvad v Arogyanagar Coop Housing Society Ltd*, AIR 2003 Guj 294: (2004) 1 Guj LR 506, land owners executed an irrevocable power of attorney for sale of land, death of one of them did not make it necessary that he should take consent of his legal heirs, *Bhaskar Aditya v Minati Majumdar*, AIR 2003 Cal 178: (2003) 1 ICC 573 (Cal), owner entered into agreement for development with a developer, the work was that of the owner, through the developer—an agent, the developer acquired interest in the property which was the subject-matter of development. *Jeet Kumari v Girdhari Lal*, (2003) 4 ICC 501, rights given for sale of a house property for consideration on power of attorney, held, agency coupled with interest.

of attorney holder. It was held that an interest was created in favour of the holder. The agency could not be terminated to the prejudice of the holder.<sup>487</sup>

### *Protection of existing interest, primary purpose of agency*

Secondly, "the test to be applied for finding out whether a power of attorney given to an agent is irrevocable or not is to see whether the primary object in giving the power was for the purpose of protecting or securing any interest of the agent. If the primary object was to recover on behalf of the principal the fruits of his decree and, in doing so, the agent's rights were also incidentally protected, then the power is revocable".<sup>488</sup> Similarly, the prospect of earning a commission is not an interest for this purpose.<sup>489</sup> Again, a "mere arrangement that the plaintiff's salary should be paid out of the rents could not be regarded as giving to the agent an interest in the property, the subject-matter of the agency, within the meaning of Section 202".<sup>490</sup> A mere mention that the agency is irrevocable does not make it so.<sup>491</sup> The concept of irrevocable power of attorney is not known to jurisprudence unless the power is coupled with interest. Accordingly, an agency to give effect to an agreement for development of property does not create an interest in the property.<sup>492</sup> A power of attorney was executed to enable the attorney to look after the construction work. He was not authorized to take personal loans for the purpose. The property was not offered as a security for pecuniary liabilities incurred by the agent. He was not allowed to say that the agency had become irrevocable by reason of his pecuniary involvement which he could not even prove.<sup>493</sup>

### **Renunciation by agent [S. 206]**

An agent may renounce the business of agency in the same manner in which the principal has the right of revocation. In the first place, if the agency is for a fixed period, the agent would have to compensate the principal

487. *Birat Chandra Dugara v Taurian Exim (P) Ltd*, AIR 2005 Ori 147.

488. *Mocker J in Palani Vannan v Krishnaswami Konar*, AIR 1946 Mad 9; (1946) ILR Mad 191. In *Dalchand v Hazarimal*, AIR 1932 Nag 34, security given as against a pre-existing debt, S. 202 does not apply.

489. *Lakhmi Chand v Chotooram*, ILR (1900) 24 Bom 403; even where the commission agency was for a period of five years it did not become one coupled with interest. *Doward Dickson & Co v Williams & Co*, (1890) 6 TLR 316. The earning of commission by a booking and shipping agent was held to be not an interest for the purposes of the section, *Jaytee Exports v Natvar Parekh Industries Ltd*, AIR 2001 Cal 150 at p. 153.

490. *Vishnucharya v Ramchandra*, ILR (1881) 5 Bom 253. The same is true of an auctioneer who is authorised to deduct his commission from sale proceeds, *Taplin v Florence*, (1851) 10 CB 744 and of an agent for execution of a decree, his remuneration to be paid from the proceeds of the decree, *Palani Vannan v Krishnaswami Konar*, AIR 1946 Mad 9. *Ishwarappa v Arunkumar*, 2004 AIR Kant HCR 2273: AIR 2004 Kant 417, power of attorney executed for looking after construction work, no authorisation for incurring loan liability, property not offered as a security for payment, agency not coupled with interest.

491. *Barses J.A. D'Souza v Municipal Corp of Greater Bombay*, (2003) 6 Bom CR 846.

492. *Vipin Bhimani v Sunanda Das*, (2006) 2 CHN 396: AIR 2006 Cal 209 (DB).

493. *Ishwarappa v Arunkumar*, 2004 AIR Kant HCR 2273: AIR 2004 Kant 417.

for any premature renunciation without sufficient cause. [S. 205] Secondly, a reasonable notice of renunciation is necessary. Length of notice is to be determined by the same principles which apply to revocation by the principal. If the agent renounces without proper notice, he shall have to make good any damage thereby resulting to the principal. [S. 206]

### Completion of business [S. 201]

An agency is automatically and by operation of law determined when its business is completed. Thus, for example, the authority of an agent appointed to sell goods ceases to be exercisable when the sale is completed. He cannot afterwards alter the terms of the sale.<sup>494</sup> But the Allahabad and Calcutta High Courts have held that agency is not terminated on the completion of the sale but continues until payment of the sale proceeds to the principal.<sup>495</sup>

### Death or insanity [S. 201]

An agency is determined automatically on the death<sup>496</sup> or insanity<sup>497</sup> of the principal or the agent. Winding up of a company or dissolution of a partnership has the same effect.<sup>498</sup> Acts done by the agent before death would remain binding. Where an attorney appointed a counsel for his principal, it was held that such an appointment would survive the death of attorney.<sup>499</sup> The court cited the following passage from *Girshan Industrial Co Ltd v Interchem Corp*.<sup>500</sup> "An attorney is merely an agent of the principal and what he does, he does for the principal. So long as the principal is alive, any act done by the attorney or his counsel is valid and continues to be valid irrespective of the fact whether the attorney is alive or dead. But the counsel for the attorney cannot act if the principal is dead." A reading of Section 201 makes it clear that on the death of an agent his agency comes to an end but it does not obliterate acts done by the agent on behalf of the principal during the tenure of his agency.

Where a principal authorised his power of attorney to present a document disposing of his property for registration, but the principal died before the agent could do so, a subsequent registration was held to be invalid. In this case the Registrar also knew that the principal was dead.<sup>501</sup>

494. *Venkatachalam v Narayanan*, ILR (1914) 39 Mad 376. In the matter of an agency for collection of bills and remitting the amount, agency terminates as soon as the drafts are despatched to the principal, *Alliance Bank of Simla v Amritsar Bank*, AIR 1915 Lah 214.

495. *Babu Ram v Ram Dayal*, ILR (1890) 12 All 541; *W.R. Fink v Buldeo Dass*, ILR (1899) 26 Cal 715.

496. *Campañari v Woodburn*, (1854) 15 CB 400; *Pool v Pool*, (1889) 58 LJP 67.

497. *Yonge v Toynebee*, (1910) 1 KB 215 (CA).

498. *Salton v New Beeston Cycle Co*, (1900) 1 Ch 43; *Harold Fielding Ltd v Mansi*, (1974) 1 All ER 1035.

499. *Nasib Kaur v Chanan Singh*, (1999) 1 PLR 216.

500. 1970 Curr LJ 387.

501. *Mujibunnissa v Abdul Rahim*, (1900–01) 28 IA 15; (1901–03) 23 All 233. *A.B. Ramulu v B. Yadigir*, (1993) 2 An LT 425, proceedings could not be continued by the power of attorney after the death of the principal without taking power from legal representatives.

### Principal's insolvency [S. 201]

An agency ends on the principal being adjudicated insolvent.<sup>502</sup>

### On expiry of time [S. 201]

"Where an agent has been appointed for a fixed term, the expiration of the term puts an end to the agency, whether the purpose of the agency has been accomplished or not."<sup>503</sup> An agency comes to an automatic end on the expiry of its term. Where the agency was to run a petrol pump for a specified period, it was held that the agent was bound to vacate the premises on expiry of the period. There was no renewal clause, nor in fact there was any renewal.<sup>504</sup>

### Effects of termination [S. 208]

**S. 208. When termination of agent's authority takes effect as to agent, and as to third persons.**—The termination of the authority of an agent does not, so far as regards the agent, take effect before it becomes known to him, or, so far as regards third persons, before it becomes known to them.

#### *Illustrations*

- (a) A directs B to sell goods for him, and agrees to give B five per cent commission on the price fetched by the goods. A afterwards, by letter, revokes B's authority. B, after the letter is sent, but before he receives it, sells the goods for 100 rupees. The sale is binding on A, and B is entitled to five rupees as his commission.
- (b) A, at Madras, by letter, directs B to sell for him some cotton lying in a warehouse in Bombay, and afterwards, by letter, revokes his authority to sell, and directs B to send the cotton to Madras. B, after receiving the second letter, enters into a contract with C, who knows of the first letter, but not of the second, for the sale to him of the cotton. C pays B the money, with which B absconds. C's payment is good as against A.
- (c) A directs B, his agent, to pay certain money to C. A dies, and D takes out probate to his will. B, after A's death, but before hearing of it, pays the money to C. The payment is good as against D, the executor.

As between the principal and the agent, the authority of the agent ends when he comes to know of the termination. Where, for example, the authority of an agent appointed to sell goods is revoked, but he sells the goods before receiving the letter of revocation, the sale is good. Illustration (a) is relevant to this point.

But as regards third persons, the agency does not terminate until they come to know of the fact of termination. Where, for example, an agent sells the principal's goods even after receiving notice revoking his authority, the sale is binding on the principal and the buyer gets a good title provided

502. *Ernest Charles Elliott v William Turquand*, (1881) LR 7 AC 79; insolvency of an agent would also have the same effect if it makes him unfit to perform his duties, *McCall v Australian Meat Co Ltd*; (1870) 19 WR 188.

503. *Per Mookerjee J, Lalljee Mahommad v Dadabhai Jivanji Guzadar*, AIR 1916 Cal 964.

504. *P. Sukhadev v Commr of Endowments*, (1998) 1 BC 403 (AP).

he did not know of the fact of termination. Illustration (b) is relevant to this point.<sup>505</sup> Where the power of attorney-holder executed the sale deed in favour of the third party who had already paid the price to the principal under an agreement with him, the principal became bound though he had terminated the power of attorney but the third party was not aware of the fact of termination at the crucial moment.<sup>506</sup> The court cited the following passage from the decision of the Madras High Court in *Khatoon Bivi Ammal v Arulappa Nadar*:<sup>507</sup> “Policy of law apparently in the interest of trade and commerce is that the agent’s action should bind the principal even though the principal might have cancelled the agent’s authority, unless the third party with whom the agent enters into the contract knows of the termination of the agency.” The court also placed reliance upon the judgment in *Trueman v Loder*.<sup>508</sup> “Here A traded as B’s agent. With the authority of B, all parties with whom A made contracts in that business, were held to have a right to hold B liable to them until B gives notice to the world that A’s authority is revoked and it makes no difference if in a particular case the agent intended to keep the contract on his own account. The court repelled the contention that it was very unreasonable to expect that the principal should inform the whole world that he has cancelled the power of attorney given to his agent and that he cannot be expected to approach everybody with whom the agent was likely to enter into a contract and inform him of the cancellation.”

Even when the agency is terminated by the death of the principal, the termination is effective only when it comes to the knowledge of the agent. Illustration (c) is relevant to this point. A wife was authorised by her husband to keep buying goods from a dealer. The husband became a person of unsound mind. The wife kept up her purchases from the seller, the latter not knowing of the husband’s incapacity. The husband was held liable to pay for the goods.<sup>509</sup>

#### *Termination of sub-agency*

When the authority of an agent terminates, it entails the termination of the authority of all sub-agents appointed by him. Section 210 is as follows:

**S. 210. Termination of sub-agent’s authority.**—The termination of the authority of an agent causes the termination (subject to the rules herein contained regarding the termination of an agent’s authority) of the authority of all sub-agents appointed by him.

505. Where in the case of a partnership firm the authority of partners could be terminated by a public notice which was not done and the bank not knowing took acknowledgment from a partner, the same was effective. *Assiamma v State Bank of Mysore*, (1990) 1 KLT 18.

506. *Kashi Ram v Raj Kumar*, AIR 2000 Raj 405.

507. AIR 1970 Mad 76.

508. (1840) 11 Ad & El 589.

509. *Drew v Nunn*, (1879) LR 4 QBD 661. Registration of a transfer deed effected by a person whose authority had ended, held void. *Sekar Mudaliar v Shajathi Bi*, AIR 1987 Mad 239.

The allotment of works to a contractor is not the creation of an agency or sub-agency for the purposes of this section.<sup>510</sup>

#### Agent's duty on termination [S. 209]

Section 209 gives the duty of the agent on termination.

**S. 209. Agent's duty on termination of agency by principal's death or insanity.**—When an agency is terminated by the principal dying or becoming of unsound mind, the agent is bound to take, on behalf of the representatives of his late principal, all reasonable steps for the protection and preservation of the interests entrusted to him.

Section 210 provides that the termination of an agent's authority amounts to termination of all sub-agents appointed by him. Section 209 charges the agent with duty to protect his principal's interest where the principal has died or become a person of unsound mind.

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510. *Dalmia Cement (Bharat) Ltd v T.V. Oomen*, (1987) 1 KLT 534.

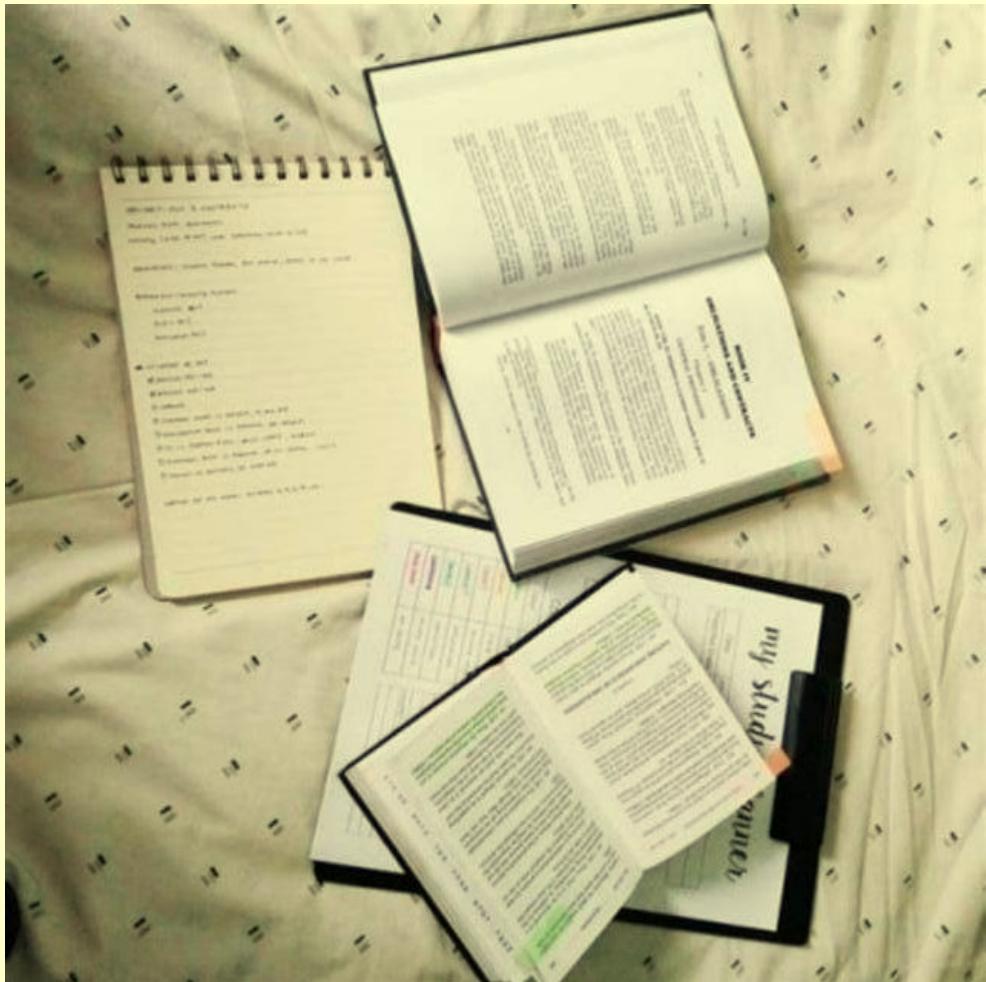
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**The following cases from this chapter are available through EBC Explorer™:**

- *Abdulla Ahmed v Animendra Kissen Mitter*, AIR 1950 SC 15:  
1950 SCR 30
- *Mohanlal Jain v Sawai Man Singhji*, AIR 1962 SC 73:  
(1962) 1 SCR 702
- *Pannalal Jankidas v Mohanlal*, AIR 1951 SC 144: 1950 SCR 979:  
(1951) 21 Comp Cas 1
- *Prager v Blastpiel Stamp & Heacock Ltd*, (1924) 1 KB 566

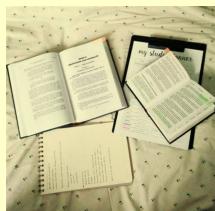




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**PART III**

**LAW OF SPECIFIC RELIEF**  
**(Ss. 1–142)**

16

# Specific Relief Act, 1963

THE SPECIFIC RELIEF ACT, 1963<sup>1</sup>

[Act 47 of 1963]

[13 December 1963]

*An Act to define and amend the law relating  
to certain kinds of Specific Relief*

**Prefatory Note.**—The following extract from the Statement of Objects and Reasons is given below:

"This Bill seeks to implement the recommendations of the Law Commission contained in its Ninth Report on the Specific Relief Act, 1877, except in regard to Section 42 which is being retained as it now stands. An earlier Bill on the subject introduced in the Lok Sabha on the 23rd December, 1960, lapsed due to dissolution. The notes on clauses, extracted from the Report of the Law Commission, explain the changes made in the existing Act." (*Vide Gaz. of India, Extra., Part II, S. 2, dated June 15, 1962.*)

Be it enacted by Parliament in the Fourteenth Year of the Republic of India as follows:—

## PART I

### PRELIMINARY

**S. 1. Short title, extent and commencement.**—(1) This Act may be called the Specific Relief Act, 1963.

(2) It extends to the whole of India except the State of Jammu and Kashmir.

(3) It shall come into force on such date<sup>2</sup> as the Central Government may, by notification in the Official Gazette, appoint.

### Act not exhaustive

Though Specific Relief Act widens the sphere of the civil court, its preamble shows that the Act is not exhaustive of all kinds of specific reliefs. The Act is not restricted to specific performance of contracts as the statute

1. The Act received the assent of the President on December 13, 1963 and published in the *Gaz. of India, Extra., Part II, S. 1, dated December 16, 1963.*

2. 1st March, 1964, *vide* Notification No S.O. 189, dated 13th January, 1964, *Gaz. of India, Part II, S. 3(ii)*, p. 214.

governs powers of the court in granting specific reliefs in a variety of fields. Even so, the Act does not cover all specific reliefs conceivable.<sup>3</sup>

**S. 2. Definitions.**—In this Act, unless the context otherwise requires,—

- (a) “obligation” includes every duty enforceable by law;
- (b) “settlement” means an instrument [other than a will or codicil as defined by the Indian Succession Act, 1925 (39 of 1925)] whereby the destination or devolution of successive interests in movable or immovable property is disposed of or is agreed to be disposed of;
- (c) “trust” has the same meaning as Section 3 of the Indian Trusts Act, 1882 (2 of 1882), and includes an obligation in the nature of a trust within the meaning of Chapter IX of that Act;
- (d) “trustee” includes every person holding property in trust;
- (e) all other words and expressions used herein but not defined, and defined in the Indian Contract Act, 1872 (9 of 1872), have the meanings respectively assigned to them in that Act.

**S. 3. Savings.**—Except as otherwise provided herein, nothing in this Act shall be deemed—

- (a) to deprive any person of any right to relief, other than specific performance, which he may have under any contract; or
- (b) to affect the operation of the Indian Registration Act, 1908 (16 of 1908), on documents.

**S. 4. Specific relief to be granted only for enforcing individual civil rights and not for enforcing penal laws.**—Specific relief can be granted only for the purpose of enforcing individual civil rights and not for the mere purpose of enforcing a penal law.

## SPECIFIC RELIEF

### Introduction to the outline of the Act

A large number of remedial aspects of law have been taken care of by the Specific Relief Act of 1963 (47 of 1963). This Act is a replacement of the earlier Act of 1877. A mere declaration of rights and duties is not sufficient to give protection to life and property. Enumeration of rights and duties must be supplemented by legal devices which can help the individual to enforce his rights. Every person who is injured in the social process must have a social redress. Only then it will be possible to say that human societies have been so organised as to assure that wherever there is a wrong there must be a remedy. This is the mission of the Specific Relief Act. Generally, remedies are also provided by the branch of substantive law which defines rights and duties for its own purposes. The law of contract provides the remedy of damages for breach of contract. The law of torts similarly provides for recovery of damages in several cases of tortious wrongs. Substantive laws,

3. *Ashok Kumar Srivastav v National Insurance Co Ltd*, (1998) 4 SCC 361: AIR 1998 SC 2046.

however, can never afford to be exhaustive in terms of their remedies and reliefs. Scope remains for an Act whose only purpose is to provide a network of reliefs in certain specific terms. Such an Act does not confer any rights in itself. It only provides a specific relief so as to remedy the violation of a legal right. The network of reliefs allowed by the Act falls under the following outlines:

### *1. Recovery of possession of property*

Though the Specific Relief Act is concerned only with the enforcement of civil rights and not penal laws, even civil law has to take care of certain rights, the violation of which is capable of creating serious violent clashes, and these are rights to possession of property. The very first chapter provides relief to those who have been dispossessed of their property.

### *2. Specific performance of contracts*

One of the most important aspects of civil rights is the fulfilment of expectations created by a contract voluntarily made by the parties. Contracts are at the base of almost all economic relations. All employments and professions are contract bound. All property, whether business assets or personal, remain locked up under contracts. For example, money in banks and in other forms of investment is contractually bound. Thus contracts constitute the modern wealth. They are sacred *per se*. Moreover, a particular contract is not just an isolated transaction. It is often a link in a chain of several contracts. A failure at one place can cause a serious dislocation of economic and social life. Contracts must be enforced. But the only way the law of contract can enforce a contract is by awarding compensation to the injured person. In many cases, however, compensation fails to serve the economic purpose of the contract. A hospital is, for example, interested in the fulfilment of its requirements and not in receiving compensation from a failed supplier. There was thus the need for a remedy which would compel a defaulting contractor to actually perform his contract. This important function is undertaken by the second chapter of the Specific Relief Act under the heading: SPECIFIC PERFORMANCE OF CONTRACTS.

### *3. Rectification and cancellation of instruments and rescission of contracts*

Many transactions are required by law to be in writing. Many more transactions are put into writing because of expediency. A written transaction is an instrument. An instrument is the result of negotiations. Occasionally it happens that the instrument that emerges fails to express the intention of the parties. Its rectification may become necessary. Accordingly, Chapter III of the Specific Relief Act helps parties who want to have their mistakenly executed documents rectified.

Closely allied with documents mistakenly executed is the category of documents which are afterwards discovered to be void or which become void. They ought to be cancelled. Chapter V provides relief from such kinds of documents.

Then there is a category of contracts which, for one reason or another, such as, for example, lack of free consent, are voidable at the option of the party whose consent was not free. He has a right to have the contract rescinded. Relief by way of rescission is provided by Chapter IV of the Act.

#### *4. Preventive relief*

There are cases in which the nature of the contract does not admit of specific performance, nor damages are likely to serve any purpose. In such cases the court may have to restrain the party threatening breach, to the extent to which it is possible to do so. For example, a person contracts to sing at a particular place and also undertakes not to sing elsewhere during the same period. He threatens breach. The court cannot force him to sing. The positive side of the bargain is not specifically enforceable. But the negative undertaking "not to sing elsewhere" can be enforced by restraining him from giving his performances elsewhere. When he is so prevented from resorting to other openings, it may exert some pressure upon his mind and he may be persuaded to go ahead with the performance of his contract. This type of remedy is known as preventive relief. It is granted by issuing an order, known as "injunction", upon the party concerned directing him not to do a particular act or asking him to perform a particular duty, known as a mandatory injunction. Such relief is granted under the provisions of Part III of the Act running from Chapter VII to the end.<sup>4</sup>

#### *5. Declaratory relief*

There is one more matter of which the Specific Relief Act takes care and that is "declaratory relief". Occasionally it may happen that a person is entitled to some status or character or has a right in some property, but there are persons who are denying him the enjoyment of his right. He is allowed by Chapter VI of the Specific Relief Act to proceed against any person who is denying or interested in denying him his right and the court may issue a general declaration as to his entitlement to such right (declaratory decrees).

### **RECOVERY OF POSSESSION OF IMMOVABLE PROPERTY**

Section 5 of the Specific Relief Act, 1963 provides that a person entitled to the possession of specific immovable property may recover it in the manner prescribed by the Code of Civil Procedure, 1908.<sup>5</sup>

4. *Adhunik Steels Ltd v Orissa Manganese Minerals (P) Ltd*, (2007) 7 SCC 125: AIR 2007 SC 2563, the Supreme Court explained the various types of relief under the Act and their nature and scope.

5. *Sanjay Kumar Pandey v Gulbahar Sheikh*, (2004) 4 SCC 664, the proceedings under the section are of summary nature and limited in their scope to finding out the fact of possession

**S. 5. Recovery of specific immovable property.**—A person entitled to the possession of specific immovable property may recover it in the manner provided by the Code of Civil Procedure, 1908 (5 of 1908).

This section deals with action for recovery of possession of specific immovable property based on title. The essence of the section is that whoever proves a “better title” is a person “entitled to possession”. The title may be on the basis of ownership or possession. Thus, suppose *A* enters into peaceful possession of land claiming it as his own although he might have no title to it, still he can sue another who has forcibly ousted him from possession and who has no better title to it, because *A*, although he has no legal title, has at least a possessory title. The purpose behind Section 6 is to restrain a person from using force and to dispossess a person without his consent otherwise than in due course of law.<sup>6</sup>

A suit under Section 5 is an ordinary suit under the general law and the plaintiff has to prove that he has a better title. Further, specific performance can be decreed only against the executant of the contract having the right to dispose of the property in question.<sup>7</sup>

It is a principle of law that a person who has been in long continuous possession of an immovable property, can protect the same by seeking an injunction against any person in the world other than the true owner. It is also well settled that even the owner of the property can get back his possession only by resorting to the due process of law.<sup>8</sup>

A decision as to a specified part of the property in question may not constitute *res judicata* in respect of any subsequent proceedings about the entire property.<sup>9</sup>

**S. 6. Suit by person dispossessed of immovable property.**—(1) If any person is dispossessed without his consent of immovable property otherwise

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within period of six months preceding to the institution of the suit. The question of title is ignored in these proceedings. If the summary proceeding is unsuccessful, the person in question should file a regular suit for title to be decided on merits. The remedy of revision is available but only by way of exception and not as a general rule. A case has to be made out under S. 115 CPC. *Bajranglal Shivchandrai Ruia v Shashikant N. Ruia*, (2004) 5 SCC 272, for success of his suit the plaintiff would have to establish his title.

6. *Puthukkattil Parangodan v Puthukkattil Parameswaran*, AIR 2002 Ker 221, the subject-matter of the tenancy was completely destroyed and the lease automatically terminated. But even so the landlord could claim and recover possession only through the court process. *ITC Hotels Ltd v Adarsh Coop Housing Society Ltd*, (2013) 10 SCC 169: (2012) 94 AIR 682, remedy under the section is only for recovery of possession of the person who has been dispossessed. A regular suit has to be filed for establishing title or ownership.

7. *Annapoorani Ammal v G. Thagapalam*, (1989) 3 SCC 287.

8. *Prataprai N. Kothari v John Braganza*, (1999) 4 SCC 403: AIR 1999 SC 1666. *Ram Chander Aggarwal v Hans Raj Banga*, AIR 2003 NOC 109 (Del): 2002 AIHC 4102 (Del), the plaintiff has to prove his right to possession. He could not prove in this case that he had purchased the premises. The sale certificate produced by him was found to be not reliable. *Market Committee, Hodal v Sukhdevi*, (2016) 1 SCC 290: AIR 2016 SC 2226, no suit lies for recovery of possession of land which had already been acquired under statutory provisions, i.e. Land Acquisition Act, 1894.

9. *V. Rajeshwari v T.C. Saravanabava*, (2004) 1 SCC 551.

than in due course of law, he or any person claiming through him may, by suit, recover possession thereof, notwithstanding any other title that may be set up in such suit.

(2) No suit under this section shall be brought—

- (a) after the expiry of six months from the date of dispossession; or
- (b) against the Government.

(3) No appeal shall lie from any order or decree passed in any suit instituted under this section, nor shall any review of any such order or decree be allowed.

(4) Nothing in this section shall bar any person from suit to establish his title to such property and to recover possession thereof.

Sections 5 and 6 give alternative remedies and are mutually exclusive. Under Section 5 a person dispossessed can get possession on the basis of title, whereas under Section 6 a person dispossessed may recover possession merely by proving previous possession and subsequent wrongful dispossession. Under Section 6 he need not prove a better title against the occupier. The occupier will not be allowed to show his title by ownership, contract, prescription or inheritance.

Clause (4) of Section 6, however, provides that the person against whom a decree may be passed under clause (1) of Section 6 may, notwithstanding such a decree, sue to establish his title and to recover possession. The objects of Section 6 are:

- (i) To discourage people from taking the law into their own hands, however good their title may be.
- (ii) To provide a summary, cheap and useful remedy to a person dispossessed of immovable property otherwise than in due course of law.

Section 6 is applicable only if the plaintiff proves—

- (1) that he was in juridical possession of the immovable property in dispute;<sup>10</sup>
- (2) that he had been dispossessed without his consent and otherwise than in due course of law;<sup>11</sup> and

10. *Prem Sharma v Nishi Sharma*, AIR 2003 HP 45, entries in the Municipal Register of Assessments and the report lodged with the police of dispossession showed that the complainant was in possession of the house immediately before he was dispossessed. Relief for recovery of possession was granted. *Siya Ram v Nagar Palika Parishad*, AIR 2010 NOC 1111 (All), a footpath cannot be allotted to any person for business or otherwise. A person selling his goods by laying them on a footpath gets no right to make such use. His dispossession is not illegal. *Shantabai Sonba Madavi v Nanibai Udeebhan Uike*, AIR 2015 NOC 47 (Bom), plaintiff's case was that the suit property was purchased by her father and that she inherited it after her parents' death. Entries in Village Panchayat record, payment of taxes and electricity bills supported her claim of being the rightful owner. The defendant trespassed and was in wrongful possession. She was allowed to recover possession and mesne profit.

11. *Narbada Devi Gupta v Birendra Kumar Jaiswal*, (2003) 8 SCC 745; AIR 2004 SC 175, receipt for payment of rent shown with thumb impression of the land lady at back side and also signed by her son (plaintiff) at the back. The plaintiff admitted his signature. Thus tenancy became established ruling out a case of dispossession. The court said that the tenant had not to produce further evidence on the point. *Raj Narayan Pandey v Kameshwar Thakur*, AIR 2011

- (3) that the dispossession took place within six months from the date of the suit.<sup>12</sup>

Possession here means legal possession which may exist with or without actual possession and with or without a rightful origin. The plaintiff need not establish his title. It is enough to prove long standing peaceful possession.<sup>13</sup> Questions of title can be ignored. Relief can also be given on the basis of title with a permanent injunction against the defendant not to interfere in the plaintiff ownership and possessory rights.<sup>14</sup> A property was donated to All India Congress Party. There was split in the party. The party led by Indira Gandhi was declared by the Election Commission as the Indian National Congress. Its right of possession of the property was protected. The defendants who were in possession were ordered to vacate the property.<sup>15</sup> Thus where a trespasser is allowed to continue on the property and the owner sleeps upon his rights and makes no efforts to remove him, he will gain possession under Section 6. The possession of a tenant after the termination of the tenancy continues to be a juridical possession. His right to possession remains unless the owner gets a decree of eviction against him. Till then if he is dispossessed he is entitled to seek restitution of his possession.<sup>16</sup> In *Express Newspapers (P) Ltd v Union of India*<sup>17</sup> the Supreme Court reminded the Government that even where a perpetual lease for construction of an office block provided for the lessor's right of re-entry upon forfeiture of lease upon breaches of the conditions of the lease, the lessor

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Jha 13, shop tenant thrown out without recourse to the applicable Bihar tenancy legislation, restored to his possession by court order.

12. *Nair Service Society Ltd v K.C. Alexander*, AIR 1968 SC 1165: 1968 SCD 500. *Tirumala Tirupati Devasthanams v K.M. Krishnaiah*, (1998) 3 SCC 331: AIR 1998 SC 1132, where the suit for possession could not be filed within six months, the court said that a regular civil suit could be filed thereafter. *George Thomas v Srividya*, AIR 2003 Mad 290, property in wife's name, assessment in her name for payment of taxes, the building plan was also sanctioned in her name. The court did not accept the theory of *benami* for evasion of taxes. She was allowed to recover possession and damages. *Annakili v A. Vedanayagam*, (2007) 14 SCC 308: AIR 2008 SC 346, the High Court finding was that the title of the plaintiff had attained finality, it was for the defendant to prove that they had hostile possession under which the plaintiff's title became extinguished. The defendant could not do so. The plaintiff had not to file a suit for declaration of his title. *R. Rama Rao v R. Appala Swamy*, AIR 2011 Ori 1, six months have to be taken from the date of dispossession which may be found by the court on its own evidence and not on the basis of police report.

13. *Sanwal Ram v Ramjan*, AIR 2016 Chh 48.

14. *Manoj v Chandra Kishore*, AIR 2015 NOC 87 (Bom).

15. *Janatha Dal Party v Indian National Congress*, (2014) 16 SCC 731: AIR 2014 SC 1062.

16. See K.K. Verma v *Union of India*, AIR 1954 Bom 358: ILR 1954 Bom 950; *Lallu Yeshwant Singh v Rao Jagdish Singh*, AIR 1968 SC 620: (1968) 2 SCR 203; S.R. Ejaz v T.N. Handloom Weavers' Coop Society Ltd, (2002) 3 SCC 137: AIR 2002 SC 1152, the tenant proved that he was dispossessed, remand of the matter after a long period was held be wrongful because it had defeated the very purpose of the summary remedy. *Subrata Kumar Das v State of WB*, AIR 2010 Cal 49 (DB), suit filed after six months, has no meaning, police cannot be blamed for not putting the dispossessed person into possession. There is no violation of legal or fundamental rights.

17. (1986) 1 SCC 133: AIR 1986 SC 872.

would not have the right to declare such forfeiture all by itself and then take to itself to throw out the lessee either directly or through the summary procedure under the Public Premises (Eviction of Unauthorised Occupants) Act, 1971. The court said that where a breach is found, the lessor must adopt the due process of law by filing a civil suit to enforce the right of re-entry. Such a lessee is not an “unauthorised occupant” of a “public premises”. He will be entitled to relief against such eviction.

A tenant was dispossessed forcibly. The court said that he could institute his suit for repossession at that stage immediately. But he himself gained forcible repossession. He became a trespasser and therefore could not be regarded to be in lawful possession. He did file a suit subsequently but did not pursue it for numbering. It was numbered after three years. Relief of possession was not granted to him.<sup>18</sup>

Regarding appeals, the section itself says that there is no right of “appeal” against a decree in a suit under this section. Similarly a “review” of the decision is also barred. But a revision under Section 115 of the CPC may lie to the High Court, although courts have not favoured this remedy because the aggrieved party has another remedy open to him by way of a regular suit.

An interesting question may arise: Whether an action under Section 6 can be maintained in relation to incorporeal or intangible property, e.g. right of ferry, right of fishery, right to collect rents, right to cut grass, etc. There is a conflict of decisions on the point. The High Courts of Bombay and Madras have answered this question in the affirmative.<sup>19</sup> These courts have held that a man is said to be in possession of a right when he can exercise it, and he recovers possession of an incorporeal right when the obstruction which interfered with it is removed. But a contrary view has been expressed by the Calcutta High Court,<sup>20</sup> which has pointed out that this section does not extend to incorporeal rights because they are not rights of which possession can be taken and delivered to the plaintiff.

No injunction was issued against the owner of an item of movable property (vehicle) which had been delivered on hire purchase to prevent him from entering the premises of the hirer on his default in payments and to take away the vehicle. There was a clause to that effect in the contract.<sup>21</sup>

Further, it should be noted that the only prayer in a suit under Section 6 can be a prayer for recovery of possession. Consequently a claim for damages cannot be combined with that for possession. The section does not apply to suits based on title to property.<sup>22</sup>

18. *K. Krishna v A.N. Paramkusha Bai*, AIR 2011 AP 165.

19. *Mangaldas v Jivan Ram*, ILR (1899) 23 Bom 673; *Krishna v Akilanda*, ILR (1889) 13 Mad 54.

20. *Fadu Jhala v Gour Mohun Jhala*, 19 Cal 544.

21. *G.E. Capital Transportation Financial Services Ltd v Amritajit Mitra*, AIR 2009 NOC 1969 (Cal). Even in such a case, there would have to be permissive entry and not forcible entry.

22. *Nagar Palika v Jagat Singh*, (1995) 3 SCC 426: AIR 1995 SC 1377.

Possession, under the section, may be actual (*i.e.* physical) or constructive. Hence the possession of a mortgagee or a lessee is that of the mortgagor or the lessor and *vice versa*.<sup>23</sup>

A person who is in settled possession cannot be summarily dispossessed. Settled possession creates such a right that even the rightful owner may recover only by taking recourse to a court of law. The settled possession even of a trespasser may be protected.<sup>24</sup>

Relief cannot be refused only on the ground that the property in question is a joint family property. One of the co-owners was ousted from the property. He was allowed to exercise his right to seek possession of his share.<sup>25</sup> The right acquired by adverse possession, if not perfected by resort to Section 6, would cease to exist if possession is interrupted in the meantime.<sup>26</sup>

### Recovery of possession where possession gratuitous [S. 6]

Where the grant of possession was purely gratuitous, the owner had the right to reclaim possession even without the knowledge of the person in possession. The party in possession in this case was using the garage owned by his sister. The owner dispossessed him. The trial court ordered restoration of possession. The High Court confirmed this order. The Supreme Court described this as an error.

It was evident that the respondent was using the garage of the appellant on permission having been granted by the sister to the brother. According to the judgment of the High Court the respondent was claiming no legal interest in the said garage as he was not claiming its ownership because he was not claiming to be a tenant or even a licensee. His possession was purely gratuitous and even if without the knowledge of the respondent the appellant has reclaimed the possession, it was not a fit case for the High Court to have interfered under Article 227 of the Constitution.<sup>27</sup>

The person who was in permissive possession and whose claim of adverse possession proved to be false, was directed to handover possession to the owner.<sup>28</sup> Where possession was given for repairs but the premises happened to come down, it was held that there was no question of seeking restoration of possession. The proper course would have been to claim damages.<sup>29</sup>

23. *Jageshwar Singh v Jawahir Singh*, ILR (1875–80) 1 All 311.

24. *Rame Gowda v M. Varadappa Naidu*, (2004) 1 SCC 769. *Ajay Kumar v Chanchala Devi*, AIR 2011 HP 37, a trespasser who is settled in possession can regain his possession from any person, other than the owner, who dispossessed him.

25. *Gautam Gazmer v Uttam Gazmer*, 2014 SCC OnLine Cal 18020; AIR 2015 Cal 15; *City Municipal Council Bhalki v Gurappa*, (2016) 2 SCC 200, legal representatives of the deceased owner established before the trial court and High Court. Suit for title and possession allowed.

26. *Binode Das v Sarumai Parangia*, AIR 2014 NOC 73 (Gau).

27. *Anima Mallick v Ajoy Kumar Roy*, (2000) 4 SCC 119.

28. *Lakshmi v Karappathal*, AIR 2011 Bom 192; *Sardar Malkiat Singh v Kanwaljit Kaur*, AIR 2010 NOC 733 (Del), daughter-in-law living in father-in-law's house, she had to give up possession, she had already taken residential house where she was living after parting company with her husband.

29. *Ashok Kumar Chowan v A.G. Anwar Ali*, AIR 2010 Kant 70.

### Prayer for declaration of title

Although normally such a suit is not maintainable in the absence of a prayer for declaration of title, it was held on facts that as the necessary averments were made in the plaint (that registered lease deed for 99 years in favour of appellant-lessee was void and not binding and that suit property was trust property), and answered in the written statement, issues framed, evidence led and arguments advanced, no prejudice was caused to the appellant-defendant by the fact that there was no formal prayer seeking a declaration. The High Court rightly dismissed the LPA filed by the appellant-defendant under Order 6, Rule 1 of the Civil Procedure Code, 1908. The court said: "Even though there was no formal prayer, no prejudice has been caused to the appellant inasmuch as he has not been prevented from leading evidence on this aspect and has not been precluded from raising contentions in this behalf. All that was necessary to cure the defect was an amendment by incorporating one prayer. This could have been done at any stage."<sup>30</sup>

The Supreme Court has once again held that a suit for possession simpliciter without declaration of title is maintainable. On the facts here, however, title could not be successfully questioned.<sup>31</sup>

### No appeal or review [Sub-s. (3)]

No appeal lies from a decision in a suit under Section 6, nor any review is maintainable. But where a suit upon title is wrongly treated as a suit under Section 6, an appeal lies. The proper procedures for the appellate court in such a case is to remand the suit for fresh disposal. In a suit decided under Section 6, revision can be preferred on various grounds. If the error is palpable and the remedy is clear, the High Court can interfere in its revisional jurisdiction, but could not interfere on point of law especially when it is raised for the first time in revision. In the absence of jurisdictional error, the finding of the lower court cannot be disturbed by the High Court.<sup>32</sup>

Where an interim order was passed in a suit under Section 6 of the Specific Relief Act, it was held that the grant of such an order was not appealable under Order 43, Rule 1 of the Civil Procedure Code, 1908.<sup>33</sup>

### Application of Limitation Act

Section 14 of the Limitation Act, 1963 applies to proceedings against dispossessors. One of the effects would be that time taken in prosecuting proceedings under writ jurisdiction would be excluded.<sup>34</sup>

30. *Santokh Singh v Mahant Iqbal Singh*, (2000) 7 SCC 215: AIR 2000 SC 3155. *Bina Roy v Basanti Bhattacharya*, AIR 2009 NOC 119 (Cal), the matter of court fee is between the claimant and State, the claimant may pay court fee on his valuation, the defendant cannot say that no relief should be allowed because of inadequate court fee.

31. *Maddasani Venkata Narasaiah v Muddasani Sarojana*, AIR 2016 SC 2250.

32. *Gafoor Khan v Amiruddin*, AIR 2012 Raj 35.

33. *Madhukarbhai Trambaklal Shahthro v Sterling Bhopal City Coop Housing Society*, AIR 2009 NOC 262 (Guj).

34. *Pratapsing Ganpatrao Kadam v Maruti Raghunath Todkar*, AIR 2003 Bom 11.

*Six months limitation not applicable to proceedings under CrPC*

The finding that the appellants should have come within six months from the date of dispossession was held to be not tenable as the Specific Relief Act has no application to proceedings under Section 145(6) of the Criminal Procedure Code.<sup>35</sup>

#### *Counterclaim and court fee*

The defendant was unlawfully dispossessed and wanted enforcement of his statutory right under Section 6 of regaining possession. A counterclaim was filed against it. The counterclaim being in the nature of a plaint in a suit, the court said, it did not require to be valued under Section 6(v) of the Bombay Court Fees Act.<sup>36</sup>

### RECOVERY OF POSSESSION OF MOVABLE PROPERTY [SS. 7-8]

Sections 7 and 8 of the Specific Relief Act, 1963 provide methods for recovery of possession of some specific movable property.

**S. 7. Recovery of specific movable property.**—A person entitled to the possession of specific movable property may recover it in the manner provided by the Code of Civil Procedure, 1908 (5 of 1908).

*Explanation I.*—A trustee may sue under this section for the possession of movable property to the beneficial interest in which the person for whom he is trustee is entitled.

*Explanation II.*—A special or temporary right to the present possession of movable property is sufficient to support a suit under this section.

#### Main ingredients

By Section 7, it is provided that a person entitled to the possession of the specific movable property may recover the same in the manner prescribed by the Code of Civil Procedure.<sup>37</sup> The main ingredients of this section are:

35. *Shakuntala Devi v Chamru Mahto*, AIR 2009 SC 2075.

36. *Sushila Uttamchand Jain v Rajesh Kumar Prakashchand Jain*, AIR 2012 Bom 22.

37. *Punjab Urban Planning & Development Authority v Shiv Saraswati Iron & Steel Re-Rolling Mills*, (1998) 4 SCC 539, the plaintiff has to prove his own case. He cannot think of succeeding because of the weakness of the defendant's case. This "section" corresponds to S. 10 of the erstwhile Specific Relief Act, 1877. That section carried the following illustrations:

- (a) A bequeaths land to B for his life, with remainder to C. A dies. B enters on the land, but C, without B's consent, obtains possession of the title-deeds. B may recover them from C.
- (b) A pledges certain jewels to B to secure a loan. B disposes of them before he is entitled to do so. A, without having paid or tendered the amount of loan, sues B for possession of the jewels. The suit should be dismissed, as A is not entitled to their possession, whatever right he may have to secure their safe custody. [Based on *Donald v Suckling*, (1866) LR 1 QB 585.]
- (c) A receives a letter addressed to him by B. B gets back the letter without A's consent. A has such a property therein as entitles him to recover it from B. [Based on *Oliver v Oliver*, (1861) 11 CB NS 139.]

- (i) The plaintiff must be entitled to the possession. A person may be entitled to possession either by ownership or as provided by Explanation 2 to Section 7 by virtue of a special or temporary right. It is not necessary, however, that the plaintiff should have been previously in possession, or that the goods should have been removed from his possession. A special or temporary right may arise by either:
  - (a) the act of the owner of the goods, e.g., bailment, pawn, etc. In this case the bailee or pawnee has special right, or;
  - (b) not by the act of the owner of goods, e.g., finder of lost goods. In this case the finder of lost goods has a special right to possession except against the true owner.

*Explanation I* makes it clear that a trustee is the person entitled to the immediate possession of trust property. Hence if trust property is taken away by someone, he can recover the same.

A person who does not have a right to present possession of movable property cannot maintain a suit under this section. An illustration in point is: *A* pledges certain jewels with *B* to secure a loan. *B* disposes the jewels to *C* before he is entitled to do so. *A* without having paid the amount of the loan, sues *C* for possession of jewels. The suit should be dismissed, as *A* is not entitled to immediate possession of jewels, whatever interest he may have to secure their safe custody.

- (ii) Property in question must be specific movable property. Specific means that which is ascertained or ascertainable. Specific property means the very property itself, not its equivalent. Thus coins or grains are not specific movable property, because they cannot be distinguished from other coins or grain.

The specific movable property must be capable of being seized and delivered. Where the goods have ceased to be recoverable or are not in possession or control of the defendant, the plaintiff is not entitled to a decree for recovery *in specie*; his only remedy then being damages or compensation.

### Suit for title

The substantive prayer in the plaint was for a declaration that the plaintiffs "were fully entitled" to the suit bonds and certain reliefs which were founded upon this declaration. A suit for such a declaration would certainly be a title suit so far as the suit bonds were concerned. On dismissal of the suit, the appeal against it was brought on the footing that the plaintiff had fully proved its title to the suit bonds and that the Special Court had erroneously held against the plaintiff. The court said that looking at the suit from

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- (d) *A* deposits books and papers for safe custody with *B*. *B* loses them and *C* finds them, but refuses to deliver them to *B* when demanded. *B* may recover them from *C*, subject to *C*'s right, if any, under Section 168 of the Indian Contract Act, 1872.
  - (e) *A*, a warehouse-keeper, is charged with the delivery of certain goods to *Z*, which *B* takes out of *A*'s possession, *A* may sue *B* for the goods.

any point of view it could not be held that the suit was a mere declaratory suit, it had to be regarded as a title suit.<sup>38</sup>

## Limitation

Article 91(b) of the Limitation Act, 1963 prescribes a period of three years' limitation for the suit computable from the date when the property is wrongfully taken or injured or when the detainer's possession becomes unlawful.

## Liability to deliver possession to person entitled

**S. 8. Liability of person in possession, not as owner, to deliver to person entitled to immediate possession.**—Any person having the possession or control of a particular article of movable property, of which he is not the owner, may be compelled specifically to deliver it to the person entitled to its immediate possession, in any of the following cases:

- (a) when the thing claimed is held by the defendant as the agent or trustee of the plaintiff.
- (b) when compensation in money would not afford the plaintiff adequate relief for the loss of the thing claimed.<sup>39</sup>
- (c) when it would be extremely difficult to ascertain the actual damage caused by its loss;<sup>40</sup>
- (d) when the possession of the thing claimed has been wrongfully transferred from the plaintiff.<sup>41</sup>

*Explanation.*—Unless and until the contrary is proved, the court shall in respect of any article of movable property claimed under clause (b) or clause (c) of this section, presume—

- (a) that compensation in money would not afford the plaintiff adequate relief for the loss of the thing claimed, or, as the case may be;
- (b) that it would be extremely difficult to ascertain the actual damage caused by its loss.<sup>42</sup>

38. *Standard Chartered Bank v Andhra Bank Financial Services Ltd*, (2006) 6 SCC 94.

39. Proof of entrustment of the property in question would be necessary. *Ganga Bishan v Jai Narain*, (1986) 1 SCC 75: AIR 1986 SC 441. There may be a thing which may not have much intrinsic value, but, by reason of peculiar association or some special consideration, have obtained in the eyes of its holders a value that cannot be estimated in money, e.g. family idol. It would be great injustice if an individual cannot have his property without being liable to the estimate of people who have not their feelings upon it. A thing may have a *prestige affections* which it is impossible to value in sordid gold or silver. However, the principle must not be extended to cases founded in weakness and folly. It would, therefore, be a perversion of the rule to apply it to the delivery of a lady's lap dog.

40. There exists no standard to ascertain their value, e.g. rare picture painted by a dead painter, articles of antiquity and the like.

41. E.g. by a tort, or where defendant has obtained the goods by fraud or where servant has pawned the goods of master without the authority of the master.

42. This section corresponds with S. 11 of the repealed Specific Relief Act, 1877. That section carried the following illustrations:

*Illustration as to clause (a).*—A, proceeding to Europe, leaves his furniture in charge of B, as his agent during his absence. B, without A's authority, pledges the furniture to C, and C,

### *Ingredients*

In order that Section 8 may come into operation the following ingredients must coexist—

- (1) the defendant has possession or control of the particular article claimed;
- (2) such article is movable property;
- (3) the defendant is not the owner of the article;
- (4) the person claiming, that is, the plaintiff, is entitled to immediate possession; and
- (5) the thing claimed is held by the defendant as the plaintiff's agent or trustee; or when compensation in money would not afford adequate relief for the loss of the thing claimed; or when it is extremely difficult to ascertain the actual damage caused by the loss of the thing claimed; or when the possession of the thing claimed has been wrongfully transferred from the claimant.

An illustration of the types of cases falling under this section would be like this. A person, while going abroad, leaves his furniture under the care of his friend. The friend is a trustee of the articles and is bound to return them when demanded. If the friend pledges the furniture, the pledgee will also remain subject to the same trust and similarly bound to return to the owner when demanded by him.<sup>43</sup>

An illustration under clause (b) would be, for example, when the idol of a family temple is in the custody of a retired priest, he is bound to return it to the family.

Cases coming under clause (c) would be, for example, when articles of rare value, like original paintings of a deceased painter, are in the possession of another. Since they are articles of irreplaceable nature and their market value is of unascertainable nature, the owner has a right to recover them *in specie*.<sup>44</sup>

Under clause (a) the onus is on the plaintiff to prove the fiduciary relationship and under clause (d) the onus is on the plaintiff to prove the wrongful transfer. The *Explanation* deals with the onus under clauses (b) and (c), which is placed on the defendant and the defendant has to prove that

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knowing that B had no right to pledge the furniture, advertises it for sale. C may be compelled to deliver the furniture to A, for he holds it as A's trustee. [Based on *Wood v Rowcliffe*, (1844) 3 Hare 304: 64 RR 303].

*Illustration as to clause (b).*—Z has got possession of an idol belonging to A's family, and of which A is the proper custodian. Z may be compelled to deliver the idol to A.

*Illustration as to clause (c).*—A is entitled to a picture by a dead painter and a pair of rare China vases. B has possession of them. The articles are of too special a character to bear an ascertainable market value. B may be compelled to deliver them to A. [Based on *Falcke v Gray*, (1859) 4 Drew 651: 113 RR 493].

43. Based on *Wood v Rowcliffe*, (1844) 3 Hare 304: 64 RR 303.

44. Based on *Falcke v Gray*, (1859) 4 Drew 651: 113 RR 493.

compensation in money would be adequate relief and that it would not be extremely difficult to ascertain the actual damage caused by the loss of the chattel.

### Difference between Sections 7 and 8

(i) Under Section 8, no suit can be brought against the owner, while under Section 7, a person having a special or temporary right to present possession may bring the suit even against the owner of the property.

(ii) Under Section 7, a decree is for the return of movable property, or for the money value thereof in the alternative, while under Section 8 the decree is only for the return of the specific article.

## SPECIFIC PERFORMANCE OF CONTRACTS

Specific performance is equitable relief given by a court in case of breach of contract in the form of a judgment that the defendant is to actually perform the contract according to its terms and stipulations.

A contract, according to the Indian Contract Act, is an agreement enforceable by law. From every contract there immediately and directly results an obligation on each of the contracting parties towards the other to perform such of the terms of the contract as he has undertaken to perform.<sup>45</sup> And if the person on whom this obligation rests, fails to discharge it, there results in morality to the other party a right at his election either to insist on the actual performance of the contract or to obtain satisfaction for the non-performance of it.

An obligation includes every duty enforceable by law. Consequently, whenever a man comes under a liability to do or forbear from doing anything, he remains under an obligation. This liability may be a consequence of either a contract or a tort. An obligation to forbear is a positive duty generally imposed by a contract. This form of specific relief is described as "the specific performance of contract".

**S. 9. Defences respecting suits for relief based on contract.**— Except as otherwise provided herein, where any relief is claimed under this Chapter in respect of a contract, the person against whom the relief is claimed may plead by way of defence any ground which is available to him under any law relating to contracts.

### Defences under law of contracts

Section 9 of the Specific Relief Act, 1963 provides that except as provided in this chapter (*i.e.* Chapter II, Sections 9 to 25) all defences open under the law of contract shall be open to a defendant, where any relief is claimed under this Chapter in respect of a contract. Defences that are available

45. *Kumari Anandan v T. Balamukunda Rao*, AIR 2002 Mad 472; *Ameer Mohd v Barkat Ali*, AIR 2002 Raj 406, in both these cases the action was founded upon oral agreement, but the details of the agreement were not proved and, therefore, no relief could be allowed.

under the law of contract, such as incapacity of parties, the uncertainty of contracts, coercion, undue influence, fraud, misrepresentation, mistake, etc. have all been dealt with in the Indian Contract Act. This section avoids their repetition in the Specific Relief Act. Thus it is necessary that the contract in question should be valid and enforceable. The Supreme Court refused to grant the relief of specific performance where the contract was in an alternative form and one form had failed to materialise and the other was void, being not enforceable by virtue of uncertainty. It was a contract of sale stipulating that if the co-seller failed to sign the sale deed then the principal seller would execute a sale deed of her own "one of two shares", otherwise pay back the advance and compensation in the same amount. The co-seller did not sign. The alternative for the promisor was either to sell her share or pay compensation. If she opted for compensation there was no breach and no question of specific performance, which was also not possible because her share was not defined nor was there any indication of the part of the lump sum consideration which was applicable to her share.<sup>46</sup>

A contingent contract to the effect that the mortgaged house would be sold as soon as the mortgage was redeemed was held by the Supreme Court to be specifically enforceable on the redemption of the mortgage, though no relief could be provided on facts because the claim was filed more than three years after the date of redemption.<sup>47</sup>

#### *Government contracts*

It has been held that a Government contract which is concluded without fulfilling the requirements prescribed by Article 299 of the Constitution of India cannot be specifically enforced.<sup>48</sup>

#### *Validity of original contract*

In a suit for specific performance, the subsequent purchaser challenged the contention that the original contract to sell was fictitious and not genuine, but the suit was ultimately decreed. It was held that the first appellate court ought to have considered the evidence and recorded its own finding as to whether the original agreement was true and valid.<sup>49</sup>

46. *Mayawanti v Kaushalya Devi*, (1990) 3 SCC 1. A contract with the Government which did not comply with the requirements of Art. 299 of the Constitution was not allowed to be enforced. *Sohan Lal v Union of India*, (1991) 1 SCC 438: AIR 1991 SC 955. *C. Bala Subba Reddy v Lakshmi Narasamma*, (2002) 10 SCC 247: AIR 2002 SC 390, a new plea not allowed to be raised at the appellate stage.
47. *Ramzan v Hussaini*, (1990) 1 SCC 104: AIR 1990 SC 529. *Parmanand v Bajrang*, (2001) 7 SCC 705, the defence raised was that money was not taken as a consideration for sale but by way of loan and the property was offered as a security for repayment of loan and he sought adjournment for adducing evidence to prove the real nature of the transaction, rejecting his defence without giving him the opportunity to prove was held to be wrong. The suit was remanded for retrial.
48. *Bishandayal & Sons v State of Orissa*, (2001) 1 SCC 555: AIR 2001 SC 544.
49. *Ram Niwas v Bano*, (2000) 6 SCC 685: AIR 2000 SC 2921. *Hansa V. Gandhi v Deep Shankar Roy*, (2013) 12 SCC 776: (2013) 116 Cut LT 457, a letter of intent does not bring about a concluded contract, without such contract there is no right to seek specific performance.

The defence that the purchase was made *bona fide* for consideration without notice of the earlier agreement for sale would have to be proved by the second purchaser. This defence can be defeated by showing that a notice of the sale was given to him. Where the only evidence of prior notice was a copy of an application appearing to be endorsed by the Sub-Registrar but there was no corresponding record or entry in the records of the Sub-Registrar, it was held that such an application would not constitute prior notice.<sup>50</sup>

Privity of contract between the parties to the suit is also a thing of cardinal importance for a decree of specific performance.<sup>51</sup>

#### *Delay as ground of defence under law of contract*

Where a suit was within the period of limitation, but delay had resulted in third parties acquiring rights in the subject-matter of the suit or had given rise to a plea of waiver it was held that it would provide grounds of defence in a suit for specific performance of contract for sale of immovable property.<sup>52</sup>

The present appeal arises out of an agreement for sale of the suit property, between the appellant would-be purchaser and respondent vendor. Under the agreement the consideration fixed was Rs 25,000; of this sum the appellant paid Rs 17,000 at the time of the execution of the contract on 20 February 1977. The balance amount was to be paid within five months, *i.e.* before 19 July 1977, at the time of the execution of the sale deed. According to the appellant, the respondent would not accept the balance amount due and did not execute the sale deed. Therefore the appellant sent three notices dated 15 March 1978, 4 April 1978 and the last on 26 November 1978, through his lawyer to no avail. On 10 August 1979, about nine months after the date of the last notice, the appellant filed a suit for specific performance and, in the alternative, for damages to the sum of Rs 38,000. The respondent-defendant denied the execution of the agreement for sale, his signature on it and the receipt of Rs 17,000 as part-consideration. The trial court found that the agreement had been executed as averred and decreed the suit for specific performance.

On appeal the Bombay High Court affirmed the finding as to the existence of the agreement but set aside the relief as to specific performance and allowed compensation. The Supreme Court allowed the appeal against this judgment with costs. The court said:

“The aspects of delay which are relevant in a case of specific performance of contract for sale of immovable property are:

- (i) delay running beyond the period prescribed under the Limitation Act;

50. *Zorawar Singh v Sarwan Singh*, (2002) 4 SCC 460: AIR 2002 SC 1711.

51. *Church of Christ Charitable Trust & Educational Charitable Society v Ponniamman Educational Trust*, (2012) 8 SCC 706: (2012) 4 SCC (Civ) 612.

52. Limitation Act, 1963, Art. 34.

- (ii) delay in cases where, though the suit is within the period of limitation, yet:
  - (a) due to delay the third parties have acquired rights in the subject-matter of the suit;
  - (b) in the facts and circumstances of the case, delay may give rise to plea of waiver or otherwise it will be inequitable to grant a discretionary relief.

Here none of the above-mentioned aspects applied. The last notice was issued on 26-11-1978 and from that date the suit was filed only after nine months and not after more than a year as noted by the High Court. Therefore on the facts of this case the ground of delay cannot be invoked to deny relief to the plaintiff.”<sup>53</sup>

Section 10 of the Specific Relief Act enumerates those cases in which the specific performance of contracts can be enforced.

**S. 10. Cases in which specific performance of contract enforceable.**—Except as otherwise provided in this chapter, the specific performance of any contract may, in the discretion of the Court, be enforced—

- (a) when there exists no standard for ascertaining the actual damage caused by the non-performance of the act agreed to be done; or
- (b) when the act agreed to be done is such that compensation in money, for its non-performance would not afford adequate relief.

*Explanation.*—Unless and until the contrary is proved, the Court shall presume—

- (i) that the breach of a contract to transfer immovable property cannot be adequately relieved by compensation in money; and
- (ii) that the breach of a contract to transfer movable property can be so relieved except in the following cases—
  - (a) where the property is not an ordinary article of commerce, or is of special value or interest to the plaintiff or consists of goods which are not easily obtainable in the market;
  - (b) where the property is held by the defendant as the agent or trustee of the plaintiff.<sup>54</sup>

53. *Motilal Jain v Ramdasi Devi*, (2000) 6 SCC 420; AIR 2000 SC 2408.

54. Clauses (a) and (b) of this section correspond with clauses (b) and (c) of S. 12 of the repealed Specific Relief Act, 1877. The relevant illustrations appended to the provision in that Act may be reproduced:

*Illustration as to clause (a).*—A agrees to buy, and B agrees to sell, a picture by a dead painter and two rare China vases. A may compel B specifically to perform this contract, for there is no standard for ascertaining the actual damage which would be caused by its non-performance. [Based on *Falcke v Gray*, (1859) 4 Drew 651: 113 RR 493.]

*Illustrations as to clause (b).*—(1) A contracts with B to sell him a house for Rs 1000. B is entitled to a decree directing A to convey the house to him, he paying the purchase-money.

(2) In consideration of being released from certain obligations imposed on it by its Act of Incorporation, a railway company contracts with Z to make an archway through their railway to connect lands of Z severed by the railway, to construct a road between certain specified points, to pay a certain annual sum towards the maintenance of this road, and

## Contracts which are specifically enforceable [S. 10]

### *Where no other suitable remedy*

In a case before the Supreme Court a family woman (appellant's mother) borrowed a sum of money from a family member (respondent's father) and executed a deed of sale of her property in favour of the lender's minor son with an agreement of reconveyance on repayment of the loan. The dues under the loan were paid back and on denial of reconveyance, the Supreme Court upheld the decree of specific performance ordering reconveyance. The mortgagee having disposed of the property, the decree was allowed to be enforced against such buyer also.<sup>55</sup>

The shares of a private company have been held to be goods of such a nature as they are not easily obtainable in the market. The court, therefore, laid down that specific performance should be granted in such cases.<sup>56</sup> The court cited the following opinion of the Privy Council:<sup>57</sup> "It is also the opinion of the Board that having regard to the nature of the company and limited market for its shares, damages would not be an adequate remedy."

### *Valid contract in existence*

There should be a concluded contract. In the present, there was an agreement for transfer of property. The transferor did not dispute the agreement in his reply to the notice from the transferee. He did not even dispute in his written statement averments made in the plaint as to the agreement. No such

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also to construct a siding and a wharf as specified in the contract. Z is entitled to have this contract specifically enforced, for his interest in its performance cannot be adequately compensated for by money; and the court may appoint a proper person to superintend the construction of the archway, road, siding and wharf. [Based on *Storer v Great Western Rly Co*, (1842) 2 Y & CCh Cas 48: 63 ER 21.]

(3) A contracts to sell, and B contracts to buy, a certain number of railway-shares of a particular description. A refuses to complete the sale. B may compel A specifically to perform *this* agreement, for the shares are limited in number and not always to be had in the market, and their possession carries with it the status of a shareholder, which cannot otherwise be procured.

(4) A contracts with B to paint a picture for B, who agrees to pay therefor Rs 1000. The picture is painted. B is entitled to have it delivered to him on payment or tender of Rs 1000.

55. *Nivarti Govind Ingale v Revana Bhimanagouda Patil*, (1997) 1 SCC 475. *Kaulashwari Devi v Nawal Kishore*, 1955 Supp (1) SCC 141: AIR 1994 SC 1200, subsequent buyer of the property affected by the decree. *M. Ramalingam v Subramanyam*, AIR 2003 Mad 305, registered sale deed, the seller could not prove that it was a mortgage transaction. Consideration not low, thus the agreement was for sale, the defendant compellable to perform his part of the contract. *Aniglase Yohannan v Ramlatha*, (2005) 7 SCC 534: AIR 2005 SC 3503, found from averments in the plaint and from evidence that the plaintiff had complied with statutory requirements. He was entitled to specific relief. *Vishwa Nath Sharma v Shyam Shanker Goenka*, (2007) 10 SCC 595, sale of sub-lease of plot taken from DDA, permission of the Authority being necessary, the decree had to be moulded accordingly. *P.S. Ranakrishna Reddy v M.K. Bhagyalakshmi*, (2007) 10 SCC 231: AIR 2007 SC 1256, agreement found to be one of sale and not loan, a provision for damages in case of default was not a determinative factor.

56. *M.S. Madhusoodhanan v Kerala Kaumudi P Ltd*, (2004) 9 SCC 204: AIR 2004 SC 909.

57. *Bank of India Ltd v Jamsetji A.H. Chinoy & Chinoy and Co*, (1949-50) 77 IA 76: AIR 1950 PC 90.



plea was raised before the High Court or the trial court. Hence, existence of the agreement was not disputed.<sup>58</sup>

The other two requirements for seeking specific relief are that the defendant committed breach of the contract and that the plaintiff was always ready and willing to perform his part of the obligation in terms of the contract.<sup>59</sup>

Where an agreement for sale prescribed a retrospective date for execution, the court said that it was not permissible. It would make the contract vague and therefore, incapable of execution. Such an agreement cannot be sought to be specifically enforced.<sup>60</sup>

#### *Contract not extinguished by decree*

The passing of decree for specific performance does not extinguish the contract between the parties. The parties continue to be entitled to their rights and bound by their obligation under the contract. The decree for specific performance merely recognises entitlement to the claim for specific performance.<sup>61</sup>

#### *Agreement for reconveyance or repurchase*

An agreement to repurchase property which had been sold, popularly known as agreement for reconveyance, has been held to be specifically enforceable. Referring to such an agreement in *V. Pechimuthu v Gowrammal*,<sup>62</sup> the Supreme Court said:

“Such an agreement, not being merely a privilege or concession, such as an option to purchase, granted to the owner, remains an agreement for sale of immovable property and must be governed by the same provisions of law as are applicable to ordinary agreements for sale. Decision as to whether an agreement is an option to purchase or an ordinary agreement depends on interpretation of its terms. It was held on the facts that the reconveyance agreement in favour of the appellant-plaintiff, the original vendor, was an ordinary agreement for sale. The High Court in second appeal erred in reversing the decree of specific performance in his favour granted by trial court and affirmed by first appellate court.”

#### *Delay*

Unreasonable delay by a plaintiff in performing his part of the contract operates as a bar to his obtaining specific performance, provided that—

58. *Kammana Sambamurthy v Kalipatnapu Atchutamma*, (2011) 11 SCC 153: AIR 2011 SC 103.

59. *Man Kaur v Hartar Singh Sangha*, (2010) 10 SCC 512. The Supreme Court emphasised that it is not necessary that there should be a provision in the contract entitling the aggrieved party to seek specific relief.

60. *Bachan Kaur v Sadhu Singh*, AIR 2016 NOC 291 (P&H).

61. *Amol v Deorao*, AIR 2011 NOC 215 (Bom).

62. (2001) 7 SCC 617: AIR 2001 SC 2446. *Bismillah Begum v Rahmatullah Khan*, (1998) 2 SCC 226: AIR 1998 SC 970, time is of the essence in a contract of reconveyance. *V.R. Sudhakara Rao v T.V. Kameswari*, (2007) 6 SCC 650, oral contract, there is necessity of proof of fully concluded contract and its essential terms.

- (i) time was originally the essential element of the contract; or
- (ii) it was made an essential element by a subsequent notice; or
- (iii) the delay has been so unreasonable and long that it amounts to abandonment of the contract.<sup>63</sup>

As a general proposition of law, in the case of sale of immovable property there is no presumption as to time being the essence of the contract. Even if it is not of the essence of the contract the Court may infer that it is to be performed within a reasonable time if the conditions are evident:

- (i) from the express terms of the contract;
- (ii) from the nature of the property; and
- (iii) from the surrounding circumstances, for example, the object of making the contract.

From the expression, “Rs 98,000 (rupees ninety-eight thousand only) will be paid by the second party to the first party within a period of ten days only” in the contract, it is clear that the amount of Rs 98,000 ought to have been paid on or before the 10th day. Failure to do so constituted a breach committed by the defendant. The word “only” has been used twice over (1) to qualify the amount of Rs 98,000, and (2) to qualify the period of 10 days. The evidence also showed that the plaintiff was not willing to pay this amount unless vacant delivery of possession of one room on the ground floor was given. The notices which were exchanged between the parties have to be looked into in determining readiness and willingness.<sup>64</sup>

It has been held that a person seeking specific enforcement of a contract must approach the court within reasonable time even if time is not of the essence of the contract. It was further held that “reasonable time” means as soon as circumstances permit. Where the defendant was to remove a telegraph pole from a property and then to execute the sale deed, but he only removed the pole and did not execute the sale deed despite notice and the plaintiff filed a suit within one month of removal of the pole, it was held, on the facts, that the suit was filed within reasonable time. Time was not of the essence of the present contract. The court said: “The word ‘reasonable’ has in law a *prima facie* meaning of reasonable in regard to those circumstances of which the person concerned is called upon to act reasonably knows or ought to know as to what was reasonable. It may be unreasonable to give an exact definition of the word ‘reasonable’. The reason varies in its conclusion according to idiosyncrasy of the individual and the time and circumstances in which he thinks. The dictionary meaning of ‘reasonable time’ is to be so much time as is necessary, under the circumstances, to do conveniently what

63. *K.S. Vidyanadam v Vairavan*, (1997) 3 SCC 1: AIR 1997 SC 1751, delay of 2½ years after paying a small amount by way of earnest money for purchasing immovable property, disentitled from claiming specific recovery of property. *Deokabai v Utam*, (1993) 4 SCC 181, delay in executing the conditions of the sale deprived the right to specific performance, refund of earnest money ordered.

64. *Chand Rani v Kamal Rani*, (1993) 1 SCC 519: AIR 1993 SC 1742.



the contract or duty requires should be done in a particular case. In other words it means, as soon as circumstances permit."

"The legal action initiated by the appellant-plaintiff was rightly held by the trial court and the first appellate court to have been commenced without delay and definitely within a reasonable time. The High Court was not justified in disturbing the finding of fact arrived at on appreciation of the evidence, while disposing of the second appeal."<sup>65</sup>

A valid contract of sale must be proved by producing the original document. In this case a copy of the contract typed in duplicate was produced before the court. The son of the deceased vendor admitted the signature of his father. The High Court found on evidence that the original document was retained by the vendor and he did not produce it. The High Court accepted the document as genuine and its contents as true. The Supreme Court held that on the evidence on the record, sufficient foundation for accepting the document by way of secondary evidence in terms of Section 65 of the Evidence Act had been laid.<sup>66</sup>

It has been held by the Supreme Court that specific performance of a contract cannot be decreed against a defendant who is devoid of title—*Nemo dat quod non habet*.<sup>67</sup>

#### *Sale by joint owners*

The Supreme Court propounded the following proposition: "Where any property is held jointly, and once any party to the contract has agreed to sell such joint property by agreement, then, even if the other co-sharer has not joined, at least to the extent of his share, he is bound to execute the sale deed. However, in the absence of the other co-sharer there could not be any decree of any specified part of the property to be partitioned and possession given. The decree could only be to the extent of transferring the share of the appellants in such property to other such contracting party. In the present case, it is not in dispute that the appellants have 5/6ths share in the property. So, the plaintiff's suit for specific performance to the extent of

65. *Veerayee Ammal v Seenii Ammal*, (2002) 1 SCC 134: AIR 2001 SC 2920. Where there is no concluded contract, the relief of specific performance cannot be had, *Ganesh Shet v C.S.G.K. Setty*, (1998) 5 SCC 381. *Gunwantbhai Mulchand Shah v Anton Elis Farel*, (2006) 3 SCC 634: AIR 2006 SC 1556, sale agreement, case remanded for redetermination on merits including the point of limitation, because the matter was 29 years old. *Vishwa Nath Sharma v Shyam Shanker Goenka*, (2007) 10 SCC 595, compensation for appreciation in value of property when specific performance was granted after several years.

66. *T. Mohan v Kannammal*, (2002) 10 SCC 82. *Jai Narain Parasrampuria v Pushpa Devi Saraf*, (2006) 7 SCC 756, a clear and valid agreement of sale was not allowed to be taken out of the scope of specific performance by trying to put in the category of a loan transaction. *Dyaneshwar Ramachandra Rao Patange v Bhagirathibai*, (2006) 6 SCC 663, the person, who was vendee of the property under an agreement, died leaving behind his widow and three daughters. His brother applied for specific enforcement of the agreement contending that the widow had remarried and two daughters relinquished the share in his favour. The court did not consider these points because the brother had no right, to the exclusion of the legal heirs, to file the suit.

67. *Maya Devi v Lata Prasad*, (2015) 5 SCC 588.

this 5/6ths share was rightly decreed by the High Court which requires no interference.”<sup>68</sup>

**S. 11. Cases in which specific performance of contracts connected with trusts enforceable.**—(1) Except as otherwise provided in this Act, specific performance of a contract may, in the discretion of the court, be enforced when the act agreed to be done is in the performance wholly or partly of a trust.

(2) A contract made by a trustee in excess of his powers or in breach of trust cannot be specifically enforced.

### Performance of trusts

Section 11(1) provides another circumstance in which contracts can be specifically enforced.

#### *Enforcement of trustee's duty*

The creation of a trust imposes a duty on the trustees, which may be enforced even by strangers to the transaction who may not have been in existence at its date, if they have an interest under the contract. Thus contracts connected with trusts can be specifically enforced either at the instance of the beneficiaries or at the instance of the trustees.

Section 11(2), however, provides that a contract made by a trustee:

- (i) in excess of his powers, or
  - (ii) in breach of trust,
- cannot be specifically enforced.

In the first case it is beyond his competence and, in the second case, it is unlawful. “In breach of trust” means acting in violation of the duties and obligations imposed by the trust.<sup>69</sup>

68. *A. Abdul Rashid Khan v P.A.K.A. Shahul Hamid*, (2000) 10 SCC 636. *Surinder Singh v Kapoor Singh*, (2002) 10 SCC 109, the other joint owner contested the suit on the ground that she was not a party to the contract. The court dissented from the decision in *Kartar Singh v Harjinder Singh*, (1999) 3 SCC 517 in which the court ordered delivery of half share of the joint property on payment of half of the consideration money. *Awadesh Yadav v Suresh Thakur*, (2002) 10 SCC 156, joint Hindu family property, the *Karta* was found to be not competent to sell.

69. S. 11 brings together Ss. 12(a) and 21(e) of the repealed Specific Relief Act, 1877. The relevant illustrations appended there that Act may be reproduced:

(1) A holds certain stock in trust for B. A wrongfully disposes of the stock. The law creates an obligation on A to restore the same quantity of stock to B, and B may enforce specific performance of this obligation. [This illustration was repealed wherever the Indian Trusts Act, 1882 is in force—see S. 2 and Schedule of that Act.]

(2) A is a trustee of land with power to lease it for seven years. He enters into a contract with B to grant a lease of the land for seven years, with a covenant to renew the lease at the expiry of the term. This contract cannot be specifically enforced. [Based on *Mortlock v Buller*, (1804) 10 Ves 292: 7 RR 417.]

(3) The directors of a company have power to sell the concern with the sanction of a general meeting of the shareholders. They contract to sell it without any such sanction. This contract cannot be specifically enforced.

(4) Two trustees, A and B, empowered to sell trust property worth a lakh of rupees, contract to sell it to C for Rs 30,000. The contract is so disadvantageous as to be a breach of trust.

### *Limitation*

A suit for specific enforcement should be filed for specific performance within the period stipulated under Article 54 of the Limitation Act, 1963.<sup>70</sup> In a contract where no date for performance was final, the court said that the period of limitation would start running from the date on which the plaintiff comes to know that the other party was refusing performance.<sup>71</sup>

**S. 12. Specific performance of part of contract.**—(1) Except as otherwise hereinafter provided in this section, the court shall not direct the specific performance of a part of a contract.

(2) Where a party to a contract is unable to perform the whole of his part of it, but the part which must be left unperformed bears only a small proportion to the whole in value and admits of compensation in money, the court may, at the suit of either party, direct the specific performance of so much of the contract as can be performed, and award compensation in money for the deficiency.<sup>72</sup>

(3) Where a party to a contract is unable to perform the whole of his part of it, and the part which must be left unperformed either—

(a) forms a considerable part of the whole, though admitting of compensation in money; or

(b) does not admit of compensation in money;

he is not entitled to obtain a decree for specific performance; but the court may, at the suit of the other party, direct the party in default to perform specifically so much of his part of the contract as he can perform, if the other party—

(i) in a case falling under clause (a), pays or has paid the agreed consideration for the whole of the contract reduced by the consideration for the part which must be left unperformed and in a case falling under clause (b),<sup>73</sup> [pays or has paid] the consideration for the whole of the contract without any abatement; and

(ii) in either case, relinquishes all claims to the performance of the remaining part of the contract and all right to compensation, either for the deficiency or for the loss or damage sustained by him through the default of the defendant.<sup>74</sup>

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C cannot enforce its specific performance. [Based on *Mortlock v Buller*, (1804) 10 Ves 292: 7 RR 417.]

(5) The promoters of a company for working mines contract that the company, when formed, shall purchase certain mineral property. They take no proper precautions to ascertain the value of such property—and in fact agree to pay an extravagant price therefor. They also stipulate that the vendors shall give them a bonus out of the purchase money. This contract cannot be specifically enforced.

70. *Thakamma Matheu v M. Azamathulla Khan*, 1993 Supp (4) SCC 492: AIR 1993 SC 1120.

71. *M.K. Usman Koya v C.S. Santha*, AIR 2003 Ker 191: (2003) 3 CLT 12.

72. For example, see Illustration to S. 14 of the old Act, cited above. Under cl. (2) performance can be enforced either by the promisor or by the promisee.

73. *Ins. by the Repealing and Amending Act, 1964* (52 of 1964), S. 3 and Sch. II.

74. While cl. (2) relaxes the rule that part of a contract cannot be specifically enforced in favour of both the parties, cl. (3) does so in favour of the party not in default. Party in default is the party who is unable to perform the whole of his part of the contract. The principle underlying cl. (3) is that the party who is not at default is entitled to specific performance of so much of a

(4) When a part of a contract which, taken by itself, can and ought to be specifically performed, stands on a separate and independent footing from another part of the same contract which cannot or ought not to be specifically performed, the court may direct specific performance of the former part.<sup>75</sup>

*Explanation.*—For the purposes of this section, a party to a contract shall be deemed to be unable to perform the whole of his part of it if a portion of its subject-matter existing at the date of the contract has ceased to exist at the time of its performance.<sup>76</sup>

### Specific performance of part of contract [S. 12]

Section 12 deals with specific performance of a part of a contract. It provides in clause (1) that as a general rule, the court shall not grant specific performance of a part of a contract. The section, however, recognises in

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- contract as the other can perform. *Rachakonda Narayana v Ponthala Parvathamma*, (2001) 8 SCC 173, the relief of directing the defendant party to perform specifically so much of his part of the contract as he can perform can be pleaded at the appellate stage also when the fact of the defaulting party's inability to perform a part of the contract comes to the knowledge of the party seeking specific performance.
75. For example, if, at an auction, a person purchases several plots of land, the inability of the vendor to make out good title to one plot will not prevent him from enforcing specific performance of the sale of other plots. *Balkar Singh v Mohabat Singh*, AIR 2004 P&H 340, agreement for sale of defendant's share in property as well as share of his minor son without court permission, enforceable to the extent of defendant's share reducing consideration proportionally.
76. Sub-sections (1), (2), (3), (4) and Explanation of this section correspond with Ss. 17, 14, 15, 16 and 13 of the repealed Specific Relief Act, 1877. That Act carried the following illustrations:

*Illustrations as to sub-section (2).*—(a) A contracts to sell B a piece of land consisting of 100 bighas. It turns out that 98 bighas of the land belong to A, and the two remaining bighas to a stranger, who refuses to part with them. The two bighas are not necessary for the use or enjoyment (of the 98 bighas, nor so important for such use or enjoyment) that the loss of them may not be made good in money. A may be directed at the suit of B to convey to B the 98 bighas and to make compensation to him for not conveying the two remaining bighas; or B may be directed, at the suit of A, to pay to A on receiving the conveyance and possession of the land, the stipulated purchase money, less a sum awarded as compensation for the deficiency. [Based on *Richardson v Smith*, (1870) LR 5 Ch App 648.]

(b) In a contract of the sale and purchase of a house and lands for two lakhs of rupees, it is agreed that part of the furniture should be taken at a valuation. The Court may direct specific performance of the contract notwithstanding that the parties are unable to agree as to the valuation of the furniture, and may either have the furniture valued in the suit and include it in the decree for specific performance, or may confine its decree to the house.

*Illustrations as to sub-section (3).*—(a) A contracts to sell to B a piece of land consisting of 100 bighas. It turns out that 50 bighas of the land belong to A, and the other 50 bighas to a stranger, who refuses to part with them. A cannot obtain a decree against B for the specific performance of the contract; but if B is willing to pay the price agreed upon, and to take the 50 bighas which belong to A, waiving all rights to compensation either for the deficiency or for loss sustained by him through A's neglect or default, B is entitled to a decree directing A to convey those 50 bighas to him on payment of the purchase money.

(b) A contracts to sell to B an estate with a house and a garden for a lakh of rupees. The garden is important for the enjoyment of the house. It turns out that A is unable to convey the garden. A cannot obtain a decree against B for the specific performance of the contract; but if B is willing to pay the price agreed upon, and to take the estate and house without the garden, waiving all rights to compensation either for the deficiency or for loss sustained by him through A's neglect or default, B is entitled to a decree directing A to convey the house to him on payment of the purchase-money.

clauses (2) to (4) certain exceptions to the above rule. Whether specific performance of a part of the contract is to be ordered or not has been wholly left by the section to one deciding factor, namely, the proportion the part which can be performed bears to that which cannot be performed. Where the part which cannot be performed bears only a small proportion to the whole in value and the unperformed part can be compensated adequately in terms of money, the court may order specific performance of one part and compensation for the other.

A slightly different principle comes into play where the part which cannot be performed forms a considerable part of the whole. In such cases the court has first to see whether the major part which has to be left out admits of money compensation or does not do so. If the unperformed portion can be compensated in terms of money the court may order specific performance of the rest, provided that the party seeking relief has paid his consideration under the contract as reduced by the amount of compensation for the unperformed portion. Where the matter does not admit of compensation the court may order specific performance only when the party seeking relief has paid his whole consideration without any reduction whatsoever.

Where the part that would remain unperformed does not admit of compensation in terms of money, the court would order specific performance only if the party seeking performance undertakes to pay the consideration for the whole of the contract without any abatement.

In either situation, the party seeking performance of a part of a contract has to relinquish all claims to the performance of the remaining part and also all rights to compensation either for the deficiency or for any loss or damage sustained through the defendant's default as to performance.

An illustrative account of the working of the principle is to be found in *Rutherford v Acton Adams*.<sup>77</sup>

If a vendor sues and is in a position to convey substantially what the purchaser has contracted to get, the court will decree specific performance with compensation for any small and immaterial deficiency, provided that the vendor has not, by misrepresentation or otherwise, disentitled himself to this remedy. Another possible case arises where a vendor claims specific performance and where the court refuses it unless the purchaser is willing to consent to a decree on the terms that the vendor will make compensation to the purchaser who agrees to such a decree on condition that he is compensated. If it is the purchaser who is suing, the court holds him to have even a larger right. Subject to considerations of hardship, he may elect to take all he can get, and to have a proportionate abatement of the purchase money. But this right applies only to a deficiency in the subject-matter described in the contract.

77. 1915 AC 866 (PC). Where the property came to the share of two brothers jointly and one of them sold the whole to a neighbour, the buyer was allowed to recover only the selling member's share. *Sardar Singh v Krishna Devi*, (1994) 4 SCC 18.

The Specific Relief Act, 1877 (now repealed) carried the following illustration in the corresponding Section 14:

A contracts to sell to B a piece of land consisting of 100 bighas. It turns out that 98 bighas of the land belong to A, and the two remaining bighas to a stranger, who refuses to part with them. The two bighas are not necessary for the use or enjoyment of the 98 bighas, nor so important for such use or enjoyment that the loss of them may not be made good in money. A may be directed at the suit of B to convey to B 98 bighas and to make compensation to him for not conveying the two remaining bighas; or B may be directed, in the suit of A, to pay to A, on receiving the conveyance and possession of the land, the stipulated purchase money less a sum awarded as compensation for the deficiency.<sup>78</sup>

In a contract for the sale and purchase of a house and lands for Rs 2 lakhs, it is agreed that part of the furniture should be taken at a valuation. The court may direct specific performance of the contract notwithstanding the parties are unable to agree as to the valuation of the furniture, and may either have the furniture valued in the suit and include it in the decree for specific performance, or may confine its decree to the house.

Where a contract was incapable of being performed and a party categorically refused to accept part-performance; it was held that there was no readiness and willingness at all stages to accept part-performance. Therefore such a party could not be permitted later to change its position and elect to accept part-performance.<sup>79</sup> The court said:

“In cases where a contract is not capable of being performed in whole then the readiness and willingness, at all stages, is the readiness and willingness to accept part-performance. If a contract is not capable of being performed in whole and a party clearly indicates that he is not willing to accept part-performance, then there is no readiness and willingness, at all stages, to accept part-performance. In that case there can be no specific performance of a part of the contract at a later stage.”<sup>80</sup>

In a case under the J&K Specific Relief Act, 1977 [S. 15] it was held that where a party was unable to perform the whole of his part, the court could direct the performance of so much of his part as he was capable of performing (1/3rd share of the property).<sup>81</sup>

The requirements of the section were stated by the Supreme Court as follows:<sup>82</sup>

“The ingredients which would attract specific performance of the part of the contract under the latter part of sub-section (3) of Section 12 are:

78. Based on *Richardson v Smith*, (1870) LR 5 Ch App 648 and *Arnold v Arnold*, (1880) LR 14 Ch D 270.

79. *Surjit Kaur v Naurata Singh*, (2000) 7 SCC 379: AIR 2000 SC 2927.

80. *Ibid.*

81. *Manzoor Ahmed Magray v Ghulam Hassan Aram*, (1999) 7 SCC 703: AIR 2000 SC 191.

82. *Rachakonda Narayana v Ponthala Parvathamma*, (2001) 8 SCC 173. *Chenguni Othayoth Thankom v Kooloth Balakrishnan Nair*, AIR 2002 Ker 297, reducing the claim to a part of the property at the appellate stage was not material to relief because the plaintiff knew from the very beginning that the document was defective.

(i) if a party to an agreement is unable to perform a part of the contract, he is to be treated as defaulting party to that extent, and (ii) the other party to an agreement must, in a suit for such specific performance, either pay or have paid the whole of the agreed amount, for that part of the contract which is capable of being performed by the defaulting party and also relinquish his claim in respect of the other part of the contract which the defaulting party is not capable of performing and relinquishes the claim of compensation in respect of loss sustained by him. If such ingredients are satisfied, the discretionary relief of specific performance is ordinarily granted unless there is delay or laches or any other disability on the part of the other party.”

*Illustrations as to Explanation.*—(a) A contracts to sell a house to B for a lakh of rupees. The day after the contract is made, the house is destroyed by a cyclone. B may be compelled to perform his part of the contract by paying the purchase-money.

(b) In consideration of a sum of money payable by B, A contracts to grant an annuity to B for B's life. The day after the contract has been made, B is thrown from his house and killed. B's representative may be compelled to pay the purchase-money.

#### Rights of purchaser or lessee where seller's or lessor's title imperfect [S. 13]

**S. 13. Rights of purchaser or lessee against person with no title or imperfect title.**—(1) Where a person contracts to sell or let certain immovable property having no title or only an imperfect title, the purchaser or lessee (subject to the other provisions of this Chapter), has the following rights, namely—

- (a) if the vendor or lessor has subsequently to the contract acquired any interest in the property, the purchaser or lessee may compel him to make good the contract out of such interest;
- (b) where the concurrence of other persons is necessary for validating the title, and they are bound to concur at the request of the vendor or lessor, the purchaser or lessee may compel him to procure such concurrence, and when a conveyance by other persons is necessary to validate the title and they are bound to convey at the request of the vendor or lessor, the purchaser or lessee may compel him to procure such conveyance;
- (c) where the vendor professes to sell unencumbered property, but the property is mortgaged for an amount not exceeding the purchase money and the vendor has in fact only a right to redeem it the purchaser may compel him to redeem the mortgage and to obtain a valid discharge, and, where necessary, also a conveyance from the mortgagee;
- (d) where the vendor or lessor sues for specific performance of the contract and the suit is dismissed on the ground of his want of title or imperfect title, the defendant has a right to a return of his deposit, if any, with

interest thereon, to his costs of the suit, and to a lien for such deposit, interest and costs on the interest, if any, of the vendor or lessor in the property which is the subject-matter of the contract.

(2) The provisions of sub-section (1) shall also apply, as far as may be, to contracts for the sale or hire of movable property.

Section 13 deals with the rights of a purchaser or lessee against a person with no title or imperfect title. The idea underlying this section is that when a person enters into a contract without the power for performing that contract and subsequently he acquires the power of performing the same, he is bound to do so. This section is, however, limited to contracts to sell or let property. This result may not necessarily follow particularly where the purchaser was aware of the lack of title. In this case, the seller was the cultivating tenant of the land in question. The purchaser (plaintiff) from him was very much aware that he had no title. The court said that such purchaser had no right to seek specific enforcement of the agreement to sell. Even subsequent acquisition of title by the seller would not enure to the benefit of such purchaser, because he could not say that he had come with clean hands.<sup>83</sup>

The different clauses of Section 13 affect the remedy of the buyer and the obligation of the seller. The section comes into play when the seller of immovable property has no title or only an imperfect title. If he acquires any interest in the property subsequently, the purchaser can compel him to make good the contract out of such interest. Where concurrence of or conveyance by some other person is necessary to enable the vendor to validate his transfer, and if that person is bound to concur at the direction of the vendor, the purchaser can compel the vendor to procure such concurrence and validate the transfer. Where the vendor purported to sell the property as free from any encumbrance, etc., but the property is in fact subject to a mortgage and, if the amount of the mortgage is equal to the sale price, the buyer may compel the vendor to redeem the mortgage and transfer the property to him free from the mortgage. Where the contract of transfer was subject to the responsibility of the vendor to apply for and to get the agricultural land converted into non-agricultural use and though he had not obtained such permission, the land in question was held to be specifically recoverable from him when, by virtue of an intervening statutory enactment, the vendee was able to get the land converted to his use.<sup>84</sup> Where the vendor sues the buyer for specific performance and the suit is dismissed on the ground of want of title or imperfect title, the vendee would be entitled to refund of his deposit along with interest and also costs and this claim will operate as a charge upon the interest, if any, of the vendor in the property.

83. *S. Kanaka Durga Manikyhumba v Ramapragda Surya Prakasa Rao*, AIR 2010 AP 99.

84. *Rojasara Ramjibhai Dahyabhai v Jani Narottamdas Lallubhai*, (1986) 3 SCC 300: AIR 1986 SC 1912.

*Amendment of plaint for relinquishment of performance of remaining part*

The relinquishment of claim as contemplated under Section 12(3)(a) as regards performance of the remaining part and rights as to compensation need not be specifically pleaded. The sub-section does not lay down any limitation for filing such an application for amendment. It can be filed at any stage of the proceedings and also before the Supreme Court. Delay is immaterial for this purpose.<sup>85</sup>

*Purchaser of share in unpartitioned property*

The case involved sale by two brothers only of their shares in the unpartitioned jointly inherited property. The other co-owners were two sisters who had not joined the sale. The Supreme Court said: "Section 12 of the Specific Relief Act would be of no assistance in the situation obtaining here. In the absence of sisters being parties to the agreement, the vendee can at best obtain the undivided interest of the two brothers in the property. Section 12 cannot be involved by the vendee in the sale of undivided share of the two brothers with a right to force partition on the sisters who were not parties to the agreement of sale. Such a relief cannot be obtained under Section 12 by a vendee on purchase of an undivided share in the property of some of the co-owners against other co-owners who were not parties to the sale."<sup>86</sup>

The defendant was the owner of 3/4th undivided share in the property. The court said that even such share could be sold. His property was identified by a specific share. The plaintiff was ready to pay the full price. A decree for specific recovery of such share could be passed.<sup>87</sup>

**Specific performance of part of contract**

The whole of the property belonging to the joint owners was contracted to be sold. One of them was a minor whose share was to be transferred on obtaining court permission. Such permission could not be obtained. The vendee claimed specific performance of that part of the property which belonged to the adult joint-owners. It was held that since they could transfer their shares in the property and they being owners of definite shares and no court permission being necessary for that purpose, the decree was granted. The contract was not of contingent nature. It was nowhere provided that

85. *Surinder Singh v Kapoor Singh*, (2005) 5 SCC 142. The claimant has to pay only a proportional part of the consideration. The promise in this case was for sale of property of the seller and his sister. He could not persuade the sister. Specific recovery of his part was allowed. *Jeet Singh v Daulat Ram*, AIR 2012 P&H 3, the vendor was not able to perform the contract to the full extent because 3/4th of the property had already been decreed in favour of co-sharers, the vendee was willing to pay full price even for getting 1/4. This was allowed. He could relinquish a part of his claim at any stage of proceeding.

86. *Shanmugasundaram v Diravia Nadar*, (2005) 10 SCC 728: AIR 2005 SC 1836.

87. *Gopal Ramvilas Gattani v Sheshrao Pundlik Hivarkar*, AIR 2009 NOC 1366 (Bom).

the contract was to become void or unenforceable on the failure of the court permission.<sup>88</sup>

**S. 14. Contracts not specifically enforceable.**—(1) The following contracts cannot be specifically enforced, namely—

- (a) a contract for the non-performance of which compensation in money is an adequate relief;
  - (b) a contract which runs into such minute or numerous details or which is so dependent on the personal qualifications or volition of the parties, or otherwise from its nature is such, that the court cannot enforce specific performance of its material terms;
  - (c) a contract which is in its nature determinable;
  - (d) a contract the performance of which involves the performance of a continuous duty which the court cannot supervise.
- (2) Save as provided by the Arbitration Act, 1940, no contract to refer present or future differences to arbitration shall be specifically enforced; but if any person who has made such a contract (other than an arbitration agreement to which the provisions of the said Act apply) and has refused to perform it sues in respect of any subject which he has contracted to refer, the existence of such contract shall bar the suit.

(3) Notwithstanding anything contained in clause (a) or clause (c) or clause (d) of sub-section (1), the court may enforce specific performance in the following cases—

- (a) where the suit is for the enforcement of a contract,—
  - (i) to execute a mortgage or furnish any other security for securing the repayment of any loan which the borrower is not willing to repay at once:  
Provided that where only a part of the loan has been advanced the lender is willing to advance the remaining part of the loan in terms of the contract; or
  - (ii) to take up and pay for any debentures of a company;
- (b) where the suit is for—
  - (i) the execution of a formal deed of partnership, the parties having commenced to carry on the business of the partnership; or
  - (ii) the purchase of a share of a partner in a firm;
- (c) where the suit is for enforcement of contract for the construction of any building or the execution of any other work on land:  
Provided that the following conditions are fulfilled, namely:—
  - (i) the building or other work is described in the contract in terms sufficiently precise to enable the court to determine the exact nature of the building or work;

88. *P.C. Varghese v Devaki Amma Balambika Devi*, (2005) 8 SCC 486. *Kammana Sambamurthy v Kalipatnapu Atchutamma*, (2011) 11 SCC 153: AIR 2011 SC 103, the husband transferred the whole of the property, it turned out that half of the property belonged to his wife and she did not consent to the transfer. Specific performance was ordered against the share of the husband only.

- (ii) the plaintiff has a substantial interest in the performance of the contract and the interest is of such a nature that compensation in money for non-performance of the contract is not an adequate relief; and
- (iii) the defendant has, in pursuance of the contract, obtained possession of the whole or any part of the land on which the building is to be constructed or other work is to be executed.<sup>89</sup>

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89. Illustrations in preceding 1877 Act. The section is based on S. 21(a), (b), (d) and (g) of the repealed Specific Relief Act, 1877. That Act carried the following illustrations:

*Illustrations as to sub-section (1)(a).*—A contracts to sell, and B contracts to buy, a lakh of rupees in the four per cent loan of the Central Government;

A contracts to sell, and B contracts to buy, 40 chests of indigo at Rs 1000 per chest;

In consideration of certain property having been transferred by A to B, B contracts to open a credit in A's favour to the extent of Rs 10,000, and to honour A's drafts to that amount.

The above contracts cannot be specifically enforced, for in the first and the second both A and B, and in the third A, would be reimbursed by compensation in money.

*Illustrations as to sub-section (1)(b).*—A contracts to render personal service to B:

A contracts to employ B on personal service:

A, an author, contracts with B, a publisher, to complete a literary work.

B cannot enforce specific performance of these contracts.

A contracts to buy B's business at the amount of a valuation to be made by two valuers, one to be named by A and the other by B. A and B each name a valuer, but before the valuation is made, A instructs his valuer not to proceed;

By a charter-party entered into in Calcutta between A, the owner of a ship, and B, the charterer, it is agreed that the ship shall proceed to Rangoon, and there load a cargo of rice, and thence proceed to London, freight to be paid, one-third on arrival at Rangoon, and two-thirds on delivery of the cargo in London;

A lets land to B and B contracts to cultivate it in a particular manner for three years next after the date of the lease;

A and B contract that, in consideration of annual advances to be made by A, B will for three years next after the date of the contract grow particular crops on the land in his possession and deliver them to A when cut and ready for delivery;

A contracts with B that, in consideration of Rs 1000 to be paid to him by B, he will paint a picture for B;

A contracts with B to execute certain works which the Court cannot superintend;

A contracts to supply B with all the goods of a certain class which B may require;

A contracts with B to take from B a lease of a certain house for a specified term, at a specified rent, "if the drawing-room is handsomely decorated", even if it is held to have so much certainty that compensation can be recovered for its breach;

A contracts to marry B.

The above contracts cannot be specifically enforced.

*Illustration as to sub-section (1)(c).*—A and B contract to become partners in a certain business, the contract not specifying the duration of the proposed partnership. This contract cannot be specifically performed, for, if it were so performed, either A or B might at once dissolve the partnership. [Based on *Scott v Rayment*, (1868) LR 7 Eq 112].

*Illustration as to sub-section (1)(d).*—A contracts to let for twenty-one years to B the right to use such part of a certain railway made by A as was upon B's land, and that B should have a right of running carriages over the whole line on certain terms, and might require A to supply the necessary engine-power, and that A should during the term keep the whole railway in good repair. Specific performance of this contract must be refused to B.

### Contracts which cannot be specifically enforced

The effect of the provisions in Section 14 can be stated in terms of certain propositions, namely, that in the case of the following contracts the relief of specific performance cannot be allowed:

#### 1. Where compensation is adequate [S. 14(1)(a)]

Courts will not order specific performance of a contract where the aggrieved party can be adequately compensated in terms of money. An ordinary contract to lend or borrow money whether with or without security is an example of a contract which cannot be specifically enforced, though where a loan has been already advanced on the understanding that a security would be provided against it, this can be specifically enforced.<sup>90</sup>

#### 2. Contracts involving personal skill [S. 14(1)(b)]

It is not possible for the court to supervise the performance of a contract which runs into minute and numerous details or is dependent upon the personal qualifications of the promisor or is otherwise of volitional nature. Contracts of employment, contracts of personal service, contracts involving performance of artistic skill, like contracts to sing, to paint, to act, contracts of authorship, are ordinary examples of things requiring personal skill and, therefore, beyond the capacity of the judicial process to enforce their actual performance. The only choice in such cases is to be content with damages.<sup>91</sup> An employer may not be compellable to keep an employee in accordance with a contract of employment, but the position will be different where an employee has been removed, for, in that case, if the removal is wrongful, the employee can be reinstated. The Supreme Court, however, did not approve of an arbitrator's award reinstating a professor removed by the Delhi University.<sup>92</sup> A contract to publish a piece of music and a contract to build a house<sup>93</sup> have been specifically enforced because both are purely mechanical functions. It is observed in CHITTY ON CONTRACTS:<sup>94</sup>

90. S. 14(3). *Meenakshisundara Mudaliar v Rathnasami Pillai*, ILR (1918) 41 Mad 959.

91. *Gunput Narain Singh, re*, ILR (1875-78) 1 Cal 74, contract of marriage; *Bansi Sah v Krishna Chandra*, AIR 1951 Pat 508, a lease carrying personal covenants for repair.

92. *S. Dutt (Dr) v University of Delhi*, AIR 1958 SC 1050: 1959 SCR 236. *Pearlite Liners (P) Ltd v Manorma Sirsi*, (2004) 3 SCC 172: AIR 2004 SC 1373, private employment, oral appointment, the employee did not comply with order of transfer and sought declaration that the transfer was illegal, that her service and benefits must be maintained, and that the employer should be restrained from holding inquiry against her. The court said that such a relief, if granted, would amount to enforcing a contract of personal service, which is not possible under the law. *Shiv Kumar Tiwari v Jagat Narain Rai*, (2001) 10 SCC 11: AIR 2002 SC 211, a declaration given by a civil court that the person in question was a permanent lecturer is the college, no binding efficacy set aside.

93. *Barrow v Chappell & Co*, (1951) 62 The Autor 38 (unrep) cited in *Joseph v National Magazine Co*, 1959 Ch 14: (1958) 3 WLR 366, cited in CHITTY ON CONTRACTS (Vol 1, 24th Edn, 1977) 1645.

94. *Ibid* at p. 1646.

“But specific performance of a contract to build can be decreed if (i) the work is precisely defined; (ii) damages will not adequately compensate the plaintiff; and (iii) the defendant is in possession of the land on which the work is to be done so that the plaintiff cannot get the work done by another builder.”

*Clauses of uncertain nature.*—The suit was for specific performance of the agreement of renewal of lease. There was a concurrent finding of the court below that the option of renewal was exercised against the terms of the renewal clause. The clause required fixation of the terms and conditions of renewal and also its period under mutual agreement or alternatively through the village *Mukhiya* or *Panchas*. Such persons were not named in the agreement. The lessee served legal notice of renewal without fulfilling the requirement of initial mutual assent. The relief of renewal was not allowed to the lessee.<sup>95</sup>

*Contracts involving personal, confidential and fiduciary service.*—The specific performance of a contract for personal, confidential and fiduciary service dependent on mutual trust, faith and confidence has been held to be barred under Section 14(1)(a), (b) & (d).<sup>96</sup>

### 3. Contracts of determinable nature [S. 14(1)(c)]

Specific performance is not ordered of a contract which is in its nature determinable. An illustration appearing under the corresponding provision in the repealed Act of 1877 sufficiently explains this point:

A and B contract to become partners in a certain business, the contract did not specify the duration of the proposed partnership. The contract cannot be specifically performed, for, if it were so performed, either A or B might at once dissolve the partnership.<sup>97</sup>

Similarly, no order of specific performance is likely to be passed when the contract is revocable at the option of the opposite party. A revocable lease is in this category.<sup>98</sup> But a tenancy from year to year, determinable by either party by half a year's notice to quit, is specifically enforceable.<sup>99</sup>

A contract of employment is not specifically enforceable. A person who was selected was not allowed to get the position to which he was selected. The court observed: “Courts do not ordinarily enforce performance of contracts of a personal character, such as a contract of employment. The

95. *Shanti Prasad Devi v Shankar Mahto*, (2005) 5 SCC 543: AIR 2005 SC 2905.

96. *Percept D'Mark (India) (P) Ltd v Zaheer Khan*, (2006) 4 SCC 227.

97. Based on *Scott v Rayment*, (1868) LR 7 Eq 112, otherwise where the agreement is for a definite term, *England v Curling*, (1844) 8 Beav 129: 68 RR 39.

98. *Lewis v Bond*, (1853) 52 ER 34: 18 Beav 85. *ONGC Ltd v Streamline Shipping Co (P) Ltd*, AIR 2002 Bom 420, a contract of hiring vessels for three years with the right reserved in the hirer to terminate it after one year, the court said that the hirer could not be prevented from exercising this right.

99. *Lever v Koffler*, (1901) 1 Ch 543.

remedy is to sue for damages. The grant of specific performance is purely discretionary and must be refused when not warranted by the ends of justice. Such relief can be granted only on sound legal principles. In the absence of any statutory requirement, courts do not ordinarily force an employer to recruit or retain in service an employee not required by the employer. There are, of course, certain exceptions to this rule, such as in the case of a public servant dismissed from service in contravention of Article 311 of the Constitution; reinstatement of a dismissed worker under the Industrial Law; a statutory body acting in breach of statutory obligations, and the like. The facts of this case do not fall within the exceptions. Therefore, the plaintiff's suit for mandatory injunction, on the facts of the case, was rightly dismissed by the trial court and wrongly decreed by the first appellate court and the High Court.”<sup>100</sup>

A distributorship was held to be determinable in nature. An order could not be passed for its restoration.<sup>101</sup> Where the plaintiff claimed that an agreement in his favour to run a restaurant was illegally terminated, the court said that the contract not being, specifically enforceable an interim injunction to restrain the termination could not be granted.<sup>102</sup> The licence to run the petrol pump was terminated. The licence was granted under a revocable agreement. The court said that the only remedy for the licensee was to sue for damages and not for enforcement of the agreement. The suit as filed was liable to be rejected.<sup>103</sup>

#### 4. Contract requiring constant supervision [S. 14(1)(d)]

Clause (d) of Section 14(1) says that a contract cannot be specifically enforced where it involves the performance of a continuous duty which the court cannot supervise.

For this reason courts have refused specifically to enforce an undertaking by the lessor of a service flat to have a porter “constantly in attendance”,<sup>104</sup> a tenant’s undertaking to cultivate a farm in a particular manner;<sup>105</sup> the obligation of a railway company to operate signals and to provide engine

100. *Nandganj Sihori Sugar Co Ltd v Badri Nath Dixit*, (1991) 3 SCC 54: AIR 1991 SC 1525. *M.K. Usman Koya v C.S. Santha*, AIR 2003 Ker 191: (2003) 3 CLT 12, in a pending eviction proceeding, the landlord entered into an agreement with the tenant that even if a decree of eviction was passed, it would not be enforced and the parties would enter into a fresh tenancy agreement. Even so, the tenant did not pay rent for 14 years and also did not pay the premium amount. It was also not clear what would be the terms of the new rent deed. Thus the tenant was not performing his part of the contract. He was not able to get an order from the court directing the landlord to execute the deed.

101. *Indian Oil Corp v Amritsar Gas Service*, (1991) 1 SCC 533.

102. *Vidya Securities Ltd v Comfort Living Hotels (P) Ltd*, AIR 2003 Del 214. *Bharat Petroleum Corp v Rajesh Sharma*, AIR 2015 NOC 881 (All), a dealership agreement was held to be of determinable nature. No injunction could be granted against determination of such agreement.

103. *Bharat Petroleum Corp v Khaybar Transport (P) Ltd*, AIR 2011 All 131.

104. *Ryan v Mutual Tontine Westminster Chambers Assn*, (1893) 1 Ch 116 (CA).

105. *Rayner v Stone*, (1762) 2 Edn 128: 28 ER 845; *Phipps v Jackson*, (1887) 56 LJ Ch 550.

power;<sup>106</sup> a contract to keep an airfield in operation;<sup>107</sup> the obligation of a shipowner under a charter party<sup>108</sup> and a contract to deliver goods by instalments.<sup>109</sup>

Where a tenant vacated a site for purposes of reconstruction under an understanding that a portion of the building would be reallocated to him, the court held that the landlord was bound to provide the premises as promised.<sup>110</sup>

Sub-section (3) qualifies to a certain extent the operation of the clauses dealing with situations where compensation is an adequate relief and where the contract is unilaterally revocable. It says that an agreement to provide a security or to execute a mortgage against a loan which has already been provided is specifically enforceable, if the borrower is not willing to pay back the loan at once. Where the lender has advanced only a part of the loan, he can claim specific relief only when he is ready and willing to advance the remaining part of the loan also. An agreement to take up, and pay for, the debentures of a company is also specifically enforceable. Agreements to execute a formal deed of partnership where the partners have already commenced business and to purchase the share of a partner in a firm are also specifically enforceable.

#### *Construction contracts [S. 14(3)(c)]*

As for agreements for the construction of a building, the principles crystallised in English law have been adopted by sub-section (3)(c). The agreement will be enforceable if the nature of the building is of exact nature, the plaintiff has a substantial interest in the work and the work is also of such nature that it cannot be compensated for in terms of money and the defendant is in possession of the whole or a part of the site.

In a case before the Supreme Court,<sup>111</sup> the Authority which had to supervise the performance of the contract had ceased to exist. The Court said: "There is also force in the contention that the agreement is not specifically enforceable in view of clause (d) of sub-section (1) of Section 14 of the Specific Relief Act, 1963. This provision provides that a contract, the performance of which involves the performance of a continuous duty which the court cannot supervise, is not specifically enforceable. Having regard to the nature of the Scheme and the facts and circumstances of the case, it is clear that the performance of the contract involves continuous supervision which is not possible for the court. After repeal, such continuous supervision cannot be

106. *Powell Duffryn Steam Coal Co v Taff Vale Rly Co*, (1874) LR 9 Ch App 331.

107. *Dowty Boulton Paul Ltd v Wolverhampton Corp*, (1971) 1 WLR 204.

108. *De Mattos v Gibson*, (1858) 4 D&J 276: 124 RR 250.

109. *Dominion Coal Co v Dominion Iron & Steel Co*, 1919 AC 293.

110. *K.M. Jaina Beevi v M.K. Govindaswami*, AIR 1967 Mad 369.

111. *Her Highness Maharani Shantidevi P. Gaikwad v Savjibhai Haribhai Patel*, (2001) 5 SCC 101: AIR 2001 SC 1462.

directed to be undertaken by the competent authority as such an authority is now non-existent.”

Where the contract involved a project of public interest and the plaintiff was not able to prove any *prima facie* case in his favour and his loss was also ascertainable in monetary terms, the court refused to grant an injunction restraining the execution of a public project.<sup>112</sup>

### Arbitration

Section 14 provides in sub-section (2) that, except as provided by the Arbitration Act, 1940, (now Arbitration and Conciliation Act, 1996) a contract to refer a present or future dispute to arbitration shall not be specifically enforced. An arbitration agreement operates as a bar to the filing of a suit.

### Lack of free consent and situation of no contract

Where the plea that the sale deed was executed under distress was not taken by the vendor in his written statement and this being a question of fact, it was not allowed to be raised for the first time in second appeal. The court found the sale agreement to be genuine and also supported by lawful consideration. The plea raised at this stage that the decree, if passed, would cause hardship to him, was not entertained.<sup>113</sup>

An agreement which was not signed by the vendee and was signed only by the vendor was held to be a concluded contract. The court said that what was necessary for enforceability was *consensus ad idem*. Suit for specific performance can be maintained even on the strength of an oral agreement.<sup>114</sup>

A trust was created by a lady. Under the trust deed, two trustees were appointed who were to act jointly. Yet the lady herself acted as a trustee and entered into an agreement of sale on behalf of the trust. Thus, the agreement was made in breach of the trust and in excess of the powers of individual trustee. The buyer could not seek specific enforcement.<sup>115</sup>

### Family settlement

An agreement for transfer of property which was found to be a part of the settlement was held to be not bereft of consideration. The settlement is a consideration in itself. The deed of settlement was produced. It carried the provision for the transfer in question. The court held that it could not be said that the settlement had not been proved. The decree of specific performance was passed.<sup>116</sup>

112. *Envision Engg v Sachin Infa Enviro Ltd*, AIR 2003 Guj 164.

113. *Ammisetti Chandram v Chodasani Suryanarayana*, AIR 2003 AP 269. *Terai Tea Co Ltd v Nathmal Kedia*, AIR 2012 Cal 43, a situation of no contract. Even an oral agreement was not proved.

114. *Mohd Abdul Hakeem v Naiyaz Ahmad*, (2004) 3 CLT 137 (AP).

115. *Sachchidananda Banerjee v Moly Gupta*, AIR 2015 NOC 552 (Cal).

116. *Kanigolla Lakshamana Rao v Gudimetla Ratna Manikyamba*, AIR 2003 AP 241.

**S. 15. Who may obtain specific performance.**—Except as otherwise provided by this Chapter, the specific performance of a contract may be obtained by—

- (a) any party thereto;
- (b) the representative-in-interest or the principal, of any party thereto:

Provided that where the learning, skill, solvency or any personal quality of such party is a material ingredient in the contract, or where the contract provides that his interest shall not be assigned, his representative-in-interest or his principal shall not be entitled to specific performance of the contract, unless such party has already performed his part of the contract, or the performance thereof by his representative-in-interest, or his principal, has been accepted by the other party;

- (c) where the contract is a settlement on marriage, or a compromise of doubtful rights between the members of the same family, any person beneficially entitled thereunder;
- (d) where the contract has been entered into by a tenant for life in due exercise of a power, the remainderman;
- (e) a reversioner in possession, where the agreement is a covenant entered into with his predecessor-in-title and the reversioner is entitled to the benefit of such covenant;
- (f) a reversioner in remainder, where the agreement is such a covenant, and the reversioner is entitled to the benefit thereof and will sustain material injury by reason of its breach;
- (g) when a company has entered into a contract and subsequently becomes amalgamated with another company, the new company which arises out of the amalgamation;
- (h) when the promoters of a company have, before its incorporation, entered into a contract for the purposes of the company, and such contract is warranted by the terms of the incorporation, the company:

Provided that the company has accepted the contract and has communicated such acceptance to the other party to the contract.

#### Persons for or against whom contracts may be specifically enforced [S. 15]

##### *Assignee from legal heir*

The expression “representative-in-interest” includes the assignee of a right to purchase the property and, therefore, he would have the title to claim specific performance.<sup>117</sup> The deed of assignment of a decree for specific

117. *T.M. Balakrishna Mudaliar v M. Satyanarayana Rao*, (1993) 2 SCC 740: AIR 1993 SC 2449; *Khiria Devi v Rameshwar Sao*, 1992 Supp (2) SCC 1: AIR 1992 SC 1482, suit for reconveyance. *Ashok Kumar J. Pandya v Suyog Coop Housing Society Ltd*, AIR 2003 NOC 118 (Guj): 2002 AIHC 3401, a clause in the agreement to sell subject to the condition that in case of rejection by the Government under Ceilings Act, the agreement would be treated as cancelled. Specific enforcement was not allowed when the agreement became cancelled by reason of the Government refusal. *Raghuvir Singh Bhatty v Ram Chandra Waman*

performance does not create any right, title or interest in immovable property in favour of the assignee. Hence, such deed does not require any compulsory registration. The decree in this case was assigned in favour of one of the plaintiffs. The assignee being representative in interest as defined in Section 15(b) was entitled to seek enforcement of the decree under Order 21, Rule 16, CPC. The assignment in question was that of a decree for specific performance of an agreement to sell. The court said that no consideration was required to be shown for such assignment.<sup>118</sup>

#### *Lease or sale in favour of company before incorporation*

Where a lease was granted in favour of a company before its incorporation and the promoters of the company, instead formed only a partnership, it was held that such partnership firm could not claim any rights or interest under clause (b) in the property. The lease deed was signed only by the lessor. The transaction was ineffective even otherwise.<sup>119</sup>

The promoters of an unincorporated company purchased certain property for the purposes of the company. Clause (b) provides that such transaction can be enforced by the company after incorporation provided that it has accepted the contract and communicated its acceptance to the other party. In this case, after its incorporation, the company filed a suit against the seller for a declaration that the company was the owner of the property. The court said that this amounted to an acceptance of the contract and communication to the other party. On the facts, however, the company could not get the relief of recovery of property because there was undesirable conduct of frivolous litigation on the part of both parties. The company was allowed compensation and refund of the earnest money with 12 per cent interest.<sup>120</sup>

#### *All buyers or contractees must join*

In order to obtain the relief of specific performance, all co-contractees must be before the court but all of them need not be on the same side. Others can be joined as co-defendants. Where there is a single indivisible contract to convey land to several persons, some of them only cannot seek specific performance if the others do not want it.<sup>121</sup>

**S. 16. Personal bars to relief.**—Specific performance of a contract cannot be enforced in favour of a person—

- (a) who would not be entitled to recover compensation for its breach;
- (b) who has become incapable of performing, or violates any essential term of, the contract that on his part remains to be performed, or acts in fraud

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*Subhedar*, AIR 2002 All 13, refusal of permission by ceiling Authority, repeal of Ceilings Act, legal hurdle removed, decree of specific performance could be passed. The purchaser had caused delay in applying for permission. Prices escalated in the meantime. Decree of specific performance not allowed.

118. *Amol v Deorao*, AIR 2011 NOC 215 (Bom).

119. *Murari Ganguli v Kanailal Garai*, AIR 2003 Cal 105.

120. *Jai Narain Parasrampuria v Pushpa Devi Saraf*, (2006) 7 SCC 756.

121. *Mukesh Kumar v Col Harbans Waraich*, (1999) 9 SCC 380: AIR 2000 SC 172.

of the contract, or wilfully acts at variance with, or in subversion of, the relation intended to be established by the contract; or

- (c) who fails to aver and prove that he has performed or has always been ready and willing to perform the essential terms of the contract which are to be performed by him, other than terms the performance of which has been prevented or waived by the defendant.

*Explanation.*—For the purposes of clause (c),—

- (i) where a contract involves the payment of money, it is not essential for the plaintiff to actually tender to the defendant or to deposit in court any money except when so directed by the court;
- (ii) the plaintiff must aver performance of, or readiness and willingness to perform, the contract according to its true construction.

#### Persons not entitled to relief of specific performance

The relief of specific performance cannot be awarded in favour of the following persons:

1. A person cannot seek specific performance where the circumstances are such that he would not have been entitled to compensation for breach of contract.
2. A person who is guilty of any of the following cannot claim specific performance:
  - (a) he has become incapable of performing his part of the contract;
  - (b) he has violated any essential term of the contract that on his part remained to be performed;
  - (c) he has acted in fraud of the contract;
  - (d) he has wilfully acted at variance with or in subversion of the relation intended to be established by the contract.
3. A person who has failed to aver and prove that he has performed or has always been ready and willing to perform the essential terms of the contract which were to be performed by him except those terms which he has been prevented from performing by the other party or the performance of which the other party has waived.

Where the contract involves payment of money, it is not essential for the plaintiff to actually tender to the other party or to deposit in court any money except when so directed by the court. Performance must be offered according to the true construction of the contract.

Before acting under Order 8, Rule 10 of the Civil Procedure Code, the court in a suit for specific performance has to scrutinise the facts set out in the plaint to find out whether all the requirements, in particular those indicated in Section 16 of the Specific Relief Act regarding readiness and willingness, have been complied with or not.<sup>122</sup> There has also to be a finding that all the requirements of an enforceable agreement are there. The Supreme

122. *Syed Dastagir v T.R. Gopalakrishna Setty*, (1999) 6 SCC 337: AIR 1999 SC 3029. The court followed *R.C. Chandiok v Chuni Lal Sabharwal*, (1970) 3 SCC 140. *S. Kaladevi v V.R.*

Court has observed that decreeing a suit for specific performance only on the basis of a finding that the agreement was genuine, is not proper. Several other aspects like readiness and willingness have also to be considered.<sup>123</sup>

*Ready and willing [Cl. (c)]*

Explanation II makes it necessary for a party claiming specific performance to aver and prove that he has been all the time ready and willing to perform his part of the contract.<sup>124</sup> Continuous readiness and willingness to perform his part of the contract on the part of the plaintiff is a condition precedent for the grant of the relief. Where the plaintiff was found to be

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Somasundaram, (2010) 5 SCC 401: AIR 2010 SC 1654, an unregistered sale deed is admissible in evidence of the contract of sale for order of specific performance.

123. *Dheeraj Developers (P) Ltd v Om Prakash Gupta*, 2016 SCC OnLine SC 192: (2016) 116 ALR 484.

124. *Gajanan Jaikishan Joshi v Prabhakar Mohanlal Kalwar*, (1990) 1 SCC 166; *Sukhbir Singh v Brij Pal*, (1997) 2 SCC 200: AIR 1996 SC 2510, the fact that the party was present in the Sub-Registrar's office with necessary funds was held to be a proof of the party's readiness and willingness. The plea that the vendee did not show readiness and willingness can be taken by vendor only and not by the subsequent buyer. *Jugraj Singh v Labh Singh*, (1995) 2 SCC 31: AIR 1995 SC 945. *Sri Brabhadambal Agency v Ramasamy*, AIR 2002 Mad 352, time not specified to be of the essence, the buyer ready and willing, bank balance is irrelevant factor, suit within limitation. Specific relief allowed. *Dularo Devi v Asturna Devi*, AIR 2012 Pat 16, purchaser ready and willing to pay the balance money after chakbandi proved, allowed relief. *M.K. Makbool Khan v Shamsunisa*, AIR 2002 NOC 87 (Kant), the tenant who purchased the premises was deducting expenditure made on repair and also for payment of taxes, the court said that this showed that he had no intention to pay the full agreed price. Specific relief was not allowed to him. *Valliamal v Angammal*, AIR 2002 Mad 292, the vendee was supposed to pay the price by redeeming the mortgages to which the property was subject, but he did not do so as a result of which the vendor had to sell some other property to pay off the bank. This showed that the vendee was not willing to do his part. *Ceean International (P) Ltd v Ashok Surana*, AIR 2003 Cal 263, the property under sale was mortgaged to the LIC, the agreement stipulated that the plaintiff was to take the property in "as it is" state, but he made it clear that he was not going to take the property until a good and a marketable title was made out. The court said that he could not seek enforcement. He was not ready and willing to take the property as it was. Time was also of the essence which the plaintiff did not keep. *Dutta Seethamalakshmamma v Yanamadala Balaramaiah*, AIR 2003 AP 430, the vendee made part payment and that too after expiry of the stipulated period, vendor cancelled the agreement, the vendee kept silent and filed a suit after a long period. His suit was rejected. He showed no credentials of either *bona fides* or willingness. *Sardar Joginder Singh v Vasandran Kakani*, AIR 2003 NOC 340 (Ori), the purchaser doubting seller's title, he also admitted that he had no sufficient money with him on the appointed date to seeking execution of sale deed, not ready and willing. He had to pay interest on daily basis on default. Interest not paid. Provision showed that time was considered to be important. Failure to keep time-bound commitments debarred the plaintiff-buyer from specific relief. *N. Satyanarayana v Vedprakash Dusaj*, (2003) 3 ALD 884, only small amount paid, no evidence that the buyer was ready and willing to pay the substantial balance amount, specific relief not allowed. The agreement was for sale of leasehold interest in immovable property, price rise in *pendente lite* period, not relevant to relief. The contract was cancelled by notice. Suit filed three years after that. Art. 54, Limitation Act applied suit barred. *T. Mohan v Kannammal*, (2002) 10 SCC 82, the vendor parted with possession in favour of the purchaser even before the expiry of the period, the requirement of being ready and willing lost its significance. The finding of the High Court was held to be justified that the purchaser had satisfied the legal requirement of being ready and willing.

dabbling in real estate transactions without means to purchase the property and failed to pay the consideration money within the time given to him by the trial court, it was held that he was not ready and willing to perform his part.<sup>125</sup> Where a contract for sale of a house stipulated making of part-payment of purchase price within a specified period so as to enable the owner who was residing in the house to purchase a suitable residence by utilising the amount, it was held that the part-payment must be made within a reasonable time and failure to do so would seriously affect the proposed vendor's right to acquire an accommodation and show that the proposed vendee was not ready and willing to perform his part of the contract. The court said that the grant of a decree for specific performance in the circumstances would amount to an instrument of oppression giving an unfair advantage to the proposed vendee which the court should take care to avoid.<sup>126</sup>

In a suit, for specific performance of a contract for sale of land, the readiness and willingness of plaintiff to perform his part of the contract is to be ascertained from his conduct and attending circumstances. Where the plaintiff neither had sufficient funds to pay the consideration amount nor was he acting promptly within the stipulated time where time was the essence of the contract, it was held that he was neither ready nor willing to perform his part of the contract. Hence he was not entitled to a decree for specific performance of the contract.<sup>127</sup> The making of a conditional offer for payment of the stipulated amount does not fulfil the requirement of law contained in Forms 47 and 48 of Appendix A to the Civil Procedure Code.<sup>128</sup> Depositing of any amount in the court at the appellate stage would not meet the requirement of Section 16(c).<sup>129</sup> Where the land under sale was mortgaged to the bank and the buyer had agreed to pay back the loan and redeem the mortgage but he did nothing in that direction nor showed any inclination to do so, rather he was appropriating the usufruct of the land to himself, the Supreme Court held that he was not ready and willing to perform his part.<sup>130</sup> Where the vendee sent a legal notice rescinding the contract and filed a suit for refund of advance paid and that was decreed by the trial court, his application for revision and for specific performance was dismissed. The court said that it would not lie in his mouth to say that he was ready and

125. *N.P. Thirugnanam v R. Jagan Mohan Rao*, (1995) 5 SCC 115.

126. *P.R. Deb and Associates v Sunanda Roy*, (1996) 4 SCC 423: AIR 1996 SC 1504. *Raj Kishore v Prem Singh*, AIR 2011 SC 382, averment as to readiness and willingness is mandatory in a suit for specific performance.

127. *Acharya Swami Ganesh Dassji v Sita Ram Thappar*, (1996) 4 SCC 526: AIR 1996 SC 2095.

128. *Umabai v Nilkanth Dhondiba Chavan*, (2005) 6 SCC 243: (2005) Mah LJ 306, the mere statement in the plaint or in the written statement of being ready and willing is not sufficient. The entire set of attending circumstances has to be examined to ascertain the real position. The onus as to this lies on the plaintiff even though not required by the defendant to do so.

129. *Ibid*. Raising of the plea of specific performance of the contract for reconveyance and the alternative plea of cancellation of the debt or a decree for accounting, inconsistent, not permissible.

130. *R.K. Parvatharaj Gupta v K.C. Jayadeva Reddy*, (2006) 2 SCC 428: (2006) 3 Mah LJ 1.

willing to go ahead with performance from his side.<sup>131</sup> Where the purchaser clearly averred his readiness and willingness to perform, the court said that it was not necessary for him to show his possession of money to the court. The court found that the transferor was trying to scuttle the sale in favour of the transferee. He executed a sale in favour of his relative for a lesser amount who knew of the earlier sale. Grant of relief of specific performance to the first purchaser was held to be proper.<sup>132</sup>

A person who makes himself a party to an illegal contract cannot enforce his rights under this section.<sup>133</sup>

Where one of the terms of an agreement for sale was that the appellants would withdraw their suit for specific performance and the suit was not withdrawn, it was held that the appellants-plaintiffs could not be said to be ready and willing to perform their part of the agreement. The finding in the impugned judgment that the condition regarding withdrawal of the suit was a condition precedent, was also correct. As the appellants did not withdraw the suit they could not be said to be ready and willing to perform their part of the agreement. For this reason also the claim for specific performance could not have been enforced.<sup>134</sup>

Averment as to readiness and willingness in a plaint has been held to be sufficient if the plaint, read as a whole, clearly indicates that the plaintiff was always and is still ready and willing to fulfil his part of the obligations. Such averment is not a mathematical formula capable of being expressed only in certain specific words or terms.<sup>135</sup> The court said: "An averment of readiness and willingness in the plaint is not a mathematical formula which should only be in specific words. If the averments in the plaint as a whole

131. *Pukhraj D Jain v G. Gopalakrishna*, (2004) 7 SCC 251: AIR 2004 SC 3504. *Pemmada Prabhakar v Youngmen's Vysya Assn*, (2015) 5 SCC 355: (2015) 3 SCC (Civ) 56, a vendee who defaulted in payment of instalments of price for the land under sale was not allowed to claim specific performance. The whole property purchased from some of the sharers only, not enforceable.

132. *Usha v Sukhdev Singh*, AIR 2015 NOC 338 (P&H).

133. *I.T.C. Ltd v George Joseph Fernandes*, (1989) 2 SCC 1: AIR 1989 SC 839.

134. *Bishandayal & Sons v State of Orissa*, (2001) 1 SCC 555: AIR 2001 SC 544; *Syed Dastagir v T.R. Gopalakrishna Setty*, (1999) 6 SCC 337: AIR 1999 SC 3029, deposit of money in court without court order cannot go against the person seeking relief. *Vijay Bhadur and Champalal v Surendra Kumar*, AIR 2003 MP 117, there was no pleading in the plaint that the purchaser had sufficient funds with him or was having the capacity to pay the sale price. He sent his notice to the seller after one year and nine months from the date of the agreement. There was also variance between pleading and proof. The court said that the purchaser had not proved his willingness.

135. *Motilal Jain v Ramdasi Devi*, (2000) 6 SCC 420: AIR 2000 SC 2408; *Ajai Singh v Tulsi Devi*, (2000) 6 SCC 566: AIR 2000 SC 2493, default in payment of instalment, readiness and willingness not proved. *A. Abdul Rashid Khan v P.A.K.A. Shahul Hamid*, (2000) 10 SCC 636, acting in accordance with the terms of the contract, no delay and, therefore, ready and willing. *Boramma v Krishna Gowda*, (2000) 9 SCC 214, concurrent finding of fact by three lower courts as to readiness and willingness. *Rakha Singh v Babu Singh*, AIR 2002 P&H 270, drafting of plaint, need not be strictly as per Forms 47, 48 of CPC, a substantial compliance with the requirements of the Forms would be sufficient. *M.S. Madhusoodhanan v Kerala Kaumudi P Ltd*, (2004) 9 SCC 204: AIR 2004 SC 909, agreement between members

do clearly indicate the readiness and willingness of the plaintiff to fulfil his part of the obligations under the contract which is the subject-matter of the suit, the fact that they are differently worded will not militate against the readiness and willingness of the plaintiff in a suit for specific performance of contract for sale.

In the instant case, a perusal of the plaint does clearly indicate the readiness and willingness of the plaintiff. The only obligation which he had to comply with was payment of balance of consideration. The appellant-plaintiff had parted with two-thirds of the consideration at the time of execution of the agreement for sale. There is no reason why he would not pay the balance of one-third consideration to have the property conveyed in his favour.”<sup>136</sup>

The judgment of the High Court was set aside and the judgment and decree of the trial court were restored.

Thus, there can be no straight jacket formula about readiness and willingness. It depends upon overall conduct of the parties prior to and subsequent to filing of the suit. The provision in the agreement was that the balance amount was to be paid to the IT Authorities. The court said that the vendor could not insist that it should be paid to him. He could not on that ground say that the vendee was not ready and willing.<sup>137</sup>

An agreement between the parties stipulated terms of reconveyance on payment of loan amount. The plaintiffs sent notices time and again for execution of sale deed and also deposited money in the court before the date fixed in the judgment which was passed for specific performance. This showed their readiness and willingness. Plaintiffs were held entitled to specific performance.<sup>138</sup>

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of a private company for transfer of shares on the death of a member, suit filed within 10 months of the death of the widowed mother, could not be said to be delayed. *Aniglase Yohannan v Ramlatha*, (2005) 7 SCC 534: AIR 2005 SC 3503, where the essential points contained in the plaint led to an interference of the plaintiff's readiness and willingness, the Supreme Court held that the High Court rightly concluded that the requirement of S. 16(c) was satisfied. *Subhash Maini v Nathi Ram*, AIR 2012 All 67, the court saw averment as to readiness from the total state of the pleadings. The vendee repeatedly requested the vendor to take balance money and to get the transfer registered, he appointed a place where he would come with balance money but vendor did not turn up. The court said that the vendee was ready and willing and was entitled to specific performance.

136. *Deendayal v Harjot Kanwar*, AIR 2003 Raj 202, the vendor postponed the purchaser's request for execution of sale deed by saying that her husband was not well, he filed the suit just after one month from the date of refusal, the court said that the purchaser was ready and willing to complete the transaction. The second purchaser was not found to be in a state of bona fides. *Emani Krishna Rao v Vijaya Chitra Films*, AIR 2003 NOC 142 (AP): 2003 AIHC 334, readiness and willingness can be considered in appeal also while appreciating other facts and circumstances. *Dharamveer v Suresh Chandra Bhardwaj*, AIR 2016 All 48, vendee claimed that he was ready with money and willing to pay and had sent a notice to the vendor fixing the date for registration, he waited in the office of Registrar, but vendor did not turn up, requirements proved. *R R. Aravindhan v K.R.S. Janakiraman*, AIR 2016 NOC 240 (Mad), the purchaser proved loan arrangement, ability for readiness and willingness proved.

137. *Satya Jain v Anis Ahmedd Rushdie*, (2013) 8 SCC 131: (2013) 3 SCC (Civ) 738.

138. *Biswanath Ghosh v Gobinda Ghosh*, (2014) 11 SCC 605: (2014) 104 ALR 184; *Mohd Abdul Azeem v South India Prime Tannery (P) Ltd*, AIR 2016 Hyd 170, vendee showed sufficient arrangement of money, made payment to some of the vendors and obtained registered sale

Where the plaintiff showed that he was ready and willing to pay the purchase price and continued to be so, the failure to plead that he had money in the bank and had not withdrawn it, was immaterial because this was a matter of evidence and had not to be pleaded.<sup>139</sup> Possession of adequate means is not a material factor where the vendee has not taken any steps to discharge his part of the obligation as provided in the agreement. Prohibition of Section 16(c) gets attracted in such a case. The court said that if there was undue delay or indifference on his part, his willingness deserves to be doubted. The refusal to grant relief was proper.<sup>140</sup>

When the purchaser had not sent any communication to the vendor regarding his readiness and willingness, had paid only an insignificant amount as advance, had not obtained permission from Ceiling Authorities, had taken no steps towards the valuation of the superstructure on the land as required under the sale agreement, neither led evidence nor entered the witness box in support of his willingness, the Supreme Court held that the High Court had rightly upheld the dismissal of his suit for specific performance.<sup>141</sup> A plea was set up that two applicable statutes prohibited the transfer in question. This plea was not raised before the trial court or Appellate Court. No evidence was produced on the point. The Acts only carried restrictions which were capable of being cleared. There were concurrent findings of fact in favour of the plaintiff. The court said that they were not liable to be interfered with. The decree passed for specific performance could not be faulted. The court added than the fact that there was a considerable increase in the price of the suit land, even if true, could not be a ground for denying specific performance.<sup>142</sup>

Where the buyer pleaded that he was ready and willing but did not pay because the seller did not get the site measured. The court found that the buyer had already paid a part of the consideration in different spells in four years which would not have been done if measuring was an essential condition. He had taken over possession yet did not pay the balance and insist upon registration. Hence he was not ready and willing.<sup>143</sup>

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deeds from them for their respective shares, deposited money for the only other owner, cancellation of the sale agreement by the vendor was not known to vendee. Vendee purchased as a managing director on behalf of the company, specific performance could not be refused.

139. *Rakha Singh v Babu Singh*, AIR 2002 P&H 270.
140. *Malireddy Buthiramanna Dona v Dasari Veerabhadra Rao*, AIR 2012 AP 52. *Daya Ram Soni v Gyarsi Bai Khandelwal*, AIR 2016 Chh 73, vendee not able to prove his ability to pay the balance money after paying earnest money. Vendor even waited at the office of the Registrar on the agreed date but vendee did not turn up. Vendee was held not entitled to specific relief.
141. *Pushparani S. Sundaram v Pauline Manomani James*, (2002) 9 SCC 582. *P. Purushottam Reddy v Pratap Steels Ltd*, (2002) 2 SCC 686: AIR 2002 SC 771, in a suit for specific performance, the High Court decided it without considering in accordance with the law laid down by the Constitution Bench of the Supreme Court is *Chand Rani v Kamal Rani*, (1993) 1 SCC 519: AIR 1993 SC 1742, this was held to be not proper.
142. *Laxman Tatyaba Kankate v Taramati Harishchandra Dhatrak*, (2010) 7 SCC 717: AIR 2010 SC 3025.
143. *Puvvada Chiranjeeva Rao v Busi Koteswara Rao*, AIR 2012 AP 17; *Dharambir Prasad v Devendar Gope*, AIR 2011 Jha 20; conduct showed that the purchaser had no ready money,

The plaintiff (buyer) undertook the responsibility of getting the premises vacated from the unauthorised occupier. He sought specific performance without fulfilling such undertaking. The court said that how the plaintiff could say that he was ready and willing to perform his part of the contract.<sup>144</sup>

The purchaser was required under the agreement to get permission for transfer of the surplus within a specified time which he could not manage. The seller offered to return him his earnest money but he refused to take it. Without disclosing this fact, he sought recovery of the earnest money with 24 per cent interest. Looking at his conduct, the court did not allow him the relief of specific performance.<sup>145</sup>

The mere making of a plea in the plaint is not sufficient. There must be proof with satisfactory evidence of the fact at all the material times of the case. The court said that the conduct of the plaintiff in issuing notice after a period of three years was sufficient in itself to disentitle the plaintiff from claiming the discretionary relief.<sup>146</sup>

Where the acknowledgement receipt of payment of earnest money showed overwriting and banker's cheque for final payment was cancelled, it showed no proper conduct. Specific enforcement was not allowed even though the man showed enough money in his bank account.<sup>147</sup>

#### *Unregistered sale agreement*

An unregistered sale agreement was tendered in evidence. This was held to be not an evidence of a completed sale, but as proof of an agreement of

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he could not claim specific relief or refund of earnest money.

144. *Palay Dutta v Mohd Ali Afsar*, AIR 2016 Cal 199. The court, however, observed otherwise that relief could not have been denied simply on the basis of the fact that there was default in making up deficit stamp duty.
  145. *Citadel Fine Pharmaceuticals v Ramaniyam Real Estates (P) Ltd*, (2011) 9 SCC 147: AIR 2011 SC 3351.
  146. *Ayithi Appalanaidu v Petla Papamma*, AIR 2011 AP 172; *Kalash Properties (P) Ltd v Lilly Pushpam*, AIR 2010 NOC 772 (Mad). The plaintiff must plead and prove that he was ready and willing to perform the contract from its very commencement till end. He filed his suit 30 months after the date of contract, no communication in between, presumption that he was not ready and willing. *Shanthy Kawarbai v Sushila*, AIR 2010 NOC 454 Mad DB, the requisite permission which the purchaser had to manage, he could not do so, he filed his case just one day before expiry of the period of limitation of three years. No relief allowed. *Vishalkumar Nemichand Kakad v Shankar Mahadeo Kubde*, AIR 2009 NOC 258 (Bom), plaintiff was already in possession of the land to be bought by him, yet he complained that the vendor had not carried out demarcation, it was something which he could conveniently do himself. The court said that he was not ready and willing to perform his part.
  147. *Diwakar Mullick v Ganga Khandelwal*, AIR 2016 Chh 53. For a property worth Rs 9 lakhs only Rs 11,000 earnest money was offered. A suspicious conduct.
- Matadin Yadav v Midas Lids (P) Ltd*, AIR 2014 NOC 295 (Del), the plaintiff company purchased property on payment of some advance, but could not pass necessary resolution because the majority shareholder did not consent to it and he was not willing to provide funds for the purpose. The company therefore, had no basis to say that it was ready and willing. The purchaser had also obtained at his expense no objection certificates. But there was neither any application for the same, nor any effort in that direction. Specific performance, not allowed.

sale. It was admissible in evidence as an oral agreement of sale. The purchaser was entitled to relief of specific performance.<sup>148</sup>

### *Amendment of plaint*

The amendment was sought by the plaintiff vendee to incorporate the legal plea of readiness and willingness to perform his part of the contract. The plea happened to be omitted in the plaint. The court said that the plea was not new to the defendant and there was no change in the cause of action. The amendment was accordingly allowed.<sup>149</sup>

### **Default of first buyer available as defence to subsequent buyer**

The fact that the buyer defaulted with payment and was, therefore, not ready and willing to perform, which is a defence available to the seller, would also be available to the second buyer. An appeal being a continuation of the proceedings the subsequent purchaser was allowed to take that defence.<sup>150</sup>

### *Necessary or proper party*

It has been held that persons who are likely to secure interest in the suit property after decision in the pending suit, are neither a proper nor necessary parties.<sup>151</sup>

### *Jurisdiction*

The declaratory relief entails determination of rights to or interests in immovable property. Such relief can be granted only by court within whose local jurisdiction the property is situate. The plaintiff in this case had sought declaratory relief in respect of property when he had only a chance or hope of getting title to the property. His case was rejected. He had an equally efficacious remedy of applying to the Probate Court under Part VII, Chapter XXIII of the Indian Succession Act, 1925.<sup>152</sup>

*Decree, ex p.*— In a suit for specific performance by the purchaser, the seller (defendant) did not file his written statement. A decree was passed as prayed for under Order 7, Rule 10, CPC. The decree, though ex parte, was held to be valid for all purposes. The parties allowed the decree to become final. The seller could not turn around and challenge the decree as unexecutable. The court passing a decree in a specific enforcement suit retains control over the decree in the process of its execution. The purchaser had applied for execution after six and a half years. During this period prices of land shot up. The purchaser did not pay the balance consideration amount because

148. *Akshay Doogad v State of M.P.*, AIR 2016 MP 83.

149. *Jagath Swapna & Co v Church of South India Trust Assn*, AIR 2011 AP 81.

150. *Ram Awadh v Achhaibar Dubey*, (2000) 2 SCC 428: AIR 2000 SC 860. Followed in *Ceean International (P) Ltd v Ashok Surana*, AIR 2003 Cal 263.

151. *Mumbai International Airport (P) Ltd v Regency Convention Centre & Hotels (P) Ltd*, (2010) 7 SCC 417: AIR 2010 SC 3109.

152. *Priyanka Vivek Batra v Neeru Malik*, AIR 2009 NOC 260 (Del).

the transferor had not fulfilled his obligations. Neither party approached the court for appropriate directions. Both parties were at fault. The court has to balance equities in such a situation. The purchaser had to pay increased land value.<sup>153</sup>

### Selling or letting property without title [S. 17]

A person who contracts to sell or let out immovable property with knowledge that he has no right to do so cannot ask for specific enforcement in his favour. This will be so even if he honestly believed that he had the title but is not able to give at the time of performance a title free from reasonable doubt. The same principle is applicable to sale or letting of movable property also. Section 17 is as follows:

**S. 17. Contract to sell or let property by one who has no title, not specifically enforceable.**—(1) A contract to sell or let any immovable property cannot be specifically enforced in favour of a vendor or lessor—

- (a) who, knowing himself not to have any title to the property, has contracted to sell or let the property;
  - (b) who, though he entered into the contract believing that he had a good title to the property, cannot at the time fixed by the parties or by the court for the completion of the sale or letting, give the purchaser or lessee a title free from reasonable doubt.
- (2) The provisions of sub-section (1) shall not apply, as far as may be, to contracts for the sale or hire of movable property.

### Where performance not possible without variation [S. 18]

Where the contract is in writing and, as against the party seeking specific performance, the other party sets up the defence of variation, then in the following cases specific performance cannot be awarded:

- (a) where by reason of fraud, mistake of fact or misrepresentation, the written contract is different from what the parties agreed to, or does not contain all the terms on the basis of which they entered into the contract;
- (b) where the object of the parties was to produce a certain legal result which the contract, as framed, is not calculated to produce;
- (c) where the parties have varied the terms of the contract subsequent to its execution.

The provisions of Section 18 are as follows:

**S. 18. Non-enforcement except with variation.**—Where a plaintiff seeks specific performance of a contract in writing, to which the defendant sets up a variation, the plaintiff cannot obtain the performance sought, with the variation so set up, in the following cases, namely—

153. *Rajinder Kumar v Kuldeep Singh*, (2014) 15 SCC 529: AIR 2014 SC 1155.

- (a) where by fraud, mistake of fact or misrepresentation, the written contract of which performance is sought is in its terms or effect different from what the parties agreed to, or does not contain all the terms agreed to between the parties on the basis of which the defendant entered into the contract;
- (b) where the object of the parties was to produce a certain legal result which the contract as framed is not calculated to produce;
- (c) where the parties have, subsequently to the execution of the contract, varied its terms.

Where a part of the property was inalienable on account of being excess land under a ceiling legislation and another part was inalienable because of acquisition by the State, it was held that the buyer could not seek specific performance of such a contract in respect of the remaining portion of the property only. The court said that such a situation was not covered by Section 18.<sup>154</sup>

The word "court" includes an "arbitrator". Only because Section 20 confers discretion on courts to grant specific performance it does not mean that the parties cannot agree that the discretion may be exercised by a forum of their choice.<sup>155</sup>

**S. 19. Relief against parties and persons claiming under them by subsequent title.**—Except as otherwise provided by this Chapter, specific performance of a contract may be enforced against—

- (a) either party thereto;
- (b) any other person claiming under him by a title arising subsequently to the contract, except a transferee for value who has paid his money in good faith and without notice of the original contract;
- (c) any person claiming under a title which, though prior to the contract and known to the plaintiff, might have been displaced by the defendant;
- (d) when a company has entered into a contract and subsequently becomes amalgamated with another company, the new company which arises out of the amalgamation;
- (e) when the promoters of a company have, before its incorporation, entered into a contract for the purpose of the company and such contract is warranted by the terms of the incorporation, the company:

Provided that the company has accepted the contract and communicated such acceptance to the other party to the contract.

#### Relief against parties, legal representatives or subsequent transferee

Section 19 provides that the relief of specific performance can be obtained against the following parties:

1. against either party to the contract;

154. *K. Narendra v Riviera Apartments (P) Ltd*, (1999) 5 SCC 77: AIR 1999 SC 2309

155. *Olympus Superstructures (P) Ltd v Meena Vijay Khetan*, (1999) 5 SCC 651: AIR 1999 SC 2102.

2. against any other person who claims title arising subsequently to the contract, but not against a transferee for value who paid for the property in good faith and without notice of the original contract;
3. against any person claiming under a prior title which was known to the plaintiff, where the title was such that it could have been displaced by the defendant;
4. against a new company which arises out of the amalgamation of the transferor company;
5. against a company whose promoters entered into a contract for the purposes of the company before its incorporation, provided that the contract is warranted by the terms of the incorporation of the company.

*Relief against legal representative [S. 19]*

Section 19(b) provides that relief can be claimed against any person who claims title arising subsequently to the contract. This would not be so where the legal representative is not competent under the applicable personal law. A vendor died after entering into the agreement. After his death, his widow took further advance from the vendee. According to the Muslim law applicable to the vendor, the widow (mother) is not the legal guardian of her minor children. The advance taken by her for alienation of the property of her minor children did not bind them. The court said that she could not be compelled to execute the sale on the basis of the advance taken by her.<sup>156</sup>

**Parties claiming title under original owner**

*Subsequent bona fide buyer [S. 19(b)]*

Under Section 19(b) of the Specific Relief Act, 1963, a specific performance of a contract can be enforced not only against either party thereto but against any other person claiming under him by a title arising subsequently to the contract, except a transferee for value who has paid his money in good faith and without notice of original contract. Further, Section 91 of the Indian Trusts Act, 1882 provides that where a person acquires property with notice that another person has entered into an existing contract affecting that property, of which a specific performance could be enforced, the former must hold the property for the benefit of the latter to the extent necessary to give effect to the contract. In a case defendants 4 to 7 had notice of the contract between the plaintiff and Defendant 1 and they were not bona fide purchasers, therefore, the High Court was quite justified in passing a decree against them as well.<sup>157</sup>

156. *Amar Ahmad Khan v Shamim Ahmad Khan*, AIR 2012 Jhar 39.

157. *Vasantha Viswanathan v V.K. Elayalwar*, (2001) 8 SCC 133. For another authority see *Jagan Nath v Jagdish Rai*, (1998) 5 SCC 537; AIR 1998 SC 2028. *Rajender Kumar Gupta v Madan Lal*, AIR 2010 NOC 644 (P&H), suit for specific performance filed by prior purchaser. The agreement to sell was not a registered document. It was not his case that he had informed the second purchaser about the sale to him. The court regarded him as a *bona fide* purchaser

In the case of a bona fide purchaser in good faith for value without notice of the original contract between persons in actual possession and owner of the property, it was held by the Supreme Court that in order to establish his *bona fides* such purchaser must show that he had made appropriate enquiries.<sup>158</sup> The court said: "Section 19(b) of the Specific Relief Act, 1963 protects the bona fide purchaser in good faith for value without notice of the original contract. This protection is in the nature of an exception to the general rule. Hence, the onus of proof of good faith is on the purchaser who takes the plea that he is an innocent purchaser. Good faith is a question of fact to be considered and decided on the facts of each case. Section 52 of the Penal Code emphasises due care and attention in relation to good faith. In the General Clauses Act emphasis is laid on honesty."

"A transferee for value, who has paid his money in good faith and without notice of the original contract, is excluded from the purview of clause (b) of Section 19 of the Specific Relief Act providing for specific performance against "any other person claiming under him by a title arising subsequently to the contract". In order to fall within the excluded class, a transferee must show that:

- (a) he has purchased for value the property (which is the subject-matter of the suit for specific performance of the contract);
- (b) he has paid his money to the vendor in good faith; and
- (c) he had no notice of the earlier contract for sale (specific performance of which is sought to be enforced against him).

The said provision is based on the principle of English law which fixes priority between a legal right and an equitable right. This principle is embodied in Section 19(b) of the Specific Relief Act.<sup>159</sup>

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without notice of the earlier sale. The grant of alternative relief of recovery of earnest money with interest was not improper.

158. *R.K. Mohammed Ubaidullah v Hajee C. Abdul Wahab*, (2000) 6 SCC 402: AIR 2001 SC 1658. *Nathan v Nokhu Ram*, AIR 2004 HP 20, no enquiries made by the second buyer to satisfy herself, she also refused to step into the witness box. Suit of the first buyer decreed, no laxity on his part.
159. *Rajan v Yunuskutty*, AIR 2002 Ker 339, oral agreement, the plaintiff filed a piece of paper on which some amount and date were written in support of the alleged oral agreement. The owner executed a sale deed in favour of another person, who was not aware of the pendency of the suit. He was protected by S. 19. Plaintiff not allowed any relief. *Ashan Devi v Phulwasi Devi*, (2003) 12 SCC 219: AIR 2004 SC 511, objection allowed to execution of *ex parte* decree by a third party purchasers who claimed that he was in possession of the vacant land under a registered sale deed; their names were also mutated in Municipal records, they would be dispossessed by delivery of possession to the decree holder. The fact that they were physically there when the property was handed over to the decree holder was held to be immaterial. *Ranganatha Gounder v Sahadeva Gounder*, AIR 2004 Mad 520, a subsequent buyer to whom the property was handed over under registered sale deed and who was not aware of the earlier agreement acquired good title. The buyer under the earlier agreement did not pay the balance money for long and did not object to the subsequent sale except after 2½ years. *Padmakumari v Dasayyan*, (2015) 8 SCC 695: (2015) 4 SCC (Civ) 428, there was failure on the part of the buyer under an agreement of sale to pay the agreed amount of the balance price within the agreed time, hence he could not claim specific enforcement. In the

Where these requirements were not satisfied by the subsequent buyer, the court said that specific performance could be granted against the subsequent transferee. He could be directed to reconvey the property to the original buyer or the sale to the subsequent buyer may be set aside, the property revested in the original seller who may then transfer it to the first buyer. The second buyer may also be ordered to pay compensation to the first buyer.<sup>160</sup>

“Notice” may be (i) actual, (ii) constructive, or (iii) imputed. Under Section 3, Transfer of Property Act and *Explanation II* thereof, a statutory presumption of “notice” arises against any person who acquires any immovable property or any share or interest therein of the title, if any, of the person who is for the time being in actual possession thereof.

“The principle of constructive notice of any title which a tenant in actual possession may have, was laid down by Lord Eldon in *Daniels v Davison*.<sup>161</sup>

“In the present case, the purchasers have acquired a legal right under the sale deed. The right of the tenant under it, if it is true and valid, though earlier in time, is only an equitable right and it does not affect the purchasers if they are bona fide purchasers for valuable consideration without notice of that equitable right.”<sup>161</sup>

Where the first purchaser was a tenant in possession, but did not comply with the agreement for one year and nine months, his contention that the second purchaser, in order to establish his *bona fides*, should have enquired from him as to the nature of his possession, the court said that it was not necessary to make any inquiry from the person in possession.<sup>162</sup>

Where there are unnatural circumstances which may put the purchaser on his guard, an inquiry from the person actually in possession may become necessary in order for the second buyer to establish his *bona fides*. In this case the price of the land was less than 2/3rd of the price for which the land had been agreed to be sold earlier. The second purchaser did not seem to have any intention of making enquiry about the encumbrance. The matter of the land must have become a talk of the village because the first purchaser was put into possession and subsequently dispossessed. The second purchaser could not have been ignorant about all that. The burden of proof

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meantime, the property was purchased by a *bona fide* buyer without notice of the existing sale agreement which was held to be effective and binding. *S. Prasanna v Shany Jalal*, AIR 2015 Kar 172, during the subsistence of earlier agreement of sale to plaintiff, the property was sold to another buyer, burden lay on such buyer to prove that he was a *bona fide* buyer for value in good faith without notice of the earlier agreement, burden is not on the plaintiff.

160. *Rajendra Kantilal Dalal v Bombay Builders Co (P) Ltd*, AIR 2002 Bom 408. *I.S. Sikandar v K. Subramani*, (2013) 15 SCC 27; (2014) 118 Cut LT 89, an agreement for transfer of immovable property was terminated because of non-performance by the transferee (plaintiff). The same property was then transferred to another party for a higher price. The subsequent buyer's case for specific performance was not allowed to be resisted by the first failed buyer. *Mohd Aslam v Rais*, AIR 2015 NOC 31 (Utt), a seven-year old agreement which remained unperformed and gone past all time-limits, not allowed to be set up against subsequent buyer only because he also belonged to the same village.

161. *Ram Niwas v Bano*, (2000) 6 SCC 685: AIR 2000 SC 2921.

162. *Vijay Bhadur and Champalal v Surendra Kumar*, AIR 2003 MP 117.

was on him to show that he was a bona fide purchaser for value and without notice.<sup>163</sup>

A person claiming a title adverse to the title of the vendor does not fall in any of the categories of Section 19. The Supreme Court also added that the section is exhaustive of the persons against whom and by whom specific performance can be allowed.<sup>164</sup>

#### *Transfer executed by only some of owners*

The suit property was jointly owned by respondents. The sale deed was executed by some of them without authorisation from others. The transaction being improper it could not be set right by ratification by others. The execution of ratification by those joint owners who were not parties to the sale deed had no legal value. The sale deed in favour of the subsequent transferee was not saved by Section 19(b).<sup>165</sup>

#### *Acquiring title during pendency of suit*

Where a person purchases a property which had already been sold earlier and a suit about that sale is pending, he does not have the right to say that he is a *bona fide* buyer for value. Such transfer is hit by the principle of *lis pendens*.<sup>166</sup>

#### *Discretion and powers of court [S. 20]*

**S. 20. Discretion as to decreeing specific performance.**—(1) The jurisdiction to decree specific performance is discretionary, and the court is not bound to grant such relief merely because it is lawful to do so; but the discretion of the court is not arbitrary but sound and reasonable, guided by judicial principles and capable of correction by a court of appeal.

(2) The following are cases in which the court may properly exercise discretion not to decree specific performance—

- (a) where the terms of the contract or the conduct of the parties at the time of entering into the contract or the other circumstances under which the contract was entered into are such that the contract, though not voidable, gives the plaintiff an unfair advantage over the defendant; or
- (b) where the performance of the contract would involve some hardship on the defendant which he did not foresee, whereas its non-performance would involve no such hardship on the plaintiff;
- (c) where the defendant entered into the contract under circumstances which though not rendering the contract voidable, makes it inequitable to enforce specific performance.

*Explanation 1.*—Mere inadequacy of consideration, or the mere fact that the contract is onerous to the defendant or improvident in its nature, shall not be

163. *Devinder Singh v Mansha Singh*, AIR 2003 P&H 166.

164. *Kasturi v Iyymaperumal*, (2005) 6 SCC 733; AIR 2005 SC 2813.

165. *A. Pramoda v D. Komaraiah*, AIR 2010 AP 81.

166. *Ceean International (P) Ltd v Ashok Surana*, AIR 2003 Cal 263.



deemed to constitute an unfair advantage within the meaning of clause (a) or hardship within the meaning of clause (b).

*Explanation 2.* — The question whether the performance of a contract would involve hardship on the defendant within the meaning of clause (b) shall, except in cases where the hardship has resulted from any act of the plaintiff, subsequent to the contract, be determined with reference to the circumstances existing at the time of the contract.

(3) The court may properly exercise discretion to decree specific performance in any case where the plaintiff has done substantial acts or suffered losses in consequences of a contract capable of specific performance.

(4) The court shall not refuse to any party specific performance of a contract merely on the ground that the contract is not enforceable at the instance of the other party.

### Discretion

Section 20 of the Specific Relief Act further lists certain circumstances in which the court may at its discretion refuse specific enforcement. The section opens with the remark that the jurisdiction to decree specific performance is discretionary and the court is not bound to give such relief merely because it is lawful to do so. The section, however, immediately adds that such discretion shall not be arbitrarily exercised. It has to be exercised on sound and reasonable basis. Its exercise shall be guided by judicial principles and shall be open to correction by a court of appeal.<sup>167</sup> A person seeking equitable relief should come with clean hands. Where the plaintiff's case was based on certain false and incorrect facts, the relief of specific performance was not granted to him.<sup>168</sup> Specific recovery of property was granted where the buyer was all the time ready and willing to perform his part of the contract and had filed a suit for specific performance and yet the property was sold to another person who was not a bona fide buyer.<sup>169</sup> Where the vendor alleged that the land was mortgaged to a bank and was, therefore, not transferable, but there was a concurrent finding of the courts below that the mortgage stood discharged on repayment of the loan, the bar to transfer ended, the court held that the purchaser was entitled to seek specific performance of the agreement with him.<sup>170</sup>

Where the owner of the property in question agreed to sell it subject to approval under an applicable ceiling legislation but the same was rejected and the authorities permitted transfer in favour of a co-operative society, it was

167. *Kallathil Sreedharan v Kamath Pandyla Prasanna*, (1996) 6 SCC 218, impecuniosity of the party to pay for the part of the joint-family property which came to her in excess of share, advance paid, ordered to be refunded and specific recovery not granted. *Malapali Munaswamy Naidu v P. Sumathi*, (2004) 13 SCC 364, decreeing specific performance without testing the case through the provisions of S. 20 was liable to be set aside.

168. *Lourdu Mari David v Louis Chinnaya Arogiaswamy*, (1996) 5 SCC 589: AIR 1996 SC 2814.

169. *Pirthi v Jati Ram*, (1996) 5 SCC 457.

170. *Indrapal v Sham Shankar Lal*, AIR 2002 All 243.

held that the society having had no notice of the earlier transfer, it obtained a good title in good faith for a valuable consideration. The first buyer was not entitled to any relief except that of refund of advance amount.<sup>171</sup>

The Supreme Court has restated the factors which have to be kept in mind in exercising the power of discretion:<sup>172</sup>

1. Whether the plaintiff was ready and willing to perform his part of the contract in terms of Section 16;
2. Whether it was a case for exercise of discretion by the court for decreeing specific performance under Section 16;
3. Whether there were laches on the part of the plaintiff in approaching the court.<sup>173</sup>

In some cases it will be substantive question of law as to whether discretion is to be exercised or not.<sup>174</sup> The grant of relief is discretionary and not arbitrary. The trial court had exercised its discretion. The appellate court should not exercise discretion against grant of specific performance on extraneous considerations or sympathetic consideration.<sup>175</sup>

No discretion was exercised in favour of a person to whom lease of two properties was promised and of which possession having been given of one, he made illegal reconstitution and, therefore, possession of the other was not given. In such circumstances also there was no question of awarding him any compensation.<sup>176</sup> Discretion was not exercised in favour of a person who instead of performing the contract was setting up the counter claim that the property had already been gifted to her and the gift deed should be produced. There was no mention of such gift deed in the contract of sale.<sup>177</sup>

A person who becomes entitled to specific performance of his right under an agreement also becomes entitled to a decree of permanent injunction to restrain his vendors from in any manner dealing with selling, pledging, alienating or transferring or creating third party interest in the suit property except in favour of the vendee in perpetuity.<sup>178</sup>

171. *Emani Krishna Rao v Vijaya Chitra Films*, AIR 2003 NOC 142 (AP): 2003 AIHC 334.

172. *Rajeshwari v Puran Indoria*, (2005) 7 SCC 60; *K.G. Arumugham v K.A. Chinnappan*, (2005) 2 SCC 793, the purchasers by their default and long lapse of time allowed third-party rights to set in rendering specific performance in their favour to be inequitable and unjust.

173. *Raj Kishore v Prem Singh*, AIR 2011 SC 382, time for reconveyance has always been regarded as of the essence, hence no order for enforcement of such a clause after expiry of time.

174. *Ramesh Chand v Asruddin*, (2016) 1 SCC 653, where conditions or circumstances of the contract gave unfair advantage to the plaintiff, order for specific performance was not granted. *Hemanta Mondal v Ganesh Chandra Naskar*, (2016) 1 SCC 567: AIR 2015 SC 3757, recitals about property, e.g. area of land were not clear, the plaintiff buyer was not doing any substantial acts, nor suffering any monetary loss, specific relief denied.

175. *K. Prakash v B.R. Sampath Kumar*, (2015) 1 SCC 597: AIR 2015 SC 9.

176. *Subhadra Rani Pal Choudhary v Sheirly Weigal Nain*, (2005) 5 SCC 230: AIR 2005 SC 3011. *Surinder Singh v Kapoor Singh*, (2005) 5 SCC 142, the court has to see in whose favour equity lies.

177. *Madhu Verma v Urmila Devi*, AIR 2011 Pat 46.

178. *Vijay Kumar v Neeru Rajput*, AIR 2014 NOC 217 (Del).

### Buyer with notice of previous sale

A sale agreement was made with the plaintiff for discharging family debts. Possession was handed over on the date of the agreement. Subsequent to this a sale deed was executed in favour of a third party in respect of the same property. The latter was made aware of the first agreement. The court held that it could not be said that the third party acted in good faith. The plaintiff also produced the mortgage deed and the fact of payment for redemption of the mortgage was endorsed on it. The third party did not produce any such discharged mortgage bond. The court accordingly allowed the plaintiff to enforce the agreement against the third party buyer also.<sup>179</sup>

“Granting of specific performance is an equitable relief, though the same is now governed by the statutory provisions of the Specific Relief Act, 1963. These equitable principles are incorporated in Section 20 of the Act. While granting a decree for specific performance, these salutary guidelines shall be in the forefront of the mind of the court. The trial court, which had the added advantage of recording the evidence and seeing the demeanour of the witnesses, considered the relevant facts and reached a conclusion. The appellate court should not have reversed that decision disregarding these facts and the appellate court seriously flawed in its decision. Therefore, it is held that the respondent is not entitled to a decree of specific performance of the contract.”<sup>180</sup>

Discretion should be exercised in accordance with justice, equity, good conscience and fairness to both the parties.<sup>181</sup> Where in suit for specific performance filed by the respondent in 1970, alternative relief of Rs 12,000 as damages was also claimed, and the defendant-appellant was then prepared to pay Rs 10 lakhs as alternative relief, it was held that the decree for specific performance at this distance of time would be unrealistic and unfair. Hence, an alternative relief of payment of Rs 10 lakhs was ordered.<sup>182</sup>

179. *Jammula Rama Rao v Meria Krishnaveni*, AIR 2003 NOC 134 (AP): 2003 AIHC 106 (AP). *Sargunam v Chidambaram*, (2005) 1 SCC 162: AIR 2005 SC 1420, the second buyer had notice of the first sale, not allowed specific relief.

180. *A.C. Arulappan v Ahalya Naik*, (2001) 6 SCC 600: AIR 2001 SC 2783.

181. *Ameer Mohd v Barkat Ali*, AIR 2002 Raj 406, discretion to be based on sound and reasonable judicial principles and not to be exercised arbitrarily. On facts, however the oral agreement could not be proved. *Yelamati Veera Venkata Jagannatha Gupta v Vejju Venkateswara Rao*, AIR 2002 AP 369, oral agreement, the vendor was the landlord, the tenant alleged that he had paid amounts to the landlord, without taking receipts, the facts showed that the landlord was giving him receipts even for rent, other inconsistencies in evidence, oral agreement not proved. *Manjunath Anandappa v Tammanasa*, (2003) 10 SCC 390: AIR 2003 SC 1391 suit filed six years after date of agreement to sell and that too when the suitor came to know that the land had been sold to someone else, though time was not of the essence, he should have approached the seller and the court within a reasonable time, having regard to his conduct, discretionary relief was refused to him. *Nallabothu Purnaiah v Garre Mallikarjuna Rao*, AIR 2003 AP 201, purchaser had means to pay, sale deed proved, no delay in seeking relief by the buyer, relief allowed.

182. *Nahar Singh v Harnak Singh*, (1996) 6 SCC 699. *Arjun Paradeepak v G. Vani*, AIR 2003 NOC 468 (AP), the seller was always ready and willing, buyer was guilty of laches, he never

Where the subsequent purchaser did not make enquiries at the office of the sub-registrar so as to find out whether the property had already been transferred to another person, the court said that it could be concluded that the subsequent purchaser had knowledge of the first sale. They could not be termed as bona fide buyers. No discretion could be exercised in their favour.<sup>183</sup>

Sub-section (2) then enumerates situations in which the court can properly at its discretion refuse to order specific performance.

### 1. *Unfair contracts*

The court may refuse specific performance where a contract gives an unfair advantage to the plaintiff over the defendant. The unfairness of the contract may appear from the terms of the contract, from the conduct of the parties at the time of entering into the contract, or other surrounding circumstances. It is not necessary that the contract should be voidable. It is enough if it is exploitative. An ordinary example would be a case where a signature is obtained under a state of utter surprise or drunkenness. Where a person contracted to purchase a leasehold estate, the seller suppressing information that the landlord had served notice for repair of a dilapidated portion, specific performance was denied to the seller although the suppression was not sufficient in itself to allow rescission to the buyer.<sup>184</sup> Inadequacy of consideration may not be sufficient in itself unless it is shocking and it appears that the defendant has taken advantage of his superior bargaining position.<sup>185</sup>

The conduct of the person claiming specific relief also has an important bearing upon the discretion of the court. Specific relief has been refused on this ground to persons who induced others to enter into contracts with them by holding out oral assurances which they did not fulfil though such assurances may not be expressed in the contract.<sup>186</sup> A person purchased another man's right to certain property but the sale could not be completed because of the death of the seller before the execution of the sale deed. Subsequently

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treated time to be an essential factor, he also suffered no loss because there was no price rise, the seller allowed to enforce the sale against the buyer.

183. *Ram Swaroop Singh v Karan Singh*, AIR 2010 Utt 122.

184. *Beyfus v Lodge*, 1925 Ch 350. *Tci Distribution Centres Ltd v Official Liquidator*, (2009) 6 CTC 814, the official liquidator notified the sale of the company's property as per directions of the court on "as is, where is, what is" basis. The auction purchaser had all the time to see the property and examine documents connected with it. But he did not do so. Applied for setting aside of the purchase because OL had not disclosed things like overhead high tension wires in a portion of the property and a TV room in a corner. The court said that any one could have noticed these things on a mere visit to the sight.

185. *S. Ramgaraju Naidu v S. Thiruvarakkarsu*, 1995 Supp (2) SCC 680: AIR 1995 SC 1769; *S.V.R. Mudaliar v Rajabu F. Buhari*, (1995) 4 SCC 15: AIR 1995 SC 1607, inequitable conduct in assigning rights under the contract. *Jai Narain Parasrampuria v Pushpa Devi Saraf*, (2006) 7 SCC 756, inadequacy of consideration is not in itself a ground for refusing specific relief.

186. *Handley Page Ltd v Customs and Excise Commrs and Rockwell Machine Tool Co Ltd*, (1970) 2 Lloyd's Rep 459 (CA), specific relief was resorted to in order to escape a set-off; *Surya Narain Upadhyaya v Ram Roop Pandey*, 1995 Supp (4) SCC 542: AIR 1994 SC 105, a failure to make up the deficiency in court fee, an indication of inability to pay consideration.

the purchaser acquiesced in the widow of the seller disposing of the same property to another person. Subsequently still, the original purchaser disposed of his rights under the contract to another person who instituted the present proceedings to specifically recover the property. The Supreme Court did not favour him with a decree of specific performance. The original buyer had lost or waived his rights by virtue of his acquiescence. The transferee of his rights had no better rights than the letter's rights. Thus he was only entitled to recover the advance-money.<sup>187</sup>

A provision in a sale agreement for refund of the entire advance money is a normal feature in every agreement of sale. Such a clause cannot give unfair advantage to purchasers.<sup>188</sup>

The terms of the contract in question gave an unfair advantage to the plaintiff purchaser. The amount of earnest money received at the time of agreement was differently stated in the agreement and receipt. The defendants took the plea that they only took a loan of Rs 85,000 and mortgaged their land as security and were tricked into putting their thumb impression on the purported agreement of sale. It was held to be proper that relief of specific performance was refused.<sup>189</sup>

**Contingent contracts.**—In an agreement for sale of land, the condition was that the sale deed would be executed after the seller obtained permission for use of the land as village land. It was held that the contract was not contingent. It was specifically enforceable. The suit filed within three years after obtaining permission was not time-barred.<sup>190</sup>

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187. *Parakunnam Veetill Joseph's Son Mathew v Nedumbara Kuruvela's Son*, 1987 Supp SCC 340: AIR 1987 SC 2328. The old Act contained the following illustrations on this point:

(1) A, a tenant for life of certain property, assigns his interest therein to B. C contracts to buy, and B contracts to sell, that interest. Before the contract is completed, A receives a mortal injury from the effects of which he dies the day after the contract is executed. If B and C were equally ignorant or equally aware of the fact, B is entitled to specific performance of the contract. If B knew the fact, and C did not, specific performance of the contract should be refused to B.

(2) A contracts to sell to B the interest of C in certain stock-in-trade. It is stipulated that the sale shall stand good, even though it should turn out that C's interest is worth nothing. In fact, the value of C's interest depends on the result of certain partnership accounts, on which he is heavily in debt to his partners. This indebtedness is known to A, but not to B. Specific performance of the contract should be refused to A.

(3) A contracts to sell, and B contracts to buy, certain land. To protect the land from floods, it is necessary for its owner to maintain an expensive embankment. B does not know this circumstances, and A conceals it from him. Specific performance of the contract should be refused to A.

(4) A's property is put up to auction. B requests C, A's attorney, to bid for him. C does this inadvertently and in good faith. The persons present, seeing the vendor's attorney bidding, think that he is a mere puffer and cease to compete. The lot is knocked down to B at a low price. Specific performance of the contract should be refused to B.

188. *R. Aravindhan v K.R.S. Janakiraman*, AIR 2016 NOC 240 (Mad).

189. *Shamsher Singh v Rajinder Kumar*, (2015) 5 SCC 531: AIR 2014 SC 2253.

190. *Rojasara Ramjibhai Dabyabhai v Jani Narottamdas Lallubhai*, (1986) 3 SCC 300: AIR 1986 SC 1912.

The seller cannot sue for the price unless he obtains the necessary permissions first.<sup>191</sup>

According to a decision of the Supreme Court subsequent events can also be taken into account in exercising discretion under the section.<sup>192</sup> The court said:

“Jurisdiction of courts under Section 20 is discretionary. Subsequent events can be taken into consideration to decide to exercise or not to exercise jurisdiction. Hence, where the agreement to sell land stipulated that it was subject to grant of permission by the competent authority under the Urban Land (Ceiling and Regulation) Act, 1976 and the authority refused to grant such permission, it was held, that such order of the competent authority should have been necessarily taken into consideration to decide as to whether to exercise the discretionary jurisdiction to direct specific performance of the agreement or not. Till the order of the competent authority stood, decree for specific performance of the contract could not be granted. Where the discretionary jurisdiction was not exercised in favour of the plaintiff by the trial court and the appellate court (Single Judge, High Court in this case), the Division Bench of the High Court could not, in exercise of its Letters Patent jurisdiction, normally interfere with such decisions of the courts below.

**Contracts Incomplete.**—Where in an agreement for sale of flats, there was no consensus between the parties as to the price payable, the court said specific performance could not be ordered. The builder was directed to refund the amount received from the purchaser and thereafter he was to vacate the flats. The court also said that the discretion in the grant of specific performance has to be exercised on sound judicial principles and not arbitrarily. The plaintiff must prove beyond doubt the existence of a valid and enforceable contract.<sup>193</sup>

191. *Nathulal v Phoolchand*, (1969) 3 SCC 120: AIR 1970 SC 546: (1970) 2 SCR 854. *Chandnee Widya Vati Madden v C.L. Katial*, AIR 1964 SC 978: (1964) 2 SCR 495; *Ramesh Chandra Chandiok v Chuni Lal Sabharwal*, (1970) 3 SCC 140: AIR 1971 SC 1238, the court has jurisdiction to order the vendor to apply for permission within a certain time and effect the transfer after such permission.

192. *M. Meenakshi v Metadin Agarwal*, (2006) 7 SCC 470.

193. *Mirahul Enterprises v Vijaya Srivastava*, AIR 2003 Del 15. *Manohar-Lal v Maya*, (2003) 9 SCC 478: AIR 2003 SC 2362, the contention of the seller lady that her thumb impression was taken on same blank paper, the court said that it could not be brushed aside, refund of consideration allowed. *M. Jaya Rao v M. Krishna Rao*, AIR 2012 AP 34, no clear agreement, vendee claimed that he perfected his title of ownership by being in possession for more than 12 years. This fact and being ready and willing to perform contract are opposite things, no relief allowed. *Vimlesh Kumari Kulshrestha v Sambhajirao*, (2008) 5 SCC 58: AIR 2009 SC 806, sale of tenanted premises, agreement contained only boundaries of property, the plan of the property showing definite subject-matter not attached, the map of sketch attached with the plaint did not correspond with agreement, specific performance not granted. *Claridges Infotech (P) Ltd v Surendra Kapur*, AIR 2009 Bom 1, acceptance must be in terms of the offer, conditional acceptance amounts to counter offer. It is not concluded agreement that could form the basis of a suit for specific performance.

The mortgagor of property executed an unregistered document to sell the mortgaged property to the mortgagee as and when he might decide to do so at the prevailing market rate. But he sold the property to his nephew. The mortgagee filed the suit for specific performance. He was not able to place on record any material to show that the cousin was aware of the earlier agreement. The court accordingly held that the suit could not be decreed. The agreement was an inchoate agreement and also vague. The mortgagee was trying to secure an undue advantage whereas the cousin was a *bona fide* buyer for consideration.<sup>194</sup> In an auction sale of the borrower company's assets, the highest bidder deposited the earnest amount but not 25 per cent of the bid money within the stipulated period. Thus there was no concluded contract. The highest bidder was held to be not entitled to the decree of specific enforcement of the agreement of sale in his favour.<sup>195</sup>

The area of land agreed to be sold was not clear and final. The plaintiff could not be said to have done substantial acts or suffered losses due to expenditure in construction, etc. The court said that the contract was not capable of supporting an order of specific enforcement. On facts, it would be equitable, fair and proper to direct the seller to pay back the amount of earnest money with interest at 18 per cent p.a.<sup>196</sup>

*Transfer by unauthorised partners.*—A partnership firm comprised of 14–15 partners. The prospective purchaser of a property of the firm entered into an oral agreement with only two partners. Neither they were so authorised, nor it was a part of their implied authority. The agreement being not enforceable against the firm, the court did not allow any relief under the Specific Relief Act.<sup>197</sup>

*Transfer by unauthorised person.*—The transferor was only half owner of the property. The other half belonged to his wife. Yet he purported to transfer the whole. The court held that the wife, being non-consenting, was not bound by the purported sale. There could be no decree of specific performance against her.<sup>198</sup>

*Oral agreement.*—A suit was filed for specific performance of an oral agreement to purchase the premises in question. The court said that the plaintiff would be entitled to an interim relief only upon showing his readiness and willingness to perform his part of the contract. Under Section 49 of the Registration Act, a suit for specific performance can be filed on the basis of an unregistered document and also upon an oral agreement.<sup>199</sup>

194. *Sahadeva Gramani v Perumal Gramani*, (2005) 11 SCC 454.

195. *Kerala Financial Corp v Vincent Paul*, (2011) 4 SCC 171: AIR 2011 SC 1388.

196. *Hemanta Mondal v Ganesh Chandra Naskar*, (2016) 1 SCC 567: AIR 2015 SC 3757.

197. *Sagarmal Gulabchand Jain v Gujarati Beedi Co*, AIR 2011 MP 172.

198. *Kammanna Sambamurthy v Kalipatnapu Atchutamma*, (2011) 11 SCC 153: AIR 2011 SC 103. *Sohan Singh v Avtar Singh*, AIR 2015 Raj 1, sale by one of the legal heirs with a small share in the land without authority of any other legal heir not allowed to be specifically enforced.

199. *Nirav Deepak Modi v Najoo Behram Bhiwandiwala*, AIR 2012 Bom 50.

A plea for possession in part performance of an oral agreement of sale cannot be raised by the vendee in a suit for specific performance.<sup>200</sup>

In the case of an oral agreement, heavy burden lies on the plaintiff to prove that there was consensus ad idem between the parties. An oral agreement cannot be presumed unless there is evidence of the date on which the parties had come to the concluded oral agreement. There should be no finding of this kind on the basis of conjectures and assumptions.<sup>201</sup>

### *Memorandum of understandings*

A memorandum of understanding to purchase immovable properties on its basis was held to be neither equivalent to registered agreement, nor specific about any properties and therefore could not support the plea of specific performance or an injunction.<sup>202</sup>

### *2. Hardship*

Specific enforcement is refused where it would cause considerable hardship to the defendant which he did not foresee, whereas non-performance would cause no such hardship to the plaintiff. Specific enforcement was not granted where the buyer of land for farming purposes found it to be land-locked from all sides without any right of way;<sup>203</sup> where the cost of performance to the defendant was wholly out of proportion to the benefits to the plaintiff;<sup>204</sup> and where it involved litigation with uncertain results to enable the defendant to perform.<sup>205</sup>

Ordinarily, the fact that the performance would cause severe hardship to the defendant has to be considered on the basis of facts existing at the time of the contract. And where the plaintiff has caused the hardship by his subsequent conduct, that would also be taken into account. The explanation gives effect to this principle. Where the grant of specific relief would have resulted in a special hardship to the defendants who had already built costly structures on the land in question, it was held by the Supreme Court that Section 20(2)(b) should be invoked even though the plaintiffs were ready and willing to perform the contract and it were the defendants who committed breaches of the contract. Accordingly, instead of executing the sale deed in favour of the plaintiffs, the defendants were directed to pay to the plaintiffs the specified present value of the land in instalments.<sup>206</sup> The jurisdiction under

200. *Karam Chand v Labb Chand*, AIR 2009 NOC 868 (Raj).

201. *Sri Sunamani Nath v Sukumari Deb*, AIR 2009 NOC 261 (Gau). *K. Nanjappa v R.A. Hameed*, (2016) 1 SCC 762, the Supreme Court did not exercise discretion in favour of directing specific performance on the basis of an oral agreement because of many uncertain features in proof of it.

202. *Parle Biscuit (P) Ltd v Kabisco Agro Foods (India) (P) Ltd*, AIR 2009 NOC 256 (All).

203. *Denne v Light*, (1857) 8 DM&G 774: 44 ER 588.

204. *Morris v Redland Bricks Ltd*, 1970 AC 652: (1969) 2 WLR 1437 (HL).

205. *Wroth v Tyler*, 1974 Ch 30: (1973) 2 WLR 405.

206. *Damacherla Anjaneyulu v Damcherla Venkata Seshaiah*, 1987 Supp SCC 75: AIR 1987 SC 1641.

Section 20 of the Specific Relief Act, 1963 to decree specific performance is discretionary and the court is not bound to grant such relief merely because it is lawful to do so; the discretion of the court is not arbitrary but sound and reasonable, guided by judicial principles and capable of correction by a court of appeal. Performance of the contract involving some hardship on the defendant which he did not foresee, while non-performance involving no such hardship, on the plaintiff, is one of the circumstances in which the court may properly exercise discretion not to decree specific performance. The doctrine of comparative hardship has been statutorily recognized in India. However, mere inadequacy of consideration or the mere fact that the contract is onerous to the defendant or improvident in its nature shall not constitute an unfair advantage to the plaintiff over the defendant or unforeseeable hardship on the defendant.<sup>207</sup> The fact that the house under sale was the available residence with the seller and without it he would be rendered homeless was held to be not a hardship because he was aware of this fact when he made the agreement of sale.<sup>208</sup>

Where the purchasers had purchased the property some 25 years before the case reached the Supreme Court and had spent huge sums of money on improvements, it was held that decreeing the suit in favour of the opposite party would have meant hardship to the purchasers. Therefore, compensation was awarded in favour of the opposite party.<sup>209</sup> The plaintiff kept postponing registration. It was held that this conduct caused hardship to the defendant-owner inasmuch as he could not purchase another property out of the consideration money which would have come into his hand if the agreement had been performed. Discretion could not be exercised in favour of such plaintiff.<sup>210</sup>

A man sold the whole of the property whereas half of it belonged to his wife who did not sign. Both of them died. The transferee sought specific recovery of half portion of the man's share. His 10 daughters who were living in the single dwelling house, resisted the suit on the ground of hardship. The Supreme Court allowed recovery of half share because that was not likely to cause any hardship.<sup>211</sup>

**Price Escalation.**—“Where the court is considering whether or not to grant a decree for specific performance for the first time, the rise in the price of the land agreed to be conveyed may be a relevant factor in denying the relief of specific performance. But in this case, the decree for specific performance

207. *K. Narendra v Riviera Apartments (P) Ltd*, (1999) 5 SCC 77: AIR 1999 SC 2309. *A. Maria Angelina v A.G. Balkis Bee*, (2002) 9 SCC 597: AIR 2002 SC 2385: plea of hardship not raised in the written statement, raised for the first time before the Appellate Court, concurrent finding of Lower Courts of the plaintiff being ready and willing, no interference in the decree of specific performance.

208. *Darshan Singh v Dalip Kaur*, 2014 SCC OnLine P&H 19044: AIR 2015 P&H 10.

209. *V. Muthusami v Angammal*, (2002) 3 SCC 316: AIR 2002 SC 1279.

210. *K.N. Krishnamurthy v G.K. Sridhar*, AIR 2009 NOC 263: (2008) 6 AIR Kant R 369.

211. *Kammanna Sambamurthy v Kalipatnapu Atchutamma*, (2011) 11 SCC 153: AIR 2011 SC 103.

has already been passed by the trial court and affirmed by the first appellate court. The only question before the Supreme Court was whether the High Court in second appeal was correct in reversing the decree. Consequently the principle enunciated in *K.S. Vidyanadam* will not apply.”<sup>212</sup>

In another case, the Supreme Court observed:

The grant of a decree for specific performance of contract is not automatic and is one of the discretions of the court and the court has to consider whether it will be fair, just and equitable. The court is guided by principles of justice, equity and good conscience.

The court should meticulously consider all facts and circumstances of the case and motive behind the litigation should also be considered.

“In view of the clear finding of the High Court that the appellant tried to wriggle out of the contract between the parties because of escalation in prices of real estate properties, the respondent is held entitled to get a decree as he has not taken any undue or unfair advantage over the appellant. It will be inequitable and unjust at this point of time to deny the decree to the respondent after two courts below have decided in favour of the respondent.”<sup>213</sup>

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212. *V. Pechimuthu v Gowrammal*, (2001) 7 SCC 617: AIR 2001 SC 2446. The decision in *K.S. Vidyanadam v Vairavan*, (1997) 3 SCC 1: AIR 1997 SC 1751 was distinguished on facts. *Gobind Ram v Gian Chand*, (2000) 7 SCC 548: AIR 2000 SC 3106, further sum directed to be paid for securing order of performance.

213. *Gobind Ram v Gian Chand*, (2000) 7 SCC 548: AIR 2000 SC 3106. The court relied on *Parakunnan Veetill Joseph's Son Mathew v Nedumbara Kuruvila's Son*, 1987 Supp SCC 340: AIR 1987 SC 2328 and distinguished *Damacherla Anjaneyulu v Damcherla Venkata Seshaiah*, 1987 Supp SCC 75: AIR 1987 SC 1641. *Nirmala Anand v Advent Corp (P) Ltd*, (2002) 5 SCC 481: AIR 2002 SC 2290, decree for delivery of the flat at escalated price. Specific relief not refused because there was a possibility of renewal of lease and revalidation of building plan. The court said that there was no general rule that the plaintiff must necessarily be denied the benefit of price increase. While balancing equities, the court must bear in mind as to who was the defaulting party. *R. Aravindhan v K.R.S. Janakiraman*, AIR 2016 NOC 240 (Mad), seller trying to get out of the contract only because of price rise, the court in its discretion allowed specific performance.

The old Act contained the following illustrations on this point:

(1) A is entitled to some land under his father's will on condition that if he sells it within twenty-five years, half the purchase-money shall go to B. A, forgetting the condition, contracts, before the expiration of twenty-five years, to sell the land to C. Here the enforcement of the contract would operate so harshly on A, that the Court will not compel its performance in favour of C.

(2) A and B, trustees, join their beneficiary, C, in a contract to sell the trust estate to D, and personally agree to exonerate the estate from heavy incumbrances to which it is subject. The purchase-money is not merely enough to discharge those incumbrances, though, at the date of the contract, the vendors believed it to be sufficient. Specific performance of the contract should be refused to D. [Based on *Wedgwood v Adams*, (1843) 6 Beav 600: 63 RR 195: 49 ER 958.]

(3) A, the owner of an estate, contracts to sell it to B, and stipulates that he, A, shall not be obliged to define its boundary. The estate really comprises a valuable property, not known to either to be part of it. Specific performance of the contract should be refused to B unless he waives his claim to the unknown property. [Based on *Baxendale v Seal*, (1855) 19 Beav 601: 105 RR 261.]

(4) A contracts with B to sell him certain land, and to make a road to it from a certain railway station. It is found afterwards that A cannot make the road without exposing himself

Subsequent rise in price is not to be treated as a hardship to entail refusal of decree for specific performance.<sup>214</sup>

The vendor was willing to complete the transaction as early as possible. But there was delay of nearly two years on the part of the purchaser in obtaining the requisite permission of the Collector which was necessary for completion of the transaction. There was a substantial rise in the market prices of property including that of the property in question. Even if time was not of the essence, parties are supposed to perform their obligations within reasonable time when the market has become price sensitive. The court said that in such a case it would be inequitable to give the relief of specific performance to the purchaser. But he was held entitled to a money decree for repayment of consideration paid by him to the transferor along-with interest at 18 per cent p.a. from the date of payment.<sup>215</sup>

A suit for specific performance of sale of an urban property was filed after the lapse of a long period. The court said that it could refuse to grant the relief of specific performance as the value of such property escalates very fast.<sup>216</sup>

Thus, the relief of specific performance cannot be denied on the ground of efflux of time and escalation of price of the property in the meantime. In such cases, the court can grant relief under revision of the price according to the then market value.<sup>217</sup>

### 3. Inequitable, unconscionable

Where the circumstances of a contract are such that, though they do not make the contract voidable, they definitely render specific enforcement inequitable, the contract is one-sided, an imposition by one upon the other, the parties are not on equal footing, are some of the circumstances which the

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to litigation. Specific performance of the part of the contract relating to the road should be refused to *B*, even though it may be held that he is entitled to specific performance of the rest with compensation for loss of the road. [Based on *Peacock v Penson*, (1848) 11 Beav 355: 50 ER 854.]

(5) *A*, a lessee of mines, contracts with *B*, his lessor, that any time during the continuance of the lease, *B* may give notice of his desire to take the machinery and plant used in and about the mines, and that he shall have the articles specified in his notice delivered to him at a valuation on the expiry of the lease. Such a contract might be most injurious to the lessee's business, and specific performance of it should be refused to *B*. [Based on *Talbot v Ford*, (1842) 13 Sim 173: 60 RR 314.]

(6) *A* contracts to buy certain land from *B*. The contract is silent as to access to the land. No right of way to it can be shown to exist. Specific performance of the contract should be refused to *B*. [Based on *Denne v Light*, (1857) 8 DM&G 774: 44 ER 588.]

(7) *A* contracts with *B* to buy from *B*'s manufactory and not elsewhere all the goods of a certain class used by *A* in his trade. The Court cannot compel *B* to supply the goods but if he does not supply them, *A* may be ruined, unless he is allowed to buy them elsewhere. Specific performance of the contract should be refused to *B*. [Based on *Hills v Croll*, (1845) 2 Ph 60: 78 RR 23.]

214. *K. Prakash v B.R. Sampath Kumar*, (2015) 1 SCC 597: AIR 2015 SC 9.

215. *Paramananda Bose v Santosh Kumar Dutta*, AIR 2011 NOC 140 (Ori).

216. *Vimaleshwar Nagappa Shet v Noor Ahmed Sheriff*, (2011) 12 SCC 658: AIR 2011 SC 2057.

217. *Satya Jain v Anis Ahmed Rusbdie*, (2013) 8 SCC 131: (2013) 3 SCC (Civ) 738.

court keeps in mind in considering whether an order of specific enforcement would give rise to inequitable results. One of the illustrations appended to Section 22 of the repealed Act of 1877 affords an example. A contracts with B to buy from B's manufactory and not elsewhere all the goods of a certain class used by him in his trade. The court cannot compel B to supply the goods but if he does not supply them, A may be ruined, unless he is allowed to buy them elsewhere. B cannot specifically enforce the contract against A.<sup>218</sup>

"The jurisdiction to decree specific relief is discretionary and the court can consider various circumstances to decide whether such relief is to be granted. Merely because it is lawful to grant specific relief, the court need not grant the order for specific relief; but this discretion shall not be exercised in an arbitrary or unreasonable manner. Certain circumstances have been mentioned in Section 20(2) of the Specific Relief Act, 1963 as to under what circumstances the court shall exercise such discretion. If under the terms of the contract the plaintiff gets an unfair advantage over the defendant, the court may not exercise its discretion in favour of the plaintiff. So also, specific relief may not be granted if the defendant would be put to undue hardship which he did not foresee at the time of agreement. If it is inequitable to grant specific relief, then also the court would desist from granting a decree to the plaintiff."

From the terms and conditions adumbrated in the second agreement it is clear that the respondent had been trying to take unfair advantage of the appellant and that the circumstances in which this agreement was executed was within a short period of termination of the first contract by the respondent, make it highly probable that the appellant might not have readily agreed to this contract. There are other circumstances also to hold that the plaintiff-respondent had not approached the court with clean hands. It is clear that she had been trying to get possession of the house even before execution of the sale deed, for which she had apparently colluded with the tenant. Moreover, the appellant in this case was clearly in impecunious circumstances and so many loans were outstanding against him. He had executed the first agreement to pay off these debts and in order to raise some funds. From the first agreement it is clear that the parties were not very serious about the sale of the house. The fact that after a few months the respondent resiled from the agreement and sought repayment of the money also proves this fact. The appellant had voluntarily retired from service. Admittedly, he had no other house to stay in after retirement. The respondent-plaintiff had tried to take unfair advantage of the defendant and throughout the course of the transaction she had not been fair. The trial court, which had the added advantage of recording the evidence and seeing the demeanour of the witnesses, considered the relevant facts and reached a conclusion. The

218. Based on *Hills v Croll*, (1845) 2 Ph 60: 78 RR 23.

appellate court should not have reversed that decision disregarding these facts and the appellate court seriously flawed in its decision. Therefore, it is held that the respondent is not entitled to a decree of specific performance of the contract.”<sup>219</sup>

Where the true object of an agreement (construction of houses under Section 21 of the Urban Land Ceiling Act for weaker sections of society in this case) could not be fulfilled (as a result of changes in the master plan in this case), it would be inequitable to enforce specific performance of the agreement. Harm to the reputation of the plaintiff was irrelevant. Specific relief was not allowed where the transferor was not capable of dealing with the property because of the doctrine of *lis pendens*, the same being already the subject-matter of dispute in a court case.<sup>220</sup>

“Grant of decree for specific performance is a matter of discretion under Section 20 of the Specific Relief Act, 1963. The court is not bound to grant such relief merely because it is lawful to do so. Discretion is to be exercised on sound and settled judicial principles. One of the grounds on which the court may decline to decree specific performance is where it would be inequitable to enforce specific performance. The present is clearly such a case. It would be wholly inequitable to enforce specific performance for (i) residential houses for weaker sections of society cannot be constructed in view of the existing master plan and, thus, no benefit can be given to the said section of society; (ii) in any case, it is extremely difficult, if not impossible, to continuously supervise and monitor the construction and thereafter allotment of such houses; (iii) the decree is likely to result in an uncalled-for bonanza to the plaintiff; (iv) patent illegality of the order of the Competent Authority dated 20-6-1998; (v) absence of law or any authority to determine excess vacant land after construction of 4356 dwelling units; and (vi) agreement does not contemplate the transfer of nearly 600 acres of land in favour of the plaintiff for construction of 4356 units for which land required is about 65 acres. The object of the Act was to prevent concentration of urban land in the hands of a few and also to prevent speculation and profiteering therein. The object of Section 21 is to benefit weaker sections of society and not the owners. If none of these objects can be achieved, which is the

219. *A.C. Arulappan v Abalya Naik*, (2001) 6 SCC 600: AIR 2001 SC 2783. *Akbar Ali v Vinod Khanna*, (2005) 9 SCC 367: AIR 2004 SC 3940, in the absence of plea of inadequate price raised, or an issue framed, or evidence led on the point, in the written statement not to hold that the agreement to sell was unconscionable. *Devalsab v Ibrahimsab F. Karajagi*, (2005) 3 SCC 342: AIR 2005 SC 1940, the owner contracted to sell the property to the plaintiff, the owner did not execute the sale deed with the plaintiff and instead attempted to sell the property to the second buyer. The latter filed a collusive suit on the seller. The suit resulted in a compromise decree under which sale deed was executed in favour of second buyer. The Supreme Court set aside the order of specific performance in favour of the second buyer and awarded it to the first buyer. The court said that there was no such equity left in the conduct of the second buyer as the suit filed by him was preconceived and prearranged with the seller in order to cheat the first buyer.

220. *Tara Singh v State of Punjab*, AIR 2011 NOC 452 (P&H).

factual position, it would be inequitable to still maintain decree for specific performance.”<sup>221</sup>

**Plaintiff to come with clean hands.**—Where a party instituted different proceedings in different forums within a short span of time, it was held that such a party who abuses the process of courts could not be said to be possessed of clean hands and is, therefore, not entitled to equitable relief under the Act.<sup>222</sup>

Where the value of the property was much more than was mentioned in the agreement to sell, the plaintiff was in possession as a tenant and stopped paying rent since the date of the agreement, the court said that the mere fact of the agreement did not confer ownership on the plaintiff. He was not entitled to the equitable relief of specific performance.<sup>223</sup> Where the claimant was not able to prove that the sale deed was validly executed by the vendor and the vendor proved that his signature was taken on a blank paper, and on this basis as combined with other defects in the document, the court said that the refusal of the relief of specific performance was justified.

The right to specific performance of a buyer of property was not defeated by the fact that he added the names of two independent persons as marginal witnesses to the sale deed.<sup>224</sup>

The relief is discretionary. The *bona fides* of the person claiming this relief should be above-board. Lack of *bona fides* in any of the pleadings, be it as to the contents of the agreement, factum of payment, etc., disentitles the party from claiming relief even if the transaction is within the framework of law in other respects. The purchaser in this case paid a small amount and took possession at the time of the agreement. He did not pay anything further up to 8 years and claimed specific performance only by way of counter-claim to the owner's suit for recovering his possession. He did not even pay the court fee for his counter-claim saying that he did not have the means to pay. This showed that he had no means to pay the balance price. His conduct was not fair. He was not entitled to the equitable relief.<sup>225</sup>

221. *Her Highness Maharani Shantidevi P. Gaikwad v Savjibhai Haribhai Patel*, (2001) 5 SCC 101; AIR 2001 SC 1462.
222. *Mahabir Prasad Jain v Ganga Singh*, (1999) 8 SCC 274; AIR 1999 SC 3873. *Lalit Kumar Jain v Jaipur Traders Corpn (P) Ltd*, (2002) 5 SCC 383, the plaintiff who approaches the court with unclean hands is not entitled to any relief in equity.
223. *Shiddappa Adiveppa Jadi v Ramanna*, AIR 2002 Kant 416. *P. Purushotham Reddy v Pratap Steels Lid*, AIR 2003 AP 141, the vendee was making false pleas, not clean hands, not entitled to equitable relief.
224. *Ram Khilona v Sardar*, (2002) 6 SCC 375; AIR 2002 SC 2548; *Abdul Dadamiya Shaikh v Jagannath Murlidhar Rathi*, AIR 2002 Bom 413, no relief to a purchaser who had not paid the consideration money.
225. *B.R. Koteswara v C. Rameswari*, AIR 2002 NOC 42 (AP); 2002 AIHC 2973 (AP). *Kota Satyanarayana v Qamarunnisa Begum*, AIR 2003 AP 63, the purchaser instigated someone else to file a suit against the defendant seeking share in the same property. He also got the defendant's property attached and made her to deposit some amount and otherwise also put her into lot of trouble. Discretion exercised in favour of the plaintiff only to the extent of ordering refund of the advance amount but not for ordering specific performance, the order was not interfered with. *Sumer Chand Goel v Rakesh Kumar*, AIR 2002 All 82, the entire

*Agreement opposed to public policy.*—The court may not exercise discretion in favour of the claimant where the agreement is opposed to public policy. On the facts of the case, however, the court found that there was nothing against public policy. There was readiness and willingness. The power of attorney acting for the company was doing so within its limits. The company had clearly resolved to sell its property.<sup>226</sup>

*Object forbidden.*—An allotted plot was agreed to be transferred after receipt of a particular sum. The plot in question was not transferable for a period of 10 years. The agreement to sell was held to be not an enforceable contract. The decree passed by the High Court with the knowledge of that fact was set aside.<sup>227</sup>

#### 4. *Substantial performance by one side*

Where a party to a contract has already substantially performed his part of it, it would be highly inequitable to him if the other is not compellable to perform his part. Sub-section (3) accordingly provides that the court may properly exercise the discretion to decree specific performance in any case where the plaintiff has done substantial acts or suffered losses in consequence of a contract capable of specific performance. The old Act contained the following illustration on this point:

A sells land to a railway company, who contract to execute certain works for his convenience. The company take the land and use it for their railway. Specific performance of the contract to execute the works should be decreed in favour of A.<sup>228</sup>

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sale consideration was given to the vendor at the time of the agreement itself, possession of property was also given, seller's plea that he should be allowed to return the money because of the price rise was not accepted. *Puvvada Chiranjeeva Rao v Busi Koteswara Rao*, AIR 2012 AP 17, the vendee took possession and raised construction in breach of the contract provisions. It being a mala fide act, deprived the vendee of the right to seek specific performance. *Chodi Mahalakshmi v Koppadda Sathiraju*, AIR 2011 AP 125, the vendee falsely set up the case of full payment, no clean hands, disentitlement to specific relief. *Citadel Fine Pharmaceuticals v Ramaniyam Real Estates (P) Ltd*, (2011) 9 SCC 147: AIR 2011 SC 3351, plaintiff suppressed the material fact that the defendant vendor had returned the earnest money of Rs 10,00,000 which he refused to accept before filing his suit. This disentitled him to discretionary relief.

226. *Indian Financial Assn of Seventh Day Adventists v M.A. Unneerikutty*, (2006) 6 SCC 351: (2006) 4 KLT 520.

227. *Satish Kumar v Karan Singh*, (2016) 4 SCC 352: AIR 2016 SC 737.

228. Based on *Storer v Great Western Rly Co*, (1842) 2 Y & CCh Cas 48: 63 ER 21. *Gudurusyamala Devi v Attola Ammarvara Rao*, AIR 2002 AP 462, the agreement was entered into to pay off certain debts owed by the seller to the buyer. The plaintiff buyer cleared off the debts. Evidence showed that the agreement was intended to be acted upon. He was allowed to specifically recover the property. But no damages were allowed to him for delay in the execution of the sale deed in his favour. *Ranjana Nagpal v Devi Ram*, AIR 2002 HP 166, delay of 19 years was caused due to inaction on the part of the seller. The seller was not to be permitted to take advantage of his own inaction. Relief of specific recovery was granted though there had been considerable rise in the prices of real estates. There was a concurrent finding of fact by the lower courts that the plaintiff was all the time ready and willing to perform his part. No interference in such finding.

Where the father borrowed amount from the plaintiff to meet a family necessity and agreed to sell the land to the plaintiff on his failure to pay back the amount, and all this was proved by clear evidence, specific enforcement against the father and one son who was living in the family was allowed. One son had already gone out of the family and, therefore, no relief could be allowed against him.<sup>229</sup>

### 5. Mutuality of remedy (ready and willing)

Sub-section (4) declares that the court shall not refuse to any party specific performance of a contract merely on the ground that the contract is not enforceable at the instance of the other party. It had been a common belief in this field "that the court will not order specific performance at the suit of one party unless it could do so at the suit of the other". The Privy Council had laid down in *Mir Sarwarjan v Fakhruddin Mahomed Chowdhury*,<sup>230</sup> that a contract of purchase of land on behalf of a minor was not specifically enforceable at the instance of the minor because it could not have been enforced against him. Their Lordships said that as the minor was not bound by the contract, there was no mutuality and that consequently the minor could not obtain specific enforcement of the contract. But beginning with *Srikakulam Subrahmanyam v Kurra Subba Rao*,<sup>231</sup> the Privy Council allowed specific enforcement even in cases where there was no mutual equality. Thus the doctrine of mutuality ceased to have any force. In English law also the requirement of mutuality has been subjected to such a large number of exceptions that it has been observed in CHITTY: "the number and importance of these exceptions has given rise to a doubt as to the existence of the requirement of mutuality."<sup>232</sup> The provisions of Section 12 are sufficient in themselves to rid the law of the requirement of mutuality. That section has been further supported by this sub-section which quite clearly says that the court should not decline specific relief only because of lack of mutuality.

It is also necessary that the plaintiff should have either done his part or should be ready and willing to do his part. In the case of a transfer of property, the Supreme Court observed that a transferee of immovable property can claim specific performance of the contract only by showing his performance or willingness to perform his part of the contract.<sup>233</sup> Accordingly, where the court in granting relief under Section 16 paid no attention to

229. *Noti China Subba Reddy v Pulavarthi Rama Rao*, AIR 2003 AP 49.

230. (1911–12) 39 IA 1; (1912) 39 Cal 232 PC.

231. (1947–48) 75 IA 115; ILR 1949 Mad 141 PC.

232. ON CONTRACTS (24th Edn, 1977) 1659.

233. *Jawahar Lal Wadhwa v Haripada Chakroborty*, (1989) 1 SCC 76; AIR 1989 SC 606. *Pramod Buildings and Developers (P) Ltd v Shanta Chopra*, (2011) 4 SCC 741; AIR 2011 SC 1424, the buyer was not paying the whole balance amount and was instead asking the seller to pay the Municipal taxes, etc. The buyer being not willing to perform his obligation, his suit for specific performance was dismissed. *Shankarlal Bijreja v Ashok B Ahuja*, AIR 2011 Chh 66, instead of paying the full amount within six months as contemplated in the agreement, the buyer insisted upon delivery of possession proportionate to the amount paid, the court said that this amounted to setting up a new agreement, he was not willing to perform the original

the side of the seller and confined its findings to the purchaser's side, this was described by the Supreme Court as a serious error.<sup>234</sup> In this case the plaintiff said that he had deposited the requisite amount in a bank account and though he did not produce the passbook of his own accord no adverse inference could be drawn against him because neither the defendant nor the court had called upon him to produce the passbook. The concurrent finding of the trial court and High Court was described by the Supreme Court as contrary to the evidence and palpably unreasonable. The court did not hesitate to set aside the finding and decreed the plaintiff's suit for specific performance. The court said that the only inference that could reasonably be drawn was that the defendant wanted to defeat the claim of the plaintiff and wanted to wriggle out of the obligation undertaken by him. In another case, the High Court had refused to grant the relief of specific performance on the ground that it would be unjust to do so in view of passage of time resulting in escalation of prices and the Supreme Court did not agree with this view of the matter. The court went by the facts that the whole of the price had been paid long ago and the premises were in the possession of the purchaser in part-performance of the agreement. The case was remanded to the High Court for decision on merits.<sup>235</sup>

Where the buyer proved his being ready and willing throughout and only the seller was sheltering himself behind the provision in the agreement that in case the seller failed to perform his part, he would pay double the amount of earnest money, it was held that such clause could not lead to the inference that the buyer could not seek specific performance of the agreement to sell. Damages could not be treated as adequate compensation. The court passed decree of specific performance.<sup>236</sup>

Specific performance was not decreed where the parties were under a mutual mistake as to the identity of the land agreed to be sold. The purchaser did not cooperate with the transferor in sorting out the area to be transferred. The transferor had done some construction work on the land. He offered the other area to the purchaser which the latter did not accept. The purchaser could not get any order of directing the transferor to transfer the land to him.<sup>237</sup> Specific relief was also not granted where the transferee claimed that he had paid half the amount by cheque and the other half by cash, and the amount being huge in cash also, he was not able to offer any proof of the fact of presence of so much cash with him.<sup>238</sup>

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agreement, he was not entitled specific performance, he was entitled only to refund of the amount paid.

234. *Indira Kaur v Sheo Lal Kapoor*, (1988) 2 SCC 488: AIR 1988 SC 1074.

235. *Ajaib Singh v Gurbax Singh*, (1988) 1 SCC 143.

236. *Gopal Dass v Sonu*, AIR 2010 P&H 126; *Sumat Prakash Jain v Laxmi*, AIR 2010 Raj 63 (DB), clear provision that neither party would refuse specific of the contract relating to transfer of the disputed property, the provision for penal clause of double advance was immaterial.

237. *General Sales Ltd v Jagdish Rana*, AIR 2003 HP 90.

238. *M.V. Prema Chandra v Sarojamma*, AIR 2015 Kar 1.

## Protecting interest of vendor

In respect of an agreement to purchase immovable property, it was proved that the purchaser had been in possession for several years and had also been enjoying the usufruct of the property. The court accordingly ordered maintenance of status quo; but directed the purchaser to deposit in the trial court a fixed amount annually in order to protect the interest of the vendor. The suit may then be finally disposed of in favour of the transferee.<sup>239</sup> A lady buyer was not able to prove that she had been all along ready and willing to perform her side of the bargain. But her family members had been living in the property for more than 30 years in their own right. They could not therefore be forced to vacate the property. In the interest of justice, the court directed her to pay Rs 60,000 to the plaintiff inclusive of advance paid by her.<sup>240</sup>

## Limitation

The contract for transfer of property stipulated a time-period for payment of full consideration and registration of sale deed. The transferee made only part payment and that too after expiry of the stipulated date, but the transferor accepted it without stipulating any further date. The court said that limitation would start from the date of refusal by the vendor in response to the notice by the vendee of specific enforcement and not from the date stipulated in the agreement.<sup>241</sup>

Though the prescribed period of limitation is three years, the court said that courts have power to dismiss a suit even before three years if it is found that in the interregnum between the date of agreement and the date of suit, certain events, such as steep increase in prices of property, etc. have taken place. The time stated in the agreement for completion also assumes its importance. A very short period for completion was stipulated. In such a case the party cannot be permitted to wait for three years and file the suit at leisure. The court could ignore the fact that property was agreed to be sold because of acute necessity.<sup>242</sup>

The question as to bar of limitation is not a pure question of law. It cannot be decided as a preliminary issue.<sup>243</sup>

239. *Sukkha Singh v Mahal Singh*, AIR 2003 Raj 21.

240. *Azhar Sultana v B Rajamani*, (2009) 17 SCC 27; AIR 2009 SC 2157.

241. *Dutta Seethamalakshamma v Yanamadala Balaramaiah*, AIR 2003 AP 430.

242. *Puvvada Chiranjeeva Rao v Busi Koteswara Rao*, AIR 2012 AP 17; *S. Kanaka Durga Manikyhumma v Ramapragda Surya Prakasa Rao*, AIR 2010 AP 99, the suit was filed after lapse of 12 years from the date of agreement to sell. The seller had at that time no title and the purchaser knew that he was only a tenant. Subsequently he acquired title. The purchaser could not make any use of it because of the time-bar. *Jagdev Singh v Gursewak Singh*, AIR 2016 NOC 231 (P&H), initially the suit was filed for recovery of earnest money, subsequently relief by way of possession by specific performance was sought to be added, this was after three years, barred by limitation.

243. *Taj Kerala Hotels & Resorts Ltd v Easystec India (P) Ltd*, AIR 2014 Ker 9.

### *Limitation for execution of decree*

In a compromise decree execution proceedings were not filed in the same court which passed the decree. As per the terms of the agreement the decree was executable within one month. The decree holder sought execution after more than four years. The judgment debtor objected because of limitation. It was held that the proceedings were liable to be dismissed because the executing court had no power to extend time for execution of the compromise decree.<sup>244</sup>

### **Pre-emptive orders under tax measures**

Where there is a pre-emptive order under a taxing measure about some property, it has the effect of vesting the property in the Government. Such an order does not become set aside by the filing of a civil suit. Relief about the sale of such property cannot be granted automatically. So long as the order remains in force, no title can be conveyed. The Act applies to transfers by acts of parties and not to vesting of rights under statutory operations.<sup>245</sup>

### *Amendment of plaint*

In a suit for declaration of title and injunction, there was omission to claim relief of specific performance of agreement to sell. The court said that it amounted to relinquishment of that part of the claim. Subsequent inclusion of the plea of specific performance by way of amendment after eleven years of the suit was not allowed, being barred by limitation under Article 54 of the Limitation Act.<sup>246</sup>

### **Nature of jurisdiction under the Act**

The nature of jurisdiction under the Act has been held to be legal and equitable. This observation of the Supreme Court occurred in a case in which a person entered into a contract of sale of land. His sons, who were already major, opposed the suit for specific performance saying that they were joint-owners and they were neither consulted nor even informed of the transaction. But the vendee stated before the court orally that one of the sons had participated in the negotiations. The Supreme Court did not believe the sons to say that they had no knowledge of things when negotiations for sale and execution of documents took place, they being not children at the time. There was no equity in their favour because even after the suit they did not approach the Authorities under the U.P. Consolidation of Holdings Act, 1953 for having their names recorded as joint owners. Such Authorities had exclusive jurisdiction for that purpose.<sup>247</sup>

244. *Md Hanif Khan v Naresh Prasad*, AIR 2010 Jhar 73.

245. *Deepak Prakash v Jayanta Kumar Bose*, AIR 2003 Cal 153.

246. *Van Vibhag Karamchari Griha Nirman Sahkari Sanstha Maryadit v Ramesh Chander*, (2010) 4 SCC 596; AIR 2011 SC 41.

247. *Narender Singh v Jai Bhagwan*, (2005) 9 SCC 157; AIR 2005 SC 582; 2005 All LJ 289.

No relief was sought for declaration of title to property or for possession of property. The suit was for specific performance simpliciter and not suit for land. It was held that the suit was triable by the Calcutta High Court even if the premises agreed to be assigned by way of lease were situated outside the territorial limit of the court. The return of the plaint was not proper.<sup>248</sup>

The court does not lose jurisdiction after grant of decree of specific performance in view of Section 28(1) of the Act. The seller applied for rescission of the decree. The decree holder deposited the balance amount in the bank to show his *bona fides* as a purchaser. The seller applied for extension of time about his application for rescission. Extension was granted to him. Such enlargement of time was held to be proper.<sup>249</sup>

#### *Impleadment (addition of party)*

In a suit for specific performance, a third party-stranger asserted that she was in possession of the disputed property. The court said that such rights could not be adjudicated in a suit for specific performance. A stranger is neither necessary nor a proper party for effective adjudication of such suit.<sup>250</sup>

#### Power of court to award compensation [S. 21]

**S. 21. Power to award compensation in certain cases.**—(1) In a suit for specific performance of a contract, the plaintiff may also claim compensation for its breach, either in addition to, or in substitution of, such performance.

(2) If, in any such suit, the court decides that specific performance ought not to be granted, but that there is a contract between the parties which has been broken by the defendant, and that the plaintiff is entitled to compensation for that breach, it shall award him such compensation accordingly.

(3) If, in any such suit, the court decides that specific performance ought to be granted, but that it is not sufficient to satisfy the justice of the case, and that some compensation for breach of the contract should also be made to the plaintiff, it shall award him such compensation accordingly.

(4) In determining the amount of any compensation awarded under this section, the court shall be guided by the principles specified in Section 73 of the Indian Contract Act, 1872 (9 of 1872).

(5) No compensation shall be awarded under this section unless the plaintiff has claimed such compensation in his plaint:

Provided that where the plaintiff has not claimed any such compensation in the plaint, the court shall, at any stage of the proceeding, allow him to amend the plaint on such terms as may be just, for including a claim for such compensation.

*Explanation.*—The circumstance that the contract has become incapable of specific performance does not preclude the court from exercising the jurisdiction conferred by this section.

248. *Niligiri Estates (P) Ltd v Khaniva Housing (India) (P) Ltd*, AIR 2012 Cal 60.

249. *Dilip Kumar Patro v M. Gopikrishna Rao*, AIR 2015 Ori 15.

250. *Lakshmamma v P.K. Jayachandra*, AIR 2015 NOC 1037 (Kar).

### Compensation in addition to or substitution of specific performance

Every party seeking the relief of specific performance is allowed by this Section to claim compensation for the breach of the contract. Such relief may be claimed either in addition to specific performance or in substitution of it. If the court is of opinion that specific performance ought not to be ordered, the court may award compensation if a valid contract and its breach are established.<sup>251</sup> Should the court find that specific performance by itself would not be sufficient relief, it may, in addition, award compensation also to meet the ends of justice. Compensation would be assessed in accordance with the principles stated in Section 73 of the Contract Act. Even where the contract has become incapable of specific enforcement, the court can exercise the power under this section to award compensation. In a case where reconveyance was refused, the court on ordering the same, observed as follows: "When the plaintiff by his option has made specific performance impossible, Section 21 does not entitle him to seek damages. Where the contract, for no fault of the plaintiff, becomes impossible of performance Section 21 enables the award of compensation in lieu and substitution of specific performance." The court continued: "So far as the proviso to sub-section (5) of Section 21 is concerned, two positions must be kept clearly distinguished. If the amendment relates to the relief of compensation in lieu of or in addition to specific performance where the plaintiff has not abandoned his relief of specific performance the Court will allow the amendment at any stage of the proceeding. That is a claim for compensation falling under Section 21 of the Specific Relief Act, 1963 and the amendment is one under the proviso to sub-section (5). But different and less liberal standards apply if what is sought by the amendment is the conversion of a suit for specific performance into one for damages for breach of contract in which case Section 73 of the Contract Act is invoked. This amendment is under the discipline of Rule 17, Order 6, CPC. The fact that sub-section (4), in turn, invokes Section 73 of the Contract Act for the principles of quantification and assessment of compensation does not obliterate this distinction."<sup>252</sup>

The measure of compensation is by the standards of Section 73 of the Indian Contract Act. Dealing with the facts, the court said: "In the present case assuming that the respondent had not actually sought the amendment

251. *Jai Narain Parasrampuria v Pushpa Devi Saraf*, (2006) 7 SCC 756, promoters contracted to buy property for the company before incorporation. The company after incorporation adopted the contract and informed the vendor. But afterwards, vendors changed their mind and refused to sell. This provoked frivolous litigation between both parties. Either party being equally guilty of misconduct, the court refused to grant specific performance to the company to which it was otherwise entitled. Instead compensation of Rs 50 lakhs and refund of earnest money with 12 per cent interest was allowed.

252. *Harjeet Singh v Amrik Singh*, (2005) 12 SCC 270, no compensation was allowed to a person who had not been ready and willing to do his part. *Rizvi Builders v Lamarck R.C. Clemente*, AIR 2015 Bom 192, no compensation where the contract was not yet formed and no loss was shown to have been caused.



of plaint for compensation in lieu of specific performance, the amendment was hereby permitted so that complete justice could be done. The quantum of compensation is ascertainable with reference to the determination of the market value in the land acquisition proceedings. The compensation awarded may safely be taken to be the measure of damages, subject, of course, to the deduction therefrom of money value of the services, time and energy expended by the appellant in pursuing the claims of compensation and the expenditure incurred by him in the litigation culminating in the award. Accordingly, there will be a decree awarding to the respondent compensation in lieu and substitution of one for specific performance which, but for the acquisition, the respondent would have been entitled to the quantum and the measure of the compensation being the entire amount of compensation determined for the acquisition of the suit properties together with all the solatium, accrued interest and all other payments under the law authorising the acquisition, less a sum of Rs 1,50,000 which was to go to the appellant towards his services, time and amounts spent in pursuing the claims for compensation as well as the consideration stipulated for reconveyance.”<sup>253</sup>

It is necessary that the plaintiff should have asked for the relief of compensation. The court may, however, allow the plaint to be amended at any stage to enable the plaintiff to claim compensation.<sup>254</sup>

Where, for example, a buyer of land is allowed to recover it specifically and it takes him about a year to get the relief, the court may award compensation for the loss of time. The following four illustrations appeared under the earlier 1877 Act:

- (1) A contracts to sell a hundred maunds of rice to B. B brings a suit to compel A to perform the contract or to pay compensation. The Court is of opinion that A has made a valid contract and has broken it, without excuse, to the injury of B, but that specific performance is not the proper remedy. It shall award to B such compensation as it deems just.
- (2) A contracts with B to sell him a house for Rs 1000, the price to be paid and the possession given on the 1st January, 1877. A fails to perform his part of the contract, and B brings his suit for specific performance and compensation, which is decided in his favour on the 1st January, 1878. The decree may, besides ordering specific performance, award to B compensation for the loss which he has sustained by A's refusal.
- (3) A, a purchaser, sues B, his vendor, for specific performance of a contract for the sale of a patent. Before the hearing of the suit the patent expires. The court may award A compensation for the non-performance of the contract, and may, if necessary, amend the plaint for that purpose.
- (4) A sues for the specific performance of a resolution passed by the Directors of a public company, under which he was entitled to have certain shares allotted to him, and for compensation for the non-performance of the resolution. All the shares had been

253. *Jagdish Singh v Natthu Singh*, (1992) 1 SCC 647: AIR 1992 SC 1604.

254. *Jhandoo v Ramesh Chandra*, AIR 1971 All 189, Cited in *Rajendra Kantilal Dalal v Bombay Builders Co (P) Ltd*, AIR 2002 Bom 408, compensation was awarded to the plaintiff against the second buyer because he had purchased the property with full knowledge that the property had already been sold to the plaintiff and he did so *mala fide* with a view to defeat the plaintiff's title.

allotted before the institution of the suit. The court may, under this section, award A compensation for the non-performance. [Based on *Ferguson v Wilson*.<sup>255</sup>]

### Order for delivery of goods

The court can issue a direction for delivery of goods despite there being an alternative plea for damages. On the facts of this particular case,<sup>256</sup> the court said:

“In case of non-delivery of goods, where there was an alternative plea for damages, court may not direct delivery of the goods (Units of UTI) after their purchase from open market along with benefit of rights issue. Instead the court can compensate the plaintiff with return of the money paid by him with interest and award of reasonable damages.”

An agreement was entered into for sale of units of UTI by the appellant to the respondent. Payments by way of consideration for purchase of the units were made by the respondent to the appellant and banker's receipt was issued by the appellant in respect of the said transaction. But units were not delivered by the appellant. By a letter dated 1 July 1992 the respondent claimed compensation for breach of contract treating the same to have taken place on 30 May 1992 and on that basis it claimed difference in price between the rate that was paid and the rate of UTI as on 30 May 1992. Since no amount was paid by the appellant, a suit was filed by the respondent claiming delivery of the units in respect of which payments had been made. An alternative prayer was also made for payment of a certain amount as damages plus further interest at 17.5 per cent p.a. on the said amount till the date of payment. The Special Court constituted under the Special Court Act of 1992 granted relief of specific performance requiring the appellant to buy the units for which payment had been made and also to purchase and sell to the respondent the units representing the right issue which the respondent was deprived of availing because of the non-delivery of the units. Costs of Rs 27,87,000 were also awarded. Disposing of the appeal, the Supreme Court said: “The appellant admits that the respondent, to whom delivery of the units was not made, would be entitled to the refund of the money plus damages thereon calculated in accordance with the principles contained in Section 73 of the Indian Contract Act, 1872. Considering the fact that there was an alternative plea for damages, on the facts of the present case a decree for specific performance in the manner in which it was passed was probably not appropriate especially when the respondent could be compensated with the return of money and award of reasonable damages.”

255. (1866) LR 2 Ch App 77. *K. Narendra v Riviera Apartments (P) Ltd*, (1999) 5 SCC 77: AIR 1999 SC 2309, Agreement, on facts having become incapable of performance, compensation equal to the amount of price already received by the vendor, directed to be paid to the vendee by the vendor in addition to the refund of the amount received. Interest directed to be paid on the amount of compensation from the date of decision and on the refundable amount, from the date the vendor had received the same.

256. *State Bank of Saurashtra v P.N.B.*, (2001) 5 SCC 751: AIR 2001 SC 2412.

### Loss of right to compensation

The right to sue for compensation is lost where the suit for specific performance is dismissed in whole or in part, but other rights, if any, will survive. This is the effect of Section 24.

**S. 24. Bar of suit for compensation for breach after dismissal of suit for specific performance.**—The dismissal of a suit for specific performance of a contract or part thereof shall bar the plaintiff's right to sue for compensation for the breach of such contract or part, as the case may be, but shall not bar his right to sue for any other relief to which he may be entitled, by reason of such breach.

### Relief of possession, partition, etc. [S. 22]

Where the relief sought is for the transfer of immovable property, the court may also grant, if so prayed by the party, relief by way of possession, partition and separate possession. The court may also grant any other relief, such as refund of earnest money or deposit paid in case specific performance is refused. Where the party has not made any such prayer in the original plaint, the court may permit amendment of the plaint.<sup>257</sup>

**S. 22. Power to grant relief for possession, partition, refund of earnest money, etc.**—(1) Notwithstanding anything to the contrary contained in the Code of Civil Procedure, 1908 (5 of 1908), any person suing for the specific performance of a contract for the transfer of immovable property may, in an appropriate case, ask for—

- (a) possession, or partition and separate possession, of the property, in addition to such performance; or
- (b) any other relief to which he may be entitled, including the refund of any earnest money or deposit paid or [made by] him, in case his claim for specific performance is refused.

(2) No relief under clause (a) or clause (b) of sub-section (1) shall be granted by the court unless it has been specifically claimed:

Provided that where the plaintiff has not claimed any such relief in the plaint, the court shall, at any stage of the proceeding, allow him to amend the plaint on such terms as may be just for including a claim for such relief.

(3) The power of the court to grant relief under clause (b) of sub-section (1) shall be without prejudice to its powers to award compensation under Section 21.

### *Relief for possession has to be pleaded (alternative relief)*

Relief of possession can be granted only if it is specifically prayed for.<sup>258</sup>

Sub-section (1) of Section 22 of the Specific Relief Act, 1963 is an enabling provision. A plaintiff in a suit for specific performance may ask for further

257. The section is an enabling provision, *Adcon Electronics (P) Ltd v Daulat*, (2001) 7 SCC 698: AIR 2001 SC 3712.

258. *Lavinder Kumar Sharma v Pramod Kumar*, AIR 2011 P&H 30, the alternative relief of possession, partition, refund of earnest money, etc. can be granted only when specifically pleaded.

reliefs mentioned in clauses (a) and (b) thereof. Clause (a) contains reliefs of possession and partition and separate possession of the property, in addition to specific performance. The mandate of sub-section (2) of Section 22 is that no relief under clauses (a) and (b) of sub-section (1) shall be granted by the court unless it has been specifically claimed. Thus it follows that no court can grant the relief of possession of land or other immovable property, subject-matter of the agreement for sale in regard to which specific performance is claimed, unless the possession of the immovable property is specifically prayed for.

Where an execution of sale deed was made in favour of the plaintiff by process of the court itself, it was held that the onus upon the court became further extended to ensure delivery of possession through execution proceedings for the purpose of satisfying the decree. Even if there was no prayer for delivery of possession in terms of Section 22, the decree holder was entitled to be in possession of the demised property.<sup>259</sup>

In the instant case the suit is for specific performance of the agreement for sale of the suit property wherein relief of delivery of the suit property was not specifically claimed, as such it could not be treated as a "suit for land". It was not possible to accept the contention that in the present case the suit was for acquisition of title to the land and is a "suit for land". In its true sense, a suit simpliciter for specific performance of a contract for sale of land is a suit for enforcement of the terms of a contract. The title to the land as such is not the subject-matter of the suit.<sup>260</sup>

#### *Refusal of relief*

Where the property in question was transferred by a co-sharer whose share was very small and it was not possible to direct specific performance of the entire property as it could not be divided into small shares, it was held that exercise of discretion by the trial court in not decreeing the suit even to the extent of the selling co-sharer's share was proper and was not to be interfered with.<sup>261</sup>

In such cases generally the alternative relief of refund of money paid to the seller is allowed with interest.<sup>262</sup>

#### *Alternative relief*

In a claim for specific performance of an agreement to sell, the defendant proved that he never intended to sell the property in question because the

259. *Sunita Devi v Dinbandhu Shah*, AIR 2010 Jhar 151; *Krishnamurthy Gounder v Venkatakrishnan*, AIR 2012 Mad 105, the decree was silent about delivery of possession. But once specific performance is allowed, possession should be granted, whether pleaded or not.

260. *Adcon Electronics (P) Ltd v Daulat*, (2001) 7 SCC 698: AIR 2001 SC 3712; *P.C. Varghese v Devaki Amma Balambika Devi*, (2005) 8 SCC 486, the relief for partition or exclusive possession can be granted in addition to the main relief of specific performance.

261. *Khanderao Subbarao Nadagir v Hulagavva*, AIR 2003 Kant 354.

262. *Sarita Dokania v Krishna Dey*, (2014) 13 SCC 522: (2013) 3 Cal LJ 153.

intention was to provide the property as a security for a loan. The court said that it could grant the alternative relief of repayment of the loan amount to the plaintiff lender. Section 22 enables the court to take into its fold the relief of return of the amount lent.<sup>263</sup>

#### *Amendment of plaint*

An amendment of plaint was sought for including prayer for return of advance money with interest. The court said that the amendment was covered by Section 22(2) and not Order 6, Rule 17, CPC. The plaintiff was entitled to amend his pleadings at any stage of the proceedings.<sup>264</sup>

The plaintiff failed to pray for relief of possession, nor any decree for possession was passed. The court said that the plaintiff could be allowed to amend his plaint for including prayer of possession at any stage including execution. This was necessary to avoid multiplicity of proceedings and advance the cause of justice.<sup>265</sup>

#### **Liquidation of damages no bar [S. 23]**

Where the parties to the contract have fixed the amount of compensation which would be payable in the event of default, this would not constitute any bar to the relief of specific performance. The court may examine the circumstances of the case. If they show that compensation was fixed in order to secure performance and not to allow the defaulting party an option to pay compensation, the court may allow specific performance. Where, on facts, the plaintiff-respondent was found ready, willing and able to perform his part of the agreement for the sale of orchard, it was held that such plaintiff was entitled to specific performance despite the existence of a penalty clause providing for payment of Rs 10,000 by the party violating the terms and conditions of agreement. The Division Bench of the High Court rightly dismissed the appeal of the appellant-Defendant 1 vendor.<sup>266</sup> The court cannot, however, in the same decree order the payment of the fixed amount also.

The Act of 1877 carried this power under Section 20 and had the following illustration:

A contracts to grant B an under-lease of property held by A under C, and that he will apply to C for a licence necessary to the validity of the under-lease, and that, if the licence is not granted, A will pay B Rs 10,000. A refuses to apply for the licence and offers to pay B the Rs 10,000. B is nevertheless entitled to have the contract specifically enforced if C consents to give the licence.

#### **Earnest money**

An agreement for sale of property did not contain any stipulation for forfeiture of earnest money or advance made towards sale consideration.

263. *Laxman Haraklal v Ukhaji Zinga Mahajan*, AIR 2011 Bom 159.

264. *Rajesh Kumar Choudhari v Darshansingh Sardar*, AIR 2011 Chh 179.

265. *M. Palanisamy v Valmoorty*, AIR 2010 NOC 557 (Mad).

266. *Manzoor Ahmed Magray v Ghulam Hassan Aram*, (1999) 7 SCC 703: AIR 2000 SC 191.

The vender did nothing further which could be regarded as steps towards performance. He was ordered to refund the amount with 6 per cent simple interest from date of suit.<sup>267</sup>

### Alternative relief provided in contract

Where the agreement (for sale of agricultural land) itself providing for contingencies of (i) seller refusing to sell and (ii) purchaser refusing to buy by stipulating the return of earnest money plus another sum in either circumstance, it was held, that on facts, there was no obligation on the seller to complete the sale transaction and the contract could not be specifically enforced. The High Court erred in upholding the decree of specific performance awarded by the first appellate court.<sup>268</sup>

Even otherwise the plea of alternative relief of refund of earnest money and damages cannot by itself be a bar to claim the decree of specific performance.<sup>269</sup>

### Enforcement of arbitral awards and direction to execute settlements

Section 25 of the Act provides that the provisions of this chapter (*i.e.* Chapter II) shall apply to awards to which the Arbitration Act, 1940 does not apply and to directions in a will or codicil to execute particular settlement. (Now the Arbitration and Conciliation Act, 1996)

## RESCISSIION OF CONTRACTS

The rescission of contract necessarily constitutes a bar to its performance by either of the party to it (Fry: Chapter XXIV). The grounds for bringing a suit for rescission have been given in Sections 27 and 28 of the Specific Relief Act, 1963:

**S. 27. When rescission may be adjudged or refused.**—(1) Any person interested in a contract may sue to have it rescinded, and such rescission may be adjudged by the court in any of the following cases, namely:—

- (a) where the contract is voidable or terminable by the plaintiff.
- (b) where the contract is unlawful for causes not apparent on its face and the defendant is more to blame than the plaintiff.

(2) Notwithstanding anything contained in sub-section (1), the court may refuse to rescind the contract—

- (a) where the plaintiff has expressly or impliedly ratified the contract; or
- (b) where, owing to the change of circumstances which have taken place since the making of the contract (not being due to any act of the defendant himself), the parties cannot be substantially restored to the position in which they stood when the contract was made; or

267. *Vishalkumar Nemichand Kakad v Shankar Mahadeo Kubde*, AIR 2009 NOC 258 Bom.

268. *Dadarao v Ramrao*, (1999) 8 SCC 416.

269. *P.C. Varghese v Devaki Amma Balambika Devi*, (2005) 8 SCC 486.

- (c) where third parties have, during the subsistence of the contract, acquired rights in good faith without notice and for value; or
- (d) where only a part of the contract is sought to be rescinded and such part is not severable from the rest of the contract.

*Explanation.*—In this section “contract”, in relation to the territories to which the Transfer of Property Act, 1882, does not extend, means a contract in writing.<sup>270</sup>

### *When rescission available*

The relief of rescission comes handy to a person who has become the victim of an imposition by means of a contract. This burden of a contract has been imposed upon him by means of a fraud or illegality or something equivalent which makes the contract either void or voidable. He may ask the court that the contract should be declared as not binding upon him. This is rescission, that is, getting rid of a contract. Section 27 accordingly provides that the court may allow the relief of rescission in the following cases:

- (1) Where the contract is voidable or terminable by the plaintiff;
- (2) where the contract is unlawful for causes not apparent on its face and the defendant is more to blame.

### *Loss of right of rescission*

The relief of rescission is available subject to very important limits. This is so because every voidable contract is valid as long as it is not avoided. If the relief of rescission is not quickly obtained, circumstances may so seriously change that it may then not be desirable to put an end to the contract. Sub-section (2) accordingly provides that the right of rescission is not available in the following cases:

#### *1. Affirmation*

The plaintiff loses the right of rescission when on becoming aware of his right he chooses to ratify the contract. Once the contract is affirmed it cannot afterwards be avoided. Affirmation may be express or implied. An express affirmation takes place when the right to rescind is openly waived. An implied affirmation takes place when the party having the right to rescind is instead enjoying the benefits of the contract.

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270. This section corresponds with S. 35 of the repealed Specific Relief Act, 1877. That section carried the following illustrations:

*Illustration as to sub-section (1)(a).*—A sells a field to B. There is a right of way over the field of which A has direct personal knowledge, but which he conceals from B. B is entitled to have the contract rescinded.

*Illustration as to sub-section (1)(b).*—A, an attorney, induces his client, B, a Hindu widow, to transfer property to him for the purpose of defrauding B's creditors. Here the parties are not equally in fault, and B is entitled to have the instrument of transfer rescinded.

## 2. Where restitution not possible

The right of rescission is also lost where the position of the parties has been altered to such an extent that they cannot be put back to their original status. Where one party has already resold the goods or consumed them, restoration of the *status quo ante* becomes impossible.

The transferee obtained possession of the property in part performance of the contract. The court said that possession over property was to be protected even if the period of limitation for bringing a suit for specific performance had expired. The transferee was required to fulfil the necessary conditions in order to defend and protect his possession. The Limitation Act does not extinguish defences. It only bars the remedy.<sup>271</sup>

## 3. Intervention of third parties

Where the rights of third parties have intervened, rescission cannot be allowed to the prejudice of such rights. Where, for example, a person has obtained goods by fraud and, before the seller is able to catch him, he transfers the goods to a *bona fide* buyer, the deceived seller would not now be allowed to get rid of the sale on account of the fraud.

## 4. Severance

Rescission is not allowed where the plaintiff is seeking rescission of only a part of the contract and that part is not severable from the rest of the contract.

**S. 28. Rescission in certain circumstances of contracts for the sale or lease of immovable property, the specific performance of which has been decreed.**—(1) Where in any suit a decree for specific performance of a contract for the sale or lease of immovable property has been made and purchaser or lessee does not, within the period allowed by the decree or such further period as the court may allow, pay the purchase money or other sum which the court has ordered him to pay, the vendor or lessor may apply in the same suit in which the decree is made, to have the contract rescinded and on such application the court may, by order, rescind the contract, either so far as regards the party in default or altogether, as the justice of the case may require.

(2) Where a contract is rescinded under sub-section (1), the court—

- (a) shall direct the purchaser or lessee, if he has obtained possession of the property under the contract, to restore such possession to the vendor or lessor, and
- (b) may direct payment to the vendor or lessor of all the rents and profits which have accrued in respect of the property from the date on which possession was so obtained by the purchaser or lessee until restoration

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271. *Shrimant Shamrao Suryavanshi v Pralhad Bhairoba Suryavanshi*, (2002) 3 SCC 676: AIR 2002 SC 960.

of possession to the vendor or lessor, and, if the justice of the case so requires, the refund of any sum paid by the vendee or lessee as earnest money or deposit in connection with the contract.

(3) If the purchaser or lessee pays the purchase money or other sum which he is ordered to pay under the decree within the period referred to in sub-section (1), the court may, on application made in the same suit, award the purchaser or lessee such further relief as he may be entitled to, including in appropriate cases all or any of the following reliefs, namely:—

- (a) the execution of a proper conveyance or lease by the vendor or lessor;
- (b) the delivery of possession, or partition and separate possession, of the property on the execution of such conveyance or lease.

(4) No separate suit in respect of any relief which may be claimed under this section shall lie at the instance of a vendor, purchaser, lessor or lessee, as the case may be.

(5) The costs of any proceedings under this section shall be in the discretion of the court.

### Inbuilt remedy of rescission in decree of specific performance

Section 28 enables the court to put an inbuilt remedy of rescission in a decree of specific performance. Where a decree of specific performance has been passed in respect of a contract for the sale or lease of immovable property, but the party to whom such relief has been granted does not pay the price within the time delimited, the seller may ask the court for rescission. The court will direct the purchaser or lessee, if he has already taken over possession, to restore it to the seller and also to pay him rent for the period during which he enjoyed the benefits of possession. Where justice so requires the court may order refund of the earnest money, if any, paid by the vendee or lessee. Where, on the other hand, the vendee or lessee has deposited the money as directed by the court, he may be allowed any relief as may seem just to the court in the circumstances.<sup>272</sup>

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272. Relief was allowed even where the deposit was late but it was made during the pendency of the appeal. The court retains control over the matter even after the passing of the decree, *Ramankutty Guptan v Avara*, (1994) 2 SCC 642: AIR 1994 SC 1699. *V.S. Palanichamy Chettiar Firm v C. Alagappan*, (1999) 4 SCC 702: AIR 1999 SC 918, application to the execution court for extension of time. *M. Mohammad Aslam v C.N.A. Gowthaman*, AIR 2003 Mad 248, no rescission allowed where the purchaser paid the balance consideration money as ordered by the court. *P.R. Yelumalai v M.M. Ravi*, (2015) 9 SCC 52: (2015) 4 SCC (Civ) 309, the decree holder did not deposit the balance sale consideration within the time stipulated, nor in the manner stipulated by the court in the conditional decree. He delayed payment by one day even after extension of time. He could not seek execution of the decree which had ceased to exist because of the deemed dismissal of the suit. *T.L. Rajagopal v S.N. Shivakumar*, AIR 2015 NOC 433 (Kar), enormous delay in payment, rescission allowed. *Vinayan v Radhakrishnan*, AIR 2016 NOC 216 (Ker), vendee failed to deposit sale consideration within the prescribed period and admitted that he did not have funds for the purpose. Vendor entitled to rescission. But he had to refund the deposit amount with 7.5 per cent interest because he was having the property and deposit with him.

*Contract not automatically extinguished on decree of specific performance*

The contract between the parties is not extinguished on passing of decree of specific performance. The court does not lose its jurisdiction, nor does it become *functus officio*. The decree of specific performance is in the nature of a preliminary decree. The suit is deemed to be pending even after the grant of such decree. The court retains its control over the entire matter even after the decree. Section 28 itself is indicative of such a consequence. The court has power to enlarge time in favour of the decree holder to enable him to pay the amount or to perform the conditions mentioned in the decree. There was no default clause in the decree in the sense that if the conditions were not satisfied within a certain time, it could be avoided. The decree holder had, during the course of the proceedings stretching over 24 years, paid the entire premium amount and large sums in respect of accrued rents. It could not be said that he, being the lessee, intended to abandon the agreement. He was directed to pay the balance amount within 30 days on which the lessor was to execute the lease deed.<sup>273</sup>

Where there was no outer limit for payment of balance amount of the price and on the asking of the court the purchaser deposited the balance amount in the court and it was found that the vendors were not carrying out their part of the agreement, the remedy of rescission was not allowed to such vendors.<sup>274</sup>

The court which passes a decree for specific performance retains control over the decree. But the parties cannot deviate from the terms of the decree. Proceedings for execution of decree do not fall within the expression "pendency of suit". The suit attained finality as no appeal was preferred. During the pendency of execution proceedings, the judgment debtor sold away the suit property. The court said that this did not amount to assignment or creation of any interest during the pendency of a suit. No leave of the court was obtained before purchasing the property. The purchaser was not allowed to be impleaded as a party to execution proceedings.<sup>275</sup>

273. *Kumar Dharendra Mullick v Tivoli Park Apartments (P) Ltd*, (2005) 9 SCC 262. *Susheela Devi v Maharshi Commerce Ltd*, AIR 2010 NOC 819 (AP), rescission can be ordered for non-deposit of any other sum ordered by the court, not necessarily the balance amount of consideration. The plaintiff (buyer) was directed to deposit costs of stamp papers, expenses of registration and other incidental charges within one month. Refusal to grant relief of rescission on deposit of such amounts was held to be improper. *Khoobiram v Urmilla Chauhan*, AIR 2010 MP 211, there was no direction to the decree holder in the decree to pay the balance consideration within two months, it was for the other party to receive the balance and to execute sale deed. There was no default on the part of the decree holder within the meaning of S. 28.

274. *S.K. Gupta v Kuldeep Singh*, AIR 2011 Del 54.

275. *Mahfooz Ahmed v Neelmani*, AIR 2010 MP 165.

### *Extension of time for payment under decree*

The decree was signed and sealed on a particular date under which the decree holder was given about three weeks' time to pay under the decree. His application for extension of time was dismissed on the same day. Such order of dismissal was held to be erroneous.<sup>276</sup>

### *Limitation*

An application for rescission ought to be filed within 3 years from the date of the decree for specific performance. The cause of action commences from the date of decree, and not from the date of dismissal of application filed by the vendee for extension of time to pay the decretal amount. But, even after dismissing the petition for rescission of contract as time-barred, a direction to the vendee for deposit of the sale consideration alongwith interest would be lawful.<sup>277</sup>

For execution of proper conveyance by vendor and delivery of possession, the precondition for the plaintiff is to pay the balance purchase money within the time mentioned in Section 28(1). There was failure on the part of the plaintiff-purchaser to deposit the balance sale consideration in court. He made a false averment in the affidavit as to have paid the balance consideration. He played fraud on the court. He became disentitled to relief of execution under Section 28(3). The vendor became entitled to get the contract rescinded.<sup>278</sup>

### *Appealable order*

An order under Section 28 for rescinding an agreement amounts to a decree. An appeal lies against such order and not revision.<sup>279</sup>

### *Alternative prayer for rescission in suit for specific performance [S. 29]*

As provided by Section 29 of the Specific Relief Act, 1963, the plaintiff may in a suit for specific performance make a prayer that if such relief cannot be granted, the contract may be rescinded. He has to make delivery of the instrument for being cancelled.

But the converse is not true. So, the prayer for the rescission of the contract or, in the alternative, for a decree of specific performance is not permissible.<sup>280</sup>

**S. 29. Alternative prayer for rescission in suit for specific performance.**—A plaintiff instituting a suit for the specific performance of a contract in writing may pray in the alternative that, if the contract cannot be specifically

276. *Most Parwati Devi v Mahabir Mahto*, AIR 2015 Jhar 87.

277. *B.V. Gururaj v M R Rathindran*, AIR 2010 Mad 129.

278. *Kaniyattil Ummakulsumma v P.T. Vijaya Kumar*, AIR 2015 Ker 289.

279. *NVSM Anandvale v K.T. Santhanakrishnan*, AIR 2010 Mad 204; Ss. 96, 2(2) and Order 41, Rule 1.

280. Fry, SPECIFIC PERFORMANCE, S. 1058 (5th Edn).

enforced it may be rescinded and delivered up to be cancelled; and the court, if it refuses to enforce the contract specifically, may direct it to be rescinded and delivered up accordingly.

### Extension of time

Where the court, while ordering specific performance in favour of the plaintiff, directed him to pay the balance amount within a specified date and that, on his failure to do so, his case would be dismissed, it was held on his failure to do so, that the court could grant him extension of time.<sup>281</sup>

### Rescission and equity

Section 30 lays down that the court may require parties rescinding to do equity. It provides:

**S. 30. Court may require parties rescinding to do equity.**—On adjudging the rescission of a contract, the court may require the party to whom such relief is granted to restore, so far as may be, any benefit which he may have received from the other party and to make any compensation to him which justice may require.

It is a maxim of law that “he who seeks equity must do equity” in the transaction in respect of which relief is sought. So while decreeing rescission the court might direct not only payment of compensation to the defendant but also restoration of any benefit received by the plaintiff under the contract.

A party seeking specific relief may at the same time ask that if specific performance cannot be allowed, the contract may be ordered to be rescinded. If the court refuses one relief, it may order the other.

The Supreme Court has been of the opinion that while dealing with an application under Section 28(1) for rescission of contract in a case in which the relief of specific performance has been earlier allowed, the court does not cease to have jurisdiction over the matter. The court retains control over the decree even after the decree has been passed. It is open to the court to exercise power under Section 28(1) either for extension of time or for rescinding the contract.<sup>282</sup>

Where the purchaser deposited the money in the court as directed by the court, he was not allowed to withdraw it without first applying to the court for a direction to the vendor to execute the sale deed, because until then it

281. *Vatsala Shankar Bansole v Sambhaji Nanasaheb Khandare*, AIR 2003 Bom 57.

282. *Ramankutty Guptan v Avara*, (1994) 2 SCC 642; AIR 1994 SC 1699. *Akshayalingam Pillai v Ayyambala Ammal*, AIR 1933 Mad 386, the DB held that a decree for specific performance enures not only for the benefit of the plaintiff but also that of the defendant; the passing of the decree does not terminate the suit because all reliefs open to the plaintiff after judgment are equally available to the defendant. *Mohd Ali Sahib v Abdul Khadir Saheb*, (1927) 59 MLJ 351, after directing the purchaser to pay the price within three months, the court had the power to grant extension of time on sufficient cause shown though the application was made after the time fixed for performance had expired.

could not be said that the vendor had failed to comply with the order of the court.<sup>283</sup>

The party at whose instance the contract is cancelled may be asked by the court to restore the benefits, if any, received under the contract to the extent to which justice requires.

### RECTIFICATION OF INSTRUMENTS [S. 26]

Section 26 of the Specific Relief Act, 1963 provides remedy for rectification of instruments. The term “instrument” has been defined in Section 2, clause (14) of the Indian Stamp Act (II of 1899). Accordingly, “instrument” includes every document by which any right or liability is or purports to be created, transferred, limited, extended, extinguished or recorded. A suit, therefore, lies for the rectification of a will, a decree and also for the rectification of an award-decree on the ground of fraud. The word “instrument”, however, does not include “Articles of Association”.<sup>284</sup>

**S. 26. When instrument may be rectified.**—(1) When, through fraud or a mutual mistake of the parties, a contract or other instrument in writing [not being the articles of association of a company to which the Companies Act, 1956 (1 of 1956), applies] does not express their real intention, then—

- (a) either party or his representative-in-interest may institute a suit to have the instrument rectified; or
  - (b) the plaintiff may, in any suit in which any right arising under the instrument is in issue, claim in his pleading that the instrument be rectified; or
  - (c) a defendant in any such suit as is referred to in clause (b), may, in addition to any other defence open to him, ask for rectification of the instrument.
- (2) If in any suit in which a contract or other instrument is sought to be rectified under sub-section (1), the court finds that the instrument, through fraud or mistake, does not express the real intention of the parties, the court may, in its discretion, direct rectification of the instrument so as to express that intention, so far as this can be done without prejudice to rights acquired by third persons in good faith and for value.

(3) A contract in writing may first be rectified, and then if the party claiming rectification has so prayed in his pleading and the court thinks fit, may be specifically enforced.

(4) No relief for the rectification of an instrument shall be granted to any party under this section unless it has been specifically claimed:

Provided that where a party has not claimed any such relief in his pleading, the court shall, at any stage of the proceeding, allow him to amend the pleading on such terms as may be just for including such claim.<sup>285</sup>

283. *M. Mohammad Aslam v C.N.A. Gowthaman*, AIR 2003 Mad 248.

284. *CIT v Kamla Town Trust*, (1996) 7 SCC 349; AIR 1996 SC 620, power to order rectification of trust deed; rectification was ordered to declare that the trust was a charitable one.

285. Sub-section (1) and cl. (a) of this S. corresponds with S. 31 and sub-section (3) of this section corresponds with S. 34 of the repealed Specific Relief Act, 1877. That Act carried the following illustrations:

In the matter of rectification, the true question, is what was the intention of the parties at the time of its execution and not what the parties intentionally omitted.<sup>286</sup> The plaintiff must establish that the alleged intention to which he desires the document to be made conformable, continued concurrently in the minds of all parties down to the time of its execution. [Ibid] For, if the parties after an agreement changed their minds and it is their changed intention that is embodied in the instrument, there is no ground for rectification. What is done on purpose, is obviously not done by mistake. [Ibid]

### *Essentials to be proved*

- (1) That there was a mutual mistake or fraud, and
- (2) that the instrument on that account did not truly express the intention of the parties.<sup>287</sup>

### *Mistake*

The mistake to form a ground for the relief of rectification must be mutual and not unilateral. A mistake on one side may be a ground of defence or a ground for rescinding a contract, but not for correcting or rectifying an instrument. The mistake may be either of fact or of law although the court of equity will not generally grant relief against a mistake of law, except where the mistake results in an inequitable result.<sup>288</sup>

The principle of granting relief by way of rectification is that where a contract as finally made fails to express or embody the agreement between the parties as originally made, it can be had rectified so as to bring it in accord

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*Illustrations as to sub-section (1) and clause (a).*—(a) A, intending to sell to B his house and one of three godowns adjacent to it, executes a conveyance prepared by B, in which, through B's fraud, all three godowns are included. Of the two godowns which were fraudulently included, B gives one to C and lets the other to D for a rent, neither C nor D having any knowledge of the fraud. The conveyance may, as against B and C, be rectified so as to exclude from it the godown given to C, but it cannot be rectified so as to affect D's lease.

(b) By a marriage settlement, A, the father of B, the intended wife, covenants with C, the intended husband, to pay to C, his executors, administrators and assigns, during A's life, an annuity of Rs 5000. C dies insolvent and the official assignee claims the annuity from A. The Court, on finding it clearly proved that the parties always intended that this annuity should be paid as a provision for B and her children, may rectify the settlement and decree that the assignee has no right to any part of the annuity.

*Illustrations as to sub-section (3).*—A contracts in writing to pay to his attorney, B, a fixed sum in lieu of costs. The contract contains mistakes as to the name and rights of the client, which, if construed strictly, would exclude B from all rights under it. B is entitled, if the Court thinks fit, to have it rectified, and to an order for payment of the sum, as if at the time of its execution it had expressed the intention of the parties. [Based on *Stedman v Collett*, (1854) 17 Beav 608: 51 ER 1171.]

286. *Laxman v Ganpat*, 2 Nag LR 4.

287. *Adel Muhammed v Attorney General of Palestine*, (1947) 60 WN 118: AIR 1946 PC 42; *State of Karnataka v K.K. Mohandas*, (2007) 6 SCC 484: AIR 2007 SC 2917, rectification of written contract, in the absence of plea of mutual mistake, a fraud, such relief not permissible.

288. *Nawab Begum v A.H. Creet*, ILR (1905) 27 All 678.

with the intention of the parties. Thus where the final draft mentioned the price in weight when in fact it was agreed to be in count and riot risk was mentioned in an insurance cover by mistake, the court allowed rectification. The court said that the matter came within Section 26 of the Specific Relief Act of 1963 which provides that an instrument can be rectified if through fraud or a mutual mistake of the parties, the contract does not express their real intention.<sup>289</sup>

Under an agreement for sale of property, buyer sent notice to the seller for execution of the sale deed. The seller replied that he had agreed to sell only 5 cents of the land. There was a concurrent finding of the courts in favour of the purchaser that the agreement was to sell 5 cents plus some structures specified in the deed. The court said that Section 26 was not applicable as there was no ambiguity in the deed. There could be no interference in a concurrent finding of fact. The suit for specific performance was rightly decreed.<sup>290</sup>

In the case of a gift deed, only the donor may seek its rectification. In other cases it is permissible only to the parties to the contract and none else.<sup>291</sup>

### CANCELLATION OF INSTRUMENTS [SS. 31–33]

Sections 31 to 33 of the Specific Relief Act, 1963 provide for the cancellation of instruments.

**S. 31. When cancellation may be ordered.**—(1) Any person against whom a written instrument is voidable, and who has reasonable apprehension that such instrument, if left outstanding may cause him serious injury, may sue to have it adjudged void or voidable; and the court may, in its discretion, so adjudge it and order it to be delivered up and cancelled.

(2) If the instrument has been registered under the Indian Registration Act, 1908 the court shall also send a copy of its decree to the officer in whose office the instrument has been so registered; and such officer shall note on the copy of the instrument contained in his books the fact of its cancellation.<sup>292</sup>

289. *New India Rubber Works (P) Ltd v Oriental Fire and General Insurance Co Ltd*, (1969) 1 Comp LJ 153 (Cal).

290. *Subhadra v Thankam*, (2010) 11 SCC 514: AIR 2010 SC 3031.

291. *Joseph John Peter Sandy v Veronica Thomas Rajkumar*, (2013) 3 SCC 801: (2013) 2 SCC (Civ) 332.

292. This section corresponds with S. 39 of the repealed Specific Relief Act, 1877. That section carried the following illustrations:

(a) A, the owner of a ship, by fraudulently representing her to be seaworthy, induces B, an underwriter, to insure her. B may obtain the cancellation of the policy.

(b) A conveys land to B, who bequeaths it to C and dies. Thereupon D gets possession of the land and produces a forged instrument stating that the conveyance was made to B in trust for him. C may obtain the cancellation of the forged instrument.

(c) A, representing that the tenants on his land were all at will, sells it to B, and conveys it to him by an instrument, dated the 1st January, 1877. Soon after the day, A fraudulently grants to C a lease of part of the lands, dated the 1st October, 1876, and procures the lease to be registered under the Indian Registration Act. B may obtain the cancellation of this deed.

A sale deed which was executed by practising a fraud on the transferor who was also not of sound mind, was held liable to be quashed and not to be specifically enforced.<sup>293</sup> Cancellation of a sale without issuing notice to the vendee has been held to be not permissible. A unilateral cancellation and its registration are of no effect. The High Court directed the writ petitioner who had unilaterally cancelled the sale deed executed by him to approach a civil court. The court said that the cancellation of a sale deed and its registration are valid only when there is declaration to that effect by a competent court. In this case there was no such declaration. Further, no notice was issued to the other party. The Supreme Court set aside the cancellation and its registration.<sup>294</sup> A sale deed was executed at the time when it was proved by documentary evidence that the executant was already dead. It was held to be non est and therefore liable to be cancelled.<sup>295</sup>

### Who can seek cancellation

A sale deed was executed in respect of an ancestral property. The transferor's sons challenged it and sought a declaration that the sale was null and void. There was nothing to show their ages and whether they had birth-right in the property. They were not allowed to challenge it on the ground of the competence of the transferor. The suit was also time-barred because it could be filed only within three years of the cause of action whereas 13 years had already passed.<sup>296</sup>

The transfer of a coparcenary property by one of the coparceners without the consent of others was allowed to be cancelled at the action of a coparcener. The court said that no other person can seek cancellation of such a transaction.<sup>297</sup>

There is a presumption that a registered document has been validly executed. It is, therefore, a *prima facie* valid document in law. The onus of proof would be on the person who leads evidence to rebut the presumption.

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(d) A agrees to sell and deliver a ship to B, to be paid for by B's acceptances of four bills of exchange, for sums amounting to Rs 30,000, to be drawn by A or B. The bills are drawn and accepted, but the ship is not delivered according to the agreement. A sues B on one of the bills. B may obtain the cancellation of all the bills. [Based on *Anglo-Danubian Co v Rogerson*, (1867) LR 4 Eq 3.]

293. *Chacko v Mahadevan*, (2007) 7 SCC 363. *Kowta Subrahmanyam Sastry v Kowta Chandramouli*, AIR 2014 NOC 309 (AP), eldest brother clandestinely obtained a sale deed in favour of his son pressurising and playing fraud upon father, taking advantage of his old age and helplessness. Sale was held as liable to be cancelled.

294. *Thota Ganga Laxmi v Govt of A.P.*, (2010) 15 SCC 207: (2011) 3 KLT 345.

295. *Mahanth Ramasis Das v Noor Md Mian*, AIR 2012 Pat 67.

296. *Dayawati v Madan Lal Verma*, AIR 2003 All 276, Arts. 58 and 59 of the Limitation Act, 1963.

297. *Jagdish Tiwary v Lalita Kuer*, AIR 2011 Pat 40. *Rameshwar Lal v Jai Prakash*, AIR 2014 Raj 72, property sold by father when owners were minors and the fact of minority was mentioned in the sale deed. Purchaser could have known this fact. It is for a purchaser to take care to see that legal requirements have been complied with. Cancellation of sale deed was held to be proper.

The respondent in this case could not do so.<sup>298</sup> The ground of seeking cancellation was that because of the fiduciary relationship, the beneficiary was in a position to exert undue influence on the executant. The court said that the burden of proving goodfaith in the transaction was on the beneficiary. He could not do so. The sale deed was therefore liable to be cancelled.<sup>299</sup>

In a case for cancellation of a sale deed on the ground that the deed was void, it was held that the suit could be filed in a civil court by the recorded tenure holder, executant of the deed or his successor. The suit filed by a third party was not maintainable.<sup>300</sup>

When a document is valid, no question arises of its cancellation. When a document is *void ab initio*, a decree for setting aside the same would not be necessary as the same is non *est* in the eye of the law, as it is a nullity. Section 31 of the Specific Relief Act, 1963 refers to both *void* and *voidable* documents. It provides for a discretionary relief.<sup>301</sup> The deed in this case was void by reason of the fact that it purported to convey the interest of a minor. The court said:

“If a deed was executed by the plaintiff when he was a minor and it was *void*, he had two options to file a suit to get the property purportedly conveyed thereunder. He could either file the suit within 12 years of the deed or within 3 years of attaining majority. Here, the plaintiff did not either sue within 12 years of the deed or within 3 years of attaining majority. Therefore, the suit was rightly held to be barred by limitation by the trial court.”

A person who made misrepresentations to induce a person to purchase his land was not allowed to seek setting aside because of his own misconduct. He could not be allowed to take advantage of his own misdeed.<sup>302</sup>

Cancellation of a sale deed cannot be sought only on the basis of unpaid sale price.<sup>303</sup>

#### *No unilateral cancellation, only by court order*

A transfer by way of sale was made absolute by transfer of the property from the transferor to purchaser. The court said that such transfer could not

298. *Prem Singh v Birbal*, (2006) 5 SCC 353; (2006) 2 KLT 863; (2006) 5 Mah LJ 441.

299. *Naib Singh v Gurdev Kaur*, AIR 2011 NOC 382 (P&H).

300. *Kishori Prasad v Addl Distt Judge*, AIR 2003 All 58. *Lalit Kumar Jain v Jaipur Traders Corpn (P) Ltd*, (2002) 5 SCC 383, unexplained delay in filing the suit after the exchange of notices, vendee remained in possession of the mill and used it for the long period of 30 years. In the circumstances of the case, the Supreme Court directed transfer of the mill to the vendee subject to his paying Rs 40 lakhs in addition to the balance amount. *Hameed v Kanhaiya*, AIR 2004 All 405, the plaintiff was able to prove that he was the son at the owner of the property on whom fraud was committed. He was allowed to sue.

301. *Prem Singh v Birbal*, (2006) 5 SCC 353; (2006) 2 KLT 863; (2006) 5 Mah LJ 441.

302. *Sunderlal Bhandari Bhagat v State of Gujarat*, AIR 2012 Guj 71. *Rammachandra Monappa Kallihal v Sunanda Tukaram Koparde*, AIR 2016 Kar 140, sale made through fraudulently obtained general power of attorney 12 years ago when the person executing it was in ICU. Sale held *void ab initio*.

303. *Key Pee Buildtech (P) Ltd v Shahjahan Begum*, AIR 2015 NOC 1061 (Raj).

be annulled as cancelled unilaterally by vendor by executing a cancellation deed. Such deed could not be accepted for registration. Cancellation of sale deed can be ordered only by the court under Section 31 of the Specific Relief Act.<sup>304</sup>

It is not within the powers of the Registrar of Partnership firm to declare that the partnership deed in question was null and void. The remedy is to approach a civil court under Section 31 of the Specific Relief Act.<sup>305</sup>

On execution and registration of a sale deed, the owner completely loses his right over the property and the purchaser becomes absolute owner. The sale deed cannot be nullified by executing a deed of cancellation. It cannot be annulled even by consent or agreement between the parties. The power to cancel such deeds vests with the court. It cannot be exercised by the transferor of a property. Hence, the Bangalore Development Authority could not cancel the registered sale deed under which it had transferred property.<sup>306</sup>

### *Limitation*

There was no pleading in the plaint seeking exemption from the law of limitation in terms of Order 7, Rule 6, CPC. The plaintiff was not allowed to raise the plea of limitation for the first time in second appeal. The suit was for cancellation of the sale deed which was executed in 1997. The limitation had to be reckoned from that date. Suit was filed in 2004, seven years after execution. The suit was held to be barred by limitation.<sup>307</sup>

**S. 32. What instruments may be partially cancelled.**—Where an instrument is evidence of different rights or different obligations, the court may, in a proper case, cancel it in part and allow it to stand for the residue.

This section corresponds with Section 40 of the repealed Specific Relief Act, 1877. That section carried the following illustration:

A draws a bill on B who endorses it to C, by whom it appears to be endorsed to D, who endorses to E. C's endorsement is forged. C is entitled to have such instrument cancelled, leaving the bills to stand in other respects.

**S. 33. Power to require benefit to be restored or compensation to be made when instrument is cancelled or is successfully resisted as being void or voidable.**—(1) On adjudging the cancellation of an instrument, the court may require the party to whom such relief is granted, to restore, so far as may be, any benefit which he may have received from the other party and to make any compensation to him which justice may require.

(2) Where a defendant successfully resists any suit on the grounds—

(a) that the instrument sought to be enforced against him in the suit is voidable, the court may, if the defendant has received any benefit under the

304. *Latif Estate Line India Ltd v Hadieja Ammal*, AIR 2011 Mad 66.

305. *Sri Lakha Granites v Eklavya Singh*, AIR 2011 Raj 49.

306. *K. Raju v Bangalore Development Authority*, AIR 2011 NOC 341 (Kant).

307. *Sukhen Sarkar v Rakhal Chandra Sarkar*, AIR 2011 Gau 56.

- instrument from the other party, require him to restore, so far as may be, such benefit to that party or to make compensation for it;
- (b) that the agreement sought to be enforced against him in the suit is void by reason of his not having been competent to contract under Section 11 of the Indian Contract Act, 1872, the court may, if the defendant has received any benefit under the agreement from the other party, require him to restore, so far as may be, such benefit to that party, to the extent to which he or his estate has benefited thereby.

The relief provided in Section 33 of the Specific Relief Act is based on the principle of protective or preventive justice. This section applies to instruments executed by the plaintiff as well as to other instruments which he seeks to have adjudged void or voidable.<sup>308</sup> It is not necessary that the plaintiff must be a party to a contract; he can maintain the suit under this section if the instrument is against his interest.

The conditions precedent to the applicability of this section are—

- (a) the instrument should be void or voidable against the plaintiff;
- (b) there is a reasonable apprehension of a serious injury;<sup>309</sup>
- (c) that the case is fit for the exercise of the court's discretion to grant the prayer. [*Ibid*]

### When agreement void

An agreement not enforceable by law is said to be void [S. 2(8) of the Indian Contract Act]. A contract is void—

- (i) where the consideration or object or an agreement is forbidden by law, or
- (ii) is of such a nature that, if permitted, it would defeat the provisions of any law, or
- (iii) is fraudulent, or
- (iv) involves or implies injury to the person or property of another, or,
- (v) the court regards it is immoral or opposed to public policy [S. 23 of the Indian Contract Act].

It will also be noted that an agreement in restraint of marriage of any person other than a minor, [S. 26, Contract Act] or by which anyone is restrained from exercising a lawful profession, trade or business [S. 28, *ibid*] or legal proceedings, or agreements of unmeaning or of wagering nature and an agreement without consideration as a general rule [S. 25, *ibid*] are void. A contract by a minor is void.<sup>310</sup>

308. *Suraj Ket Prasad v Chandra Mul*, AIR 1934 All 1071.

309. *Teka Dula v Bai Jivi*, 39 BLR 1072.

310. *Mohori Bibee v Dhurmadas Ghose*, (1902–03) 30 IA 114: ILR (1903) 30 Cal 539 (PC).

### When contract voidable

An agreement which is enforceable by law, at the option of one or more parties thereto, but not at the option of the other or others, is a voidable contract. [S. 2(i) of the Indian Contract Act, 1872]

When consent to an agreement is caused by coercion, fraud or misrepresentation, the agreement is a contract voidable at the option of the party, whose consent was so caused. [S. 19, *ibid*]

A contract induced by undue influence is voidable at the option of the party whose consent was so caused. [S. 19-A, *ibid*]

### Reasonable apprehension

The relief provided under Section 31 of the Specific Relief Act is based upon protective justice and upon the idea of "*quia time*" (for fear) and, therefore, where there is no apprehension of injury to the plaintiff, no suit can be instituted.<sup>311</sup> Reasonable apprehension is to be determined with reference to the circumstances of each case which the court has to deal with.

### Requirements of ground of relief

(1) The relief under Section 31 of Specific Relief Act cannot be claimed as a matter of right; the court will act upon the principle of the exercise of sound discretion, having due regard to the conduct of the parties.<sup>312</sup>

(2) Where the parties are in *pari delicto* and fraud is alleged as the ground for cancellation, the court may refuse the relief to the plaintiff, as he is equally to blame as is defendant.<sup>313</sup>

(3) No relief can be granted under Section 31 of the Specific Relief Act where there is a question of mere inadequacy of consideration.<sup>314</sup>

(4) No suit for the cancellation of a will can be instituted during a testator's lifetime.

### Partial cancellation

Section 32 of the Specific Relief Act will be applicable only when rights and obligations under an instrument are distinct and separable.<sup>315</sup>

### Compensation

The plea of compensation must be taken in the first court.<sup>316</sup>

311. *Chaganlal v Dharamdas*, 7 Bom 607.

312. *Valley v Dallubhoy*, ILR 25 Bom 10.

313. *Bindeshari Prasad v Lekhraj Sahu*, (1915–16) 20 CWN 760.

314. *Kelam v Polavampur*, 191 Cal 746.

315. *Khub Singh v Jahan Lal*, 12 CPCR 13.

316. *Gokul v Karam*, 8 PC 782.

## Limitation

Article 59 of Indian Limitation Act, 1963 prescribes a period of three years for a suit for cancellation of an instrument computable from the date when the fact entitling the plaintiff to have the instrument cancelled first becomes known to him.

The provisions have been frequently used by the courts in rescuing minors from the burden of contracts made by them. One of the outstanding cases is the decision of the Privy Council in *Mohori Bibee v Dhurmodas Ghose*.<sup>317</sup> A minor, declaring himself to be of full age, mortgaged his two houses as against a loan, a part of which was paid to him in cash. He then applied to the court for cancellation of the mortgage. The court had to cancel the mortgage because it was in fact void. The moneylender pleaded for refund of his money. The provisions do authorise courts to require a minor to restore the benefits obtained or make compensation, but only to the extent to which justice so requires. In the present case their Lordships said that justice did not require any relief in favour of the lender because he was reckless in his dealings with the minor.

The provisions quite clearly contemplated that the court could ask only that person to make compensation who was seeking the relief of cancellation. In a case before the Lahore High Court<sup>318</sup> relief was sought by a person against a minor who had taken the price in advance of the land which he purported to sell but refused to complete the sale. It was powerfully contended that the provisions would permit relief only against a person who himself seeks cancellation and not against one who came to the court as a defendant. But the court ordered the minor to refund the money. As against it, the Allahabad High Court refused to ask the minor, who was a defendant in the court, to refund the mortgage money.<sup>319</sup> When the Specific Relief Act was re-enacted in 1963, in terms of the proposals of the Law Commission, Section 33 which provided for the relief of restitution on the cancellation of a contract contained provisions to cover both situations, namely, whether the person seeking relief is the plaintiff or the defendant. The provisions can be presented in terms of the following propositions:

- (1) Where a void or voidable contract has been cancelled at the instance of a party thereto, the court may require him to restore such benefits as he has received under the contract and to make any compensation to the other party which justice may require.
- (2) Where a defendant successfully resists any suit on the ground that the contract, by reason of his being incompetent, is void against him, he may be required to restore the benefits, if any, obtained by him under the contract, but only to the extent to which he or his estate has benefited thereby.

317. (1902–03) 30 IA 114; ILR (1903) 30 Cal 539 (PC).

318. *Khan Gul v Lakha Singh*, ILR (1928) 9 Lah 701; AIR 1928 Lah 609.

319. *Ajudbia Prasad v Chandan Lal*, AIR 1937 All 610 (FB).



### DECLARATORY DECREES

Sections 34 and 35 lay down the law relating to declaratory decrees. A declaratory decree is a decree declaratory of a right which is doubtful or which requires to be cleared. The object of declaratory decrees is to prevent future litigation by removing the existing cause of the controversy. In other words, if a cloud is cast upon the title or legal character of the plaintiff, he is entitled to seek the aid of the court to dispel it.

Section 34 of the Specific Relief Act lays down the circumstances under which a declaratory decree may be passed.

**S. 34. Discretion of court as to declaration of status or right.**—Any person entitled to any legal character, or to any right as to any property, may institute a suit against any person denying or interested to deny, his title to such character or right, and the court may in its discretion make therein a declaration that he is so entitled, and the plaintiff need not in such suit ask for any further relief:

Provided that no court shall make any such declaration where the plaintiff, being able to seek further relief than a mere declaration of title, omits to do so.

*Explanation.*—A trustee of property is a “person interested to deny” a title adverse to the title of someone who is not in existence, and for whom, if in existence, he would be a trustee.

Section 34 of the Specific Relief Act does not sanction every kind of declaration but only a declaration that the plaintiff is entitled to any legal character or to any property.<sup>320</sup> It is not a matter of absolute right to obtain a declaratory decree and it is discretionary for the court to grant or refuse to grant it.

It is essential for a decree under Section 34 that the plaintiff must be entitled to any legal character to any right to property. “Legal character” is a position recognised by law,<sup>321</sup> and a person’s legal character is made up of the attributes which law attaches to him in his individual and personal capacity and the phrase is synonymous with the word “status”.<sup>322</sup> It includes the right of franchise and the right of election.<sup>323</sup> It may be observed that the words “legal character” and “to any right as to any property” are separated by the disjunctive “or” and, therefore, the plaintiff can maintain a suit for a mere declaration, if he can show that he is entitled to any legal character, even though he cannot lay an immediate claim to any property.

320. *Firm of Fakirchand v Shri Jagadguru Shankaracharya*, AIR 1970 Guj 145.

321. *Hira Lal v Gulab*, 10 CPCR 1; *Ram Das v Salim Ahmed*, (1998) 9 SCC 719, weakness in defendant’s claim for title to the property cannot establish plaintiff’s title. Plaintiff not entitled to get declaration of title if such title could not be established by him by leading convincing evidence. High Court failed to consider the specific finding made by the lower appellate court that the plaintiff had failed to establish title.

322. *Ram Krishna v Narayan*, 27 MLJ 639.

323. *Sat Narain Gurwala v Hanuman Prashad*, AIR 1946 Lah 85: 224 IC 322.

### (i) Essentials to be set up for relief under Section 34

(1) That the plaintiff is entitled to a legal character at the time of the suit, or to any right as to any property.<sup>324</sup>

(2) Defendant has denied these or he is interested in denying that character or right of the plaintiff, and

(3) The plaintiff is not in a position to ask for relief consequential upon the declaration.

If these conditions are satisfied, the plaintiff need not ask for any further relief than a mere declaration. But the court shall not make any such declaration if he, being able to seek further relief than a mere declaration of title, omits to do so.<sup>325</sup>

### (ii) Frame of plaint

The plaint must disclose—

(1) the title or right claimed by the plaintiff,

(2) the circumstances in which the cloud was cast over the same or the same was denied or threatened,

(3) the prayer.<sup>326</sup>

324. *Padmini Chandrasekharan v R. Rajagopal Reddy*, (1996) 8 SCC 632, entitlement to property on family partition. *Sowrashttra Vipra Sabha v Namakal Municipality*, (1996) 11 SCC 584, title perfected by formalities. *Prabhakar Adsule v State of M.P.*, (2004) 11 SCC 249: AIR 2004 SC 3557, suit for restraining interference in possession, but title to the property not made out. No relief allowed. *Niranjan Singh v Bant Singh*, AIR 2004 P&H 334, persons who failed to prove they were relatives of the deceased owner, exclusive ownership of the other party, declaratory relief allowed. *N.V. Srinivasa Murthy v Mariyamma*, (2005) 5 SCC 548: AIR 2005 SC 2897, the title of the claimant was dependant on execution of the agreement of reconveyance. Without such agreement the declaration could not be granted.

325. *Mankuwar Asaram v Bodhi Mukundi*, AIR 1957 MP 211. *A. Subramanian v Thirunarakutty Desivinayagam*, AIR 2003 (NOC) 384 (Mad), the trustee of a temple declared to be not the owner of the temple property, he was ousted from trusteeship at the time when he attempted to sell, a decree for recovery of property from him was not passed. *Dalip Singh v Sikh Gurdwara Prabhandak Committee*, (2003) 10 SCC 352: AIR 2004 SC 137, claim that the property was that of the vendor from whom it was purchased because there was no Notification under S. 10(3) of the Sikh Gurdwara Act, 1925 that it belonged to SGPC, but it was included in the List under S. 7(3). Failure to produce the Notification under S. 10(3), no conclusion that the property did not belong to SGPC. *Kanwarjit Singh Dhillon v Hardyal Singh Dhillon*, (2007) 11 SCC 357: AIR 2008 SC 306, the fact that a probate under will had been granted in respect of the property in question, did not bar a civil suit for declaration of title and permanent. The probate court is not competent to decide whether the property was a joint ancestral property.

326. *State v Gudge*, Pat (HC) 262. *Soma Devi v Guin Devi*, AIR 2003 HP 158, a prayer for declaration of genuineness of signature on a document rejected because of a long delay in seeking the declaration and also because of lack of *bona fides*. *Ramachandran v Angamuthu Ammal*, AIR 2004 NOC 469 (Mad), no proof that there was continuous and uninterrupted possession for 12 years. *Venkataramana v Annayya Hedge*, AIR 2004 Kant 433, claimant failed to prove that there was permissive possession, decree on account of adverse possession affirmed. *P.B. Pathy v S Pandurangam*, AIR 2012 Kant 24, documents produced by the plaintiff showed his title and possession since the date of purchase. The defendant did not deny the specific allegation about his trespass, plaintiff entitled to declaration of title and possession.

The right to any property, mentioned in this section, must be a right actually existing at the date of the suit, though the enjoyment itself may be deferred, e.g., a right of the reversioner.<sup>327</sup> But when the plaintiff had no vested or contingent right to any property but only a faint hope of being selected as a shebait after the death of the existing shebait, he could not maintain a suit for declaration.<sup>328</sup> In *Qabool Singh v Board of Revenue*,<sup>329</sup> it was held that the plaintiff must show subsisting right not only on the date of the suit but also on the date of decree.

The defendant should be a person who actually denies or is interested to deny the plaintiff's title, status, right to any property; even the lease denied by a person or the agent of a person who is interested to deny invests the plaintiff with a cause of action for a declaratory suit under Section 34, Specific Relief Act,<sup>330</sup> but a mere apprehension existing in the mind of the plaintiff does not give him any right to bring a suit for declaration.<sup>331</sup>

**When suit for declaration does not lie.**—A suit for declaration will not lie in the following cases:

- (1) for a declaration that the plaintiff did not infringe the defendant's trade mark.<sup>332</sup> Negative declaration will not be allowed;

327. *City Municipal Council Bhalki v Gurappa*, (2016) 2 SCC 200, onus on the plaintiff to prove his title independently, without depending upon defendant's failure to prove his title. On facts, plaintiff succeeded in establishing title.

328. *Ram Sundar v Emperor*, AIR 1929 All 904. *T. Sesha Reddy v Managing Committee, Jama Masjid*, 2001 SCC OnLine AP 1148: 2002 AIHC 1811 the party claiming title over property under registered sale deed proved that the property was not a part of the wakf property, entitled to declaration of title, possession and consequential relief of permanent injunction. *Pennaiah v Thippamma*, AIR 2004 Kant 444, variance between pleading and proof, property described in the plaint not matching with the property at the site, no relief. *Ramchandra Sakhararam Mahajan v Damodar Trimbak Tanksale*, (2007) 6 SCC 737: AIR 2007 SC 2577, the suit was for recovery of possession on the strength of title. The defendant also set up rival title, but because of weakness of his evidence he was not able to establish it. The plaintiff was not entitled to claim relief on the weakness of the defence evidence. He has to establish his own case by his own evidence. The question of title was also not to be decided by survey records alone. The court emphasised the need for appointment of Commission to get the property identified and demarcated.

329. AIR 1973 All 158. *Kumari Devi v Noor Mohammad Mian*, AIR 2002 Pat 132, deed of sale which the defendant claimed in his favour was shown to be forged because its date was after the death of the executant. The court said that the burden of proving genuineness was on the claimant which he could not discharge. *Babu Sheriff v Maqbool Sheriff*, AIR 2003 Mad 355, misconduct of tenant in trying to capture ownership, title of the plaintiff was established by concurrent findings of lower courts, no interference. *Govt of India, Ministry of Defence v Indira Devi*, AIR 2003 AP 329, plaintiff's suit for title to land, the defendants contended that it was a Government land, but they could not prove their stand by their records. The suit was decreed. *Surajbai Galiyana Solanki Bhil v Roopa Nevji Dabhar Bhil*, AIR 2011 MP 160, defendant was in possession of the land and her ownership was also established by document. She could not be dispossessed.

330. *Naubahar Singh v Qadir Bux*, AIR 1930 All 753.

331. *Jagtu Mal v Laxman Das*, 157 IC 523. *Govt of A.P. v Pratap Karan*, (2016) 2 SCC 82: AIR 2016 SC 1717, plaintiff's possession of the land was not denied by the government. Title and possession were also proved. The plaintiff was held entitled to the decree claimed, i.e. declaration of title and possession.

332. 111 IC 176.

- (2) for a declaration that a disposition made by the father of the plaintiff in a will is invalid and that the property is ancestral and that the plaintiff is entitled to a share in it. This suit would be barred by the proviso of Section 42 of the Specific Relief Act, because the plaintiff can claim further relief or partition;<sup>333</sup>
- (3) for a declaration, during the lifetime of the testator, that the will is invalid. The reason is that the will is revocable and no property is transferred during the lifetime of the testator;<sup>334</sup>
- (4) for a declaration that the plaintiff is a purchaser under an unregistered deed of sale;<sup>335</sup>
- (5) no declaratory suit lies to set aside a succession certificate granted under Act XXVII of 1860;<sup>336</sup>
- (6) no one can ask for a declaration of a non-existent right, as of succession, i.e., the chance or possibility of acquiring a right in the future;
- (7) a suit by a student against a University for a declaration that he has passed an examination;<sup>337</sup>
- (8) a declaration tending to affect the free flow of capital and commercial operations would be unjust.<sup>338</sup>

**(iii) Further relief where plaintiff entitled to it (proviso)**

All that the proviso to Section 34 of the Specific Relief Act forbids is a suit for mere declaration without further relief if the plaintiff can sue for further relief. The term "further relief" means "the relief to which the plaintiff is necessarily entitled on the basis of declaration of the title". This is done in order to avoid multiplicity of suits. Further, relief must be in relation to the legal character or right to such character or the right which the defendant denies or is interested in denying. It must also be relief appropriate to, and consequent on the right asserted.<sup>339</sup>

For example, where *A* claims that he is entitled to half portion of the house in the occupation of *B*, he must pray in his suit:—

- (i) that a declaration be made that *A* is entitled to half portion of the house and;
- (ii) that the defendant be asked to deliver the half portion of the house to *A*. This is consequential relief.<sup>340</sup>

333. *Suryanarayananmurti v Tammanna*, ILR (1902) 25 Mad 504.

334. *Rambhajan Kunwar v Gurcharan Kunwar*, ILR (1905) 27 All 14.

335. *Sk Rahmatulla v Sk Sariutulla Kagchi*, 10 WR 51 (FB). See also S. 53-A of Transfer of Property Act, 1882.

336. *Goodwin v Gray*, (1874) 22 WR 312. The new Act is the Indian Succession Act, 1925.

337. *Ramugrah v Banaras Hindu University*, (1919–20) 47 IA 434.

338. *American Express Bank Ltd v Calcutta Steel Co*, (1993) 2 SCC 199, 213.

339. *Joy Narayan Sen v Srikantha Roy*, (1921–22) 26 CWN 206.

340. *Rajasthan Bhawan Trust v Pradnya Devi*, AIR 2003 NOC 352 (Jhar): 2003 AIHC 2272 (Jhar), the defendant in violation of an agreement with the plaintiff sold the property to another by registered deed. The plaintiff sought a mere declaration that the sale deed was void and did not seek a decree for specific performance in his favour, seeking a declaratory

The court while declaring title of the plaintiff cannot decline to adjudicate consequential questions of possession, removal of encroachments, demolition of encroaching structure upon a portion of the land to which the title of the plaintiff has been declared.<sup>341</sup>

In *Ram Saran v Ganga Devi*,<sup>342</sup> the defendant was in possession of some of the suit properties and the plaintiffs in their suit did not ask for the possession of those properties. They merely prayed for a declaration that they were the owners of the suit properties. It was held that the suit was not maintainable and was hit by Section 42 of the Act of 1877 [now S. 34 of the Specific Relief Act, 1963].

A declaration was sought in respect of a property which was in the possession of a charitable trust. The property was purchased by the adoptive mother of the plaintiff in his name and given over to the trust under a valid trust deed. The plaintiff was minor at the time. He himself was a party to the trust deed and convenor of the trust. There was no evidence to show that he had let out the property to the trust. Documentary evidence showed that the trust was in possession of the property and was paying in respect of it property tax, electricity, water charges, etc. It was held that in the circumstances the plaintiff was not entitled to the relief of declaration of title.<sup>343</sup>

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relief without seeking the main relief was held to be self-defeating. *Munilakshmamma v Vijendra Rao*, AIR 2003 NOC 376 (Kant): ILR (2003) 1 Kant 637, a blank declaration that all previous proceedings by the plaintiff be regarded as void, not allowable. *Ramesh Chand Ardawatiya v Anil Panjwani*, (2003) 2 SCC 350: AIR 2003 SC 2508, suit under agreement to buy against trespasser, relief of declaration of title, restoration of possession and injunction sought, the suit could not be dismissed for omission to seek further relief because no further relief could be sought against a trespasser, the suit was proceeding *ex parte*, the buyer was put in possession under an agreement to sell to him, his possession had to be protected against the trespasser, but he was not entitled to a declaration that he was the owner of the property. *Gangaram Rambau Zite v Chindhu Dagadu Tikone*, AIR 2003 Bom 1, dispute over lane between two houses, the party claiming possession and declaration could not prove. The court said that the description of the house property in certified copy of the house maps was conclusive and clinching evidence and that showed that the plaintiff did not own and possess the lane, as it was included in the area of the defendant. Plaintiff's case rejected.

341. *Phanidhar Kalita v Saraswati Devi*, (2015) 5 SCC 661: (2015) 3 SCC (Civ) 230.
342. (1973) 2 SCC 60: AIR 1972 SC 2685. *Shiv Charan v Sukh Ram*, AIR 2003 NOC 251 (P&H): (2003) 2 Rec Cri R 149, acquisition of ownership by the plaintiff under gift deed not disputed, the defendant claimed permanent lease and ownership, the lease had expired, but the defendant continued in possession even after expiry both under the original owner and the plaintiff. It was held that the plaintiff was entitled to declaration of ownership and possession. *Venkataraja v Vidyane Doureradjaperumal*, (2014) 14 SCC 502 declaration of ownership over the suit land filed, but without claiming subsequent relief of eviction of the tenant which was possible but was not maintainable. *Union of India v Ibrahim Uddin*, (2012) 8 SCC 148: (2012) 4 SCC (Civ) 362, suit seeking declaration of ownership of property without seeking possession when the plaintiff was not in possession, held, not maintainable.
343. *Pradeep Kumar v Mahaveer Pershad*, AIR 2003 AP 107. *N.S. Ramanathan v N. Krishnamoorthy Iyer*, AIR 2003 Mad 78, the plaintiff claimed ownership over the property by virtue of a partition decree passed in an earlier proceeding. The defendants did not produce anything to prove their title over the property. They rather admitted the plaintiff's ownership and possession. The plaintiff was held entitled to the declaration. The defendant could not take advantage of the fact that the measurement of the property was different from that shown under the earlier suit for partition.

Section 34 is a reproduction of the original Section 42 of the repealed Act. That section carried certain illustrations reproduced here in the footnote.<sup>344</sup>

Declaration of rights or status is one at the discretion of the court under Section 34 of the Specific Relief Act, 1963. Equally, the grant or refusal of the relief of declaration and injunction under the provision of that Act is discretionary. The plaintiff cannot claim the relief as of right. It has to be granted according to sound principles of law and *ex debito justitiae*. The court cannot convert itself into an instrument of injustice or vehicle of oppression. While exercising its discretionary power, the court must keep in its mind the well-settled principles of justice and fair play and the discretion would be exercised keeping in view the ends of justice since justice is the hallmark and it cannot be administered in vacuum. Grant of declaration and injunction relating to commercial transactions tend to aid dishonesty and perfidy. Conversely, refusal to grant relief generally encourages candour in business behaviour, facilitates free flow of capital, prompt compliance with covenants, sustained growth of commerce and above all inculcates respect for the efficacy of judicial adjudication. Before granting or refusing to grant relief of declaration or injunction or both the court must weigh pros and cons in each case, consider the facts and circumstances in their proper perspective and exercise discretion with circumspection to further the ends of justice. In this backdrop of fact situation it was held in a case that the relief of declaration granted was unjust and illegal as it tended to impede the free flow of capital, thwarted the growth of mercantile business and deflected the course of justice.<sup>345</sup>

344. (a) A is lawfully in possession of certain land. The inhabitants of a neighbouring village claim a right of way across the land. A may sue for a declaration that they are not entitled to the right so claimed.

(b) A bequeaths his property to B, C and D, "to be equally divided amongst all and each of them, if living at the time of my death, then amongst their surviving children". No such children are in existence. In a suit against A's executor, the court may declare whether B, C and D took the property absolutely, or only for their lives, and it may also declare the interests of the children before their rights are vested.

(c) A covenants that, if he should at any time be entitled to property exceeding one lakh of rupees, he will settle it upon certain trusts. Before any such property accrues, or any persons entitled under the trusts are ascertained, he institutes a suit to obtain a declaration that the covenant is void for uncertainty. The court may make the declaration.

(d) A alienates B's property in which A has merely a life interest. The alienation is invalid as against C, who is entitled as reversioner. The court may in a suit by C against A and B declare that C is so entitled.

(e) The widow of a sonless Hindu alienates part of the property of which she is in possession as such. The person presumptively entitled to possess the property if he survive her may, in a suit against the alienee, obtain a declaration that the alienation was made without legal necessity and was therefore void beyond the widow's lifetime. (S. 14 of the Hindu Succession Act has now changed the position into this that a widow is entitled to full rights over her property.)

(f) Out of date illustration, hence omitted.

(g) A is in possession of certain property. B, alleging that he is the owner of the property, requires A to deliver it to him. A may obtain a declaration of his right to hold the property.

345. *Thakamma Mathew v M. Azamathulla Khan*, 1993 Supp (4) SCC 492; AIR 1993 SC 1120; *J. Daulat Singh v Delhi Golf Club Ltd*, AIR 2002 Del 501, declaration that the plaintiff

A declaration of ownership of land cannot be sought by the plaintiff on the basis of adverse possession. But a claim of ownership by adverse possession can be made by way of defence when he is arrayed as a defendant in proceedings against him.<sup>346</sup>

In a suit for declaration of title, the onus to prove his title is on the plaintiff. He cannot succeed on the weakness of the defendant's case. Revenue record is not a proof of title. The plaintiff relied on the family settlement. He offered no explanation of the fact as to why the suit land was not mentioned in the family settlement. Thus, the court felt that his title became doubtful. It was not proper to have decreed the suit on the weakness of the defendant's case.<sup>347</sup>

In a suit for declaration of title, the dispute was as to the extent of the land covered by the agreement. The Supreme Court said: "The High Court finding that plaintiff made out his title in respect of 8 *guntas* of land decreed the suit to that extent. Though the plaintiff had purchased 4 *guntas* of cultivable land and 4 *guntas* of *kharab* land (land unfit for cultivating), when the entire extent of land was converted to non-agricultural use, the land ceased to be "cultivable land" and "*kharab* land" also became non-agricultural land. It was held that the High Court, therefore, rightly found on the facts that plaintiff succeeded in establishing his title and possession in regard to 8 *guntas* and he was entitled to permanent injunction.<sup>348</sup>

#### *Power to do justice*

The plaintiff claimed to have perfected title by adverse possession and sought declaration of title and possession. The suit was dismissed as the plaintiff was found to be in an unauthorised occupation for years. The plaintiff offered to purchase the suit land at market value. The court, in order to do justice, offered him the possible solution to purchase the land in question.<sup>349</sup>

#### *Transfer by partner of firm*

The suit property belonged to a partnership firm. Records showed that after retirement of a partner, the property came to the share of other partners. The retiring partner (plaintiff) had relinquished his right to the property by the deed of dissolution. He never questioned the ownership of the

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was entitled to the membership of the club was not granted. The fact that some others were admitted wrongly would not by itself entitle him to admission to membership. Art. 14 of the Constitution was not applicable to the club. *Gangadhar Behera v Surendra Barik*, AIR 2003 NOC 322 (Ori): (2003) 1 Ori LR 51, proceeding under S. 145 of the CrPC, possession taken over by receiver from the wrongdoer. On the basis of such possession, the wrongdoer was not to file a suit for declaration under the section.

346. *Gurdwara Sahib v Gram Panchayat Village Sirthala*, (2014) 1 SCC 669: (2014) 1 SCC Civ 630: (2014) 4 Mah LJ 74: (2014) 3 MPLJ 36. It would also be open to plead that the previous finding regarding adverse possession operated as *res judicata*.

347. *Union of India v Vasavi Coop Housing Society*, (2014) 2 SCC 269: AIR 2014 SC 937.

348. *Venkatappa v M. Abdul Jabbar*, (2006) 9 SCC 235.

349. *Birbal v State of Haryana*, (2014) 16 SCC 757: (2015) 3 SCC (Civ) 781.

firm over the property. The partners of the firm transferred the property. The retired partner was not allowed to question the alienation. The suit for declaration of ownership, mandatory injunction and restoration of possession was allowed.<sup>350</sup>

The suit was for restraining the defendants and other partners of the firm from alienating property of the firm as stated in the schedule to the plaint. The partnership was at will. The court said that an injunction could not be granted without there being a prayer for dissolution of the firm and settlement of account.<sup>351</sup>

#### *Suit for declaration and injunction without seeking relief of possession*

The property in question was non-agricultural land. Entries in the record of rights could not help to prove possession. Physical possession, the court said, was required to be verified from records produced by the parties. According to the evidence the plaintiff's father was in enjoyment of possession whether symbolic or real. The plaintiffs also produced tax receipts. The defendants produced no contra evidence. The plaintiffs, having already established their possession, there was no need for them to claim possession as a consequential relief.<sup>352</sup>

#### *Suit for declaration of possession and injunction*

The plaintiff claimed possession on the basis of an oral sale. The court said that an oral sale is not recognised by law. The law recognises only two modes of transfer and conveyance, namely by registered instrument or by delivery of possession. The plaintiff was not entitled to a declaration even assuming there was some evidence to show that she was settled in possession.<sup>353</sup>

#### *Simultaneous consumer complaint and civil suit*

A simultaneous consumer complaint and civil suit have been held to be maintainable. The hirer had taken away forcible possession of the vehicle. The purchaser filed a complaint before the District Forum claiming compensation for forcible deprivation of possession. He also filed a civil suit for declaration that he was the sole owner of the vehicle. The court said that such proceedings are not mutually destructive. They can run concurrently.<sup>354</sup>

#### *Declaration as to status of wife*

A declaration was sought under Section 5(1) of the Hindu Marriage Act, 1955, for being a legally wedded wife. The suit was by the second wife.

350. *Sudarshan Kumar Khosla v Rajinder Pal Khosla*, AIR 2011 NOC 52 (P&H).

351. *Scaria Paul v Paracka Industries*, AIR 2011 Ker 97.

352. *K. Jagdishwar v Sharada*, AIR 2011 Kant 148.

353. *Pankajakshy v Devaki Ramakrishnan*, AIR 2011 Ker 30.

354. *L&T Finance Ltd v Anup Kumar Bera*, AIR 2014 Cal 78.

This fact could not be proved that the first wife remained unheard of for seven years. There was no proof also of a custom in the community for second marriage after obtaining customary divorce. The resolution passed by the Gram Panchayat dissolving first marriage was not valid because the first wife was not a party to it. The certificate was managed only for sub-serving the purpose of declaration. The court refused to grant the declaration, the marriage in question being null and void.<sup>355</sup>

A suit was filed for declaration of the legal status of a legally wedded wife and children of the deceased. Identity of persons who participated in the marriage ceremony was not disclosed and none-examined. Daughter and son-in-law of the alleged wife supported her evidence but did not have direct knowledge about marriage. The court said that there is a presumption in favour of validity of marriage and legitimacy of children, if from the time of the alleged marriage, the parties have been accepted as husband and wife by the relatives and others or the fact of it has been mentioned in any document prepared after the fact of marriage. Evidence was not sufficient to prove the ceremony of marriage or the fact of customary marriage. Legal status of wife and children was therefore not proved. Sale deed executed by the actual wife was held to be valid and was therefore not to be cancelled. Appellants failed to prove their status as wife and children of the deceased. Respondents on the other hand proved title and possession of the property. Appellants were not entitled to an injunction under Section 38.<sup>356</sup>

#### *Declaration as to title as against wife*

Where a property was purchased in the name of wife, but the husband contended that he purchased it for his own and family benefit, the court said that family includes wife. Hence, there was no proof that the property was not purchased for the benefit of wife. The husband was not entitled to declaration of title for himself only.<sup>357</sup>

In a case of paternity declaration and against denial of paternity, the putative father was unwilling to subject himself to DNA test. The High Court held that it could use reasonable force by taking police assistance if the blood sample was not willingly given. The Supreme Court dismissed putative father's special leave petition but modified that High Court direction to this extent that confidentiality would be afforded to the petitioner by taking the sample at his residence and not compelling him to come to the court for the purpose. The petitioner's old age was also taken into consideration. The putative son and his mother were permitted to be present at the home collection of the sample so that genuineness of the sample remained

355. *Pilla Appala Narsamma v Madras Regiment*, AIR 2011 AP 183.

356. *Sumathy v Kamalamma*, AIR 2014 NOC 45 (Ker).

357. *Rudra Pratap Duttaa v Satendra Nath Duttaa*, AIR 2012 Pat 78, he could not make a will for the whole property of which he was not exclusive owner.

free from controversy. The DNA lab was directed to furnish the report in a sealed cover.<sup>358</sup>

### *Declaration as to Will*

A suit was filed under Section 63 of the Succession Act, 1925 for declaration and possession. The entitlement was claimed to be on the basis of the earlier Will executed in favour of the plaintiff which was duly proved and registered. The subsequent Will in favour of the defendants was not registered. It was not dictated by the testator, but by some other person. The court said that the subsequent Will was shrouded by suspicious circumstances. The plaintiff was allowed possession of the land in question on the basis of the earlier Will.<sup>359</sup>

### *Who can seek relief (locus standi)*

It was a joint suit by daughter and collateral of owner in possession. It was held that in the event of death of the owner in possession, the ancestral property (agricultural land in this case) was to devolve upon his four daughters and not upon the collateral. The collateral had no locus standi to file suit.<sup>360</sup>

### *Questioning sale deed on ground of fraud*

The document containing the sale deed was questioned on the ground of fraud alleged to have been practised by the purchaser. But fraud was not proved. The transaction was, therefore, not void. The transaction could have been repudiated in accordance with the time-limit prescribed by Article 59 of the Limitation Act, 1963.<sup>361</sup> Entries made in the revenue record by playing fraud with the Record Office were not allowed to be used for showing title and establishing ownership. A declaration of title was not granted only on the basis of revenue records.<sup>362</sup>

### *Right of way*

There was dispute as to right over the common pathway. The plaintiff and his wife had a joint right over the pathway, but it was transferred as a whole by the wife alone. The court said that the wife was not entitled to alienate the entire common pathway in which the plaintiff husband also had the right. It made no difference to the matter of title that the husband had attested the sale deed made by his wife. The defendant's right not being complete, he was

358. *Narayan Dutt Tiwari v Rohit Shekhar*, (2012) 12 SCC 554.

359. *Hans Raj v Ran Singh*, AIR 2011 NOC 451 (HP). *Gian Chand v Shiv Dei*, 2014 SCC OnLine HP 897: AIR 2014 HP 54, another Will shrouded by suspicion, executed five months before death, the wedded wife deposed that he was not in a sound state of mind, persons favoured were not even closely related to the deceased, Will rejected, normal succession allowed.

360. *Gulkandi v Dhikkal*, AIR 2016 P&H 73.

361. *Mathuri Bewa v Prafulla Routray*, AIR 2003 Ori 136.

362. *Babu Singh v Gorakh Singh*, AIR 2011 MP 79.

not entitled to put any obstruction to the ingress and egress of the plaintiff over the common pathway. The plaintiff was entitled to a declaration of his common right and also permanent injunction.<sup>363</sup>

#### *Court fee*

A suit for declaration that the sale deed executed by the plaintiff father was null and void and for seeking joint possession was held to be not a suit for cancellation of sale deed. The court fee has not to be paid on sale consideration mentioned in the sale deed. It is to be computed under Section 7(IV)(c) of the Court Fees Act, 1870.<sup>364</sup>

#### *Jurisdiction*

A claim for hereditary interest or right in respect of Watan property based on adoption. The court said that jurisdiction of civil courts has not been excluded in the matter under the Bombay Inferior Village Watan Abolition Act, 1959. Such a claim could not be decided by the Collector. Questions regarding adoption involve declaration as to status, character, etc. of a particular person. Such questions can be decided only a civil court.<sup>365</sup> There was acquisition of land without notice to land owner and forcible possession by acquiring authority. Acquisition proceeding without notice was held to be nullity. Civil court jurisdiction for declaration to be bad in law and injunct authorities from taking forcible possession has not been barred.<sup>366</sup>

#### *Effect of limitation*

The defendants lost their case in proceedings under Section 145 of the Criminal Procedure Code. They did not file their suit for declaration of title within three years from that date. It was held that the right, title and interest of the defendants in the suit land became extinguished after expiry of three years.<sup>367</sup>

#### *Declaration that statement is defamatory*

It has been held that the relief of declaration falls outside the scope of Section 34, even so the power of court to grant the declaration of a civil nature under Section 9 CPC, is not barred. The relief was sought in this case that the statement made by the defendants in their daily newspaper were defamatory. The court said that the plaint could not be rejected as the plaintiff also prayed for relief of permanent injunction not to repeat such publication in the future and a further relief of damages for the loss caused to the reputation of the plaintiff.<sup>368</sup>

363. *Thukkaram v Shanthi Varadharajan*, AIR 2011 Mad 57.

364. *Subrid Singh v Ranbir Singh*, (2010) 12 SCC 112; AIR 2010 SC 2807.

365. *Ramchandra Dagdu Sonavane v Vithu Hira Maher*, (2009) 10 SCC 273.

366. *M.P. Housing Board v State of M.P.*, AIR 2014 MP 1.

367. *Lakhan Sao v Parwati Devi*, AIR 2010 NOC 1112 (Pat).

368. *J. Jayalalithaa v Nakheerangopal*, AIR 2009 NOC 853 (Mad).

### Parties who are bound by declaration

**S. 35. Effect of declaration.**—A declaration made under this Chapter is binding only on the parties to the suit, persons claiming through them respectively, and where any of the parties are trustees, on the persons for whom, if in existence at the date of the declaration such parties would be trustees.

Section 35 lays down that a declaration made under this chapter (*i.e.* Chapter VI of the Act) is binding only:

- (i) on the parties to the suit,
- (ii) on persons claiming through them respectively, e.g. reversioners, widows and sons etc., and
- (iii) where any of the parties are trustees, on the persons for whom, if in existence at the date of the declaration such parties would be trustees.

For example, A, a Hindu, in a suit to which B, his alleged wife, and her mother, are defendants, seeks a declaration that his marriage was duly solemnised and an order for the restitution of conjugal rights. The court makes the declaration and order. C claiming that B is his wife, then sues A for the recovery of B. The declaration made in the former suit is not binding upon C.

- (iv) *Limitation.*—The governing articles in the Indian Limitation Act, 1963 are Articles 56, 57 and 58.

### Amendment of plaint and limitation

A suit for declaration was filed within limitation. The plaintiff subsequently became aware of the fact that he had failed to include his money claim. An amendment of the plaints was allowed. It was held that the entire claim as such must be deemed to have been filed within time.<sup>369</sup>

## INJUNCTIONS

The term “injunction” has been the subject of various attempts at a definition. It has been defined by Joyce as “An order remedial, the general purpose of which is to restrain the commission or continuance of some wrongful act of the party informed.”

In Burney “injunction has been defined to be a judicial process, by which one who has invaded or is threatening to invade the rights, legal or equitable, of another is restrained from continuing or commencing such wrongful act.”<sup>370</sup>

Both of these definitions are expressive more of what is called a prohibitory injunction than mandatory injunction. The definition which clearly includes both is the one given by Lord HALSBURY. According to him “An

369. *S. Veerabandra v S. Sambanda Naicker*, AIR 2003 Mad 19.

370. ENCYCLOPAEDIA OF THE LAWS OF ENGLAND, Vol 6 (1st Edn by A.W. Renton) 464.

injunction is a judicial process whereby a party is ordered to refrain from doing or to do a particular act or thing.

Injunction acts *in personam*. It does not run with the property. For example *A*, the plaintiff, secures an injunction against *B* forbidding him to erect a wall. *A* sells the property to *C*. The sale does not carry the injunction with the property.

An injunction may be issued for and against individuals, public bodies or even the State. Disobedience of an injunction is punishable as contempt of court.

There are three characteristics of an injunction:

- (i) it is a judicial process,
- (ii) the relief obtained thereby is a restraint or prevention, and
- (iii) the act prevented or restrained is wrongful.

Nelson suggests that “the nature of discretion and the rules for its guidance, in the case of Indian Courts are the same as in England”. Under English Law:

- (1) if the injury to the plaintiff’s legal rights is small; and
- (2) is one which is capable of being estimated in money; and
- (3) is one which can be adequately compensated by a small money payment; and
- (4) the case is one, in which it would be oppressive to the defendant to grant an injunction,

then damages in substitution for an injunction may be given.

In India some of these points have been incorporated into rules of jurisdiction by being enacted as sections of the Specific Relief Act, 1963.

They may be stated as below:

An injunction will not be issued—

- (i) where damages are the appropriate remedy,
- (ii) where injunction is not the appropriate relief,
- (iii) where the plaintiff is not entitled to an injunction on account of his conduct;
- (iv) where the contract cannot be specifically enforced,
- (v) where the injunction would operate inequitably.

### Kinds of injunction

**S. 36. Preventive relief how granted.**—Preventive relief is granted at the discretion of the court by injunction, temporary or perpetual.

Injunctions are either temporary (interlocutory) or perpetual. They are defined in Section 37, Specific Relief Act, which reads—

**S. 37. Temporary and perpetual injunctions.**—(1) Temporary injunctions are such as are to continue until a specified time, or until the further order of the

court and they may be granted at any stage of a suit, and are regulated by the Code of Civil Procedure, 1908.

(2) A perpetual injunction can only be granted by the decree made at the hearing and upon the merits of the suit, the defendant is thereby perpetually enjoined from the assertion of a right, or from the commission of an act, which would be contrary to the rights of the plaintiff.

### Temporary injunctions

The procedure for granting temporary injunction is governed by the rules laid down in Order XXXIX, Rules 1 and 2, Civil Procedure Code<sup>371</sup> which reads as under:

#### Cases in which temporary injunction may be granted

A temporary injunction may be granted in the following cases:

##### 1. For protection of interest in property

This category will cover the following cases:

- (a) that any property in dispute in a suit is in danger of being wasted, damaged or alienated by any party to the suit, or wrongfully sold in execution of a decree, or
- (b) that the defendant threatens, or intends, to remove or dispose of his property with a view to defraud his creditors,
- (c) that the defendant threatens to dispossess the plaintiff or otherwise cause injury to the plaintiff in relation to any property in dispute in the suit.<sup>372</sup>

the court may by order grant a temporary injunction to restrain such act, or make such other order for the purpose of staying and preventing the wasting, damaging, alienation, sale, removal or disposition of the property as the court thinks fit until the disposal of the suit or until further orders.

##### 2. Injunction to restrain repetition or continuance of breach

(1) In any suit for restraining the defendant from committing a breach of contract or other injury, of any kind, whether compensation is claimed

371. For the U.P. Amendment of Order 39, Rules 1 and 2, see S. 13 of the Uttar Pradesh Civil Laws (Reforms and Amendment) Act, 1976.

372. *Votion Investment (P) Ltd v Madhuri Jitendra Mashroo*, AIR 2003 Bom 360, sale of premises which were in possession of tenants, full payment was to be made by the buyer without waiting for consent letters from tenants to vacate, presumption that time was not of essence. Even in the absence of such letters the memorandum of understanding for transfer of premises did not end. The buyer was entitled to injunction to prevent the seller from transferring the property to any other person. *Arvind Construction Co (P) Ltd v Kalinga Mining Corp*, (2007) 6 SCC 798: AIR 2007 SC 2144, *prima facie* case for injunction under Order 39, CPC, applicable also to exercise of jurisdiction under S. 9 of the Arbitration and Conciliation Act, 1996, factual position in the case was not clear enough to assume for the purpose of these interlocutory proceedings to entitle the plaintiff to specifically enforce the agreement, the High Court did not err in refusing injunction.

in the suit or not, the plaintiff may, at any time after the commencement of the suit, and either before or after judgment, apply to the court for a temporary injunction to restrain the defendant from committing the breach of contract or injury complained of, or any breach of contract or injury of a like kind arising out of the same contract or relating to the same property or right.

(2) The court may by order grant such injunction, on such terms as to the duration of the injunction, keeping an account, giving security, or otherwise, as the court thinks fit.

The matter of temporary injunctions is not governed by the Specific Relief Act.<sup>373</sup>

### Discretionary relief

It should be noted that grant of injunction is discretionary with the court. Section 36 of the Specific Relief Act, 1963 expressly lays down that “Preventive relief is granted *at the discretion of the court* by injunction, temporary or perpetual”.<sup>374</sup> Therefore the court will grant temporary injunction if the following conditions are satisfied:

- (i) The plaintiff must establish a *prima facie* case. He is not required to make out a clear title but he must establish that there is a substantial question to be investigated and that matters should be preserved in *status quo* until the injunction is finally disposed of.
- (ii) An irreparable injury would result if the injunction were refused and that there is no other remedy open to the applicant by which he could protect himself from the consequences of the apprehended injury.
- (iii) The conduct of the plaintiff has not been blameworthy.
- (iv) The balance of convenience requires that the injunction should be granted.<sup>375</sup>

### Interim injunction when perpetual injunction is prayed for

In a suit for specific performance of an agreement to buy land, there was no prayer for a decree of perpetual injunction restraining the defendant from transferring the suit land by way of sale to some other person etc., till the disposal of the suit. But he prayed for an interim injunction which was not allowed.<sup>376</sup> The court followed its own earlier ruling in which it was said:<sup>377</sup> “It is also a settled principle that in a suit where there is no permanent

373. *Best Sellers Retail (India) (P) Ltd v Aditya Birla Nuvo Ltd*, (2012) 6 SCC 792: (2012) 4 MPLJ 16.

374. *Ravi Singhal v Manali Singhal*, (2001) 8 SCC 1, in an application for interim relief in respect of a settlement, the court said that it is at the discretion of the court to grant interim relief and exercise of discretion should not be perverse or irrational.

375. *Zaheer Khan v Percept D'mark India (P) Ltd*, AIR 2004 Bom 362, restrictive covenant in contract in the nature of restraint of trade, order to enforce not issued.

376. *Ishwarbhai v Bhanushali Hiralal Mohanlal Nanda*, AIR 2002 Guj 328.

377. *Gujarat Electricity Board v Maheshkumar & Co*, (1982) 2 Guj LR 479: AIR 1982 Guj 289.

injunction sought for, in the final analysis, ordinarily a temporary injunction cannot be granted. The principles that govern the grant of a perpetual injunction would govern the grant of a temporary injunction also."

### Disobedience or breach of injunction

Section 94(c) and Rule 2-A of Order 39 of the Civil Procedure Code (Act V of 1908) provide for the consequences of disobedience or breach of injunction. Section 94(c) provides:

In order to prevent the ends of justice from being defeated the Court may, if it is so prescribed...grant a temporary injunction and in case of disobedience commit the person guilty thereof to the civil prison and order that his property be attached and sold.

And Rule 2-A of Order 39 provides:

**"R. 2-A. Consequence of disobedience or breach of injunction.**—(1) In the case of disobedience of any injunction granted or other order made under Rule 1 or Rule 2 or breach of any of the terms on which the injunction was granted or the order made, of the Court granting the injunction or making the order, or any Court to which the suit or proceeding is transferred, may order the property of the person guilty of such disobedience or breach to be attached, and may also order such person to be detained in the civil prison for a term not exceeding three months, unless in the meantime the Court directs his release.

(2) No attachment made under this rule shall remain in force for more than one year, at the end of which time, if the disobedience or breach continues, the property attached may be sold and out of the proceeds, the Court may award such compensation as it thinks fit to the injured party and shall pay the balance, if any, to the party entitled thereto."

The above provisions provide for the penalty of either arrest or attachment of property of the person who has committed disobedience or breach of the injunction. But the detention in civil prison shall not exceed three months and the attachment of property shall not remain in force for more than one year. If the disobedience or breach continues, the property attached may be sold and out of the proceeds the Court may award such compensation as it thinks fit to the injured party.

### Perpetual injunctions

Section 37(2) lays down that a permanent injunction can be granted only by a decree at the hearing and upon the merits of the suit. In other words for obtaining a permanent injunction, a regular suit is required to be filed in which the right claimed by the plaintiff is examined on merits and finally the injunction is granted by means of the decree. A permanent injunction therefore finally decides the rights of parties whereas a temporary injunction does not do so. A permanent injunction forbids the defendant from asserting

a right or committing an act which would be contrary to the rights of the plaintiff.

#### *Restraint on person or property outside jurisdiction*

The court which passed a decree has power to restrain a person from handing over property in his possession to the judgment debtor (suit property) alongwith the title documents and keeping them in safe custody. Such an order is in the nature of a freezing order, or mareva injunction and order akin to a Anton piller order even if the property or the person concerned is outside the jurisdiction of the court.<sup>378</sup>

#### **Permanent injunction**

Section 38 of the Specific Relief Act states the circumstances in which a permanent injunction can be granted. It provides:

**S. 38. Perpetual injunction when granted.**—(1) Subject to the other provisions contained in or referred to by this chapter, a perpetual injunction may be granted to the plaintiff to prevent the breach of an obligation existing in his favour, whether expressly or by implication.

(2) When any such obligation arises from contract, the court shall be guided by the rules and provisions contained in Chapter II.

(3) When the defendant invades or threatens to invade the plaintiff's right to, or enjoyment of, property, the court may grant a perpetual injunction in the following cases, namely—

- (a) where the defendant is trustee of the property for the plaintiff;
- (b) where there exists no standard for ascertaining the actual damage caused, or likely to be caused, by the invasion;
- (c) where the invasion is such that compensation in money would not afford adequate relief;
- (d) where the injunction is necessary to prevent a multiplicity of judicial proceedings.

#### **Requirements for applicability**

The conditions prerequisite to the applicability of this section are—

- (1) there must be a legal right express or implied in favour of the applicant;<sup>379</sup>
- (2) such a right must be violated or there should be a threatened invasion;<sup>380</sup>

378. *Mohit Bhargava v Bharat Bhushan Bhargava*, (2007) 4 SCC 795: AIR 2007 SC 1717.

379. *Basanti Paikaray v Prananath Paikaray*, AIR 2016 NOC 555 (Ori), gift deed by the mother-in-law in favour of son-in-law, the brother-in-law got the gift deed cancelled, the son-in-law (plaintiff) sought injunction on the ground that the cancellation deed did not carry his signature and therefore it was not valid. Injunction was granted in favour of the plaintiff.

380. *Parkash Devi v Tarsem Lal*, AIR 2003 P&H 245, suit by plaintiff for injunction restraining the defendant from interfering with plaintiff's possession. Entries in revenue records were in plaintiff's favour. Subsequent entries which came into being without notice to the possessor (the plaintiff) and without following Financial Commissioner's instructions could not sustain the defendant's claim to possession. Injunction granted. *Muddanna v Panthanagere*

- (3) such a right should be an existing one;
- (4) the case should be fit for the exercise of court's discretion.<sup>381</sup> Where the inconvenience likely to result from granting injunction is greater than that which is likely to arise from withholding it, the injunction should not be granted;<sup>382</sup>
- (5) it should not fall within the sphere of the restraining provisions contained in, or referred to, in Section 41 of the Specific Relief Act.<sup>383</sup>

### *Illustrations in preceding 1877 Act*

Section 54 of the original Act upon which the present section is based carried certain illustrations which are reproduced below:<sup>384</sup>

*Group Panchayat*, (2003) 10 SCC 349, the Panchayat could not remove the person in possession because the title to the land was in dispute. The Panchayat should have followed the normal procedure under the Panchayat Act. *Gouri v Kamalakshi*, AIR 2004 Mad 463, right to draw water from a well transferred under a will, others were drawing water by manual labour, defendant restrained from using mechanical device. *Lakshmikant Maharana v State of Orissa*, AIR 2012 Ori 4, the plaintiff could not get a restraint order where the proposed area to be leased out to him was not carved out and he had no right in respect of any other area. *Mohd Abdul Rahman v Mohd Egmal Sheikh*, AIR 2015 Gau 112, electricity is an essential requirement for any occupied premises, disconnection of power would amount to invasion of his right to fully enjoy the property legitimately occupied by him. Perpetual injunction against disconnection granted.

381. *Gur v Bhag*, 96 PR 1911: 11 IC 213.

382. *Raja Maheshwar Dayal Seth v Yuvraj Dutt Singh*, 1945 SCC OnLine Oudh 34: AIR 1946 Oudh 42.

383. *Attar Singh Balram Singh v Vishan Das-Prabh Das*, ILR (1937) 18 Lah 345. An injunction is not allowed where the suit is an abuse of the process of court, *Surya Nath Singh v Khedu Singh*, 1994 Supp (3) SCC 561.

384. (a) A lets certain land to B, and B contracts not to dig sand or gravel thereout. A may sue for an injunction to restrain B from digging in violation of his contract.

(b) A trustee threatens a breach of trust. His co-trustee, if any, should, and the beneficial owner may, sue for an injunction to restrain the breach.

(c) The directors of a public company are about to pay a dividend out of capital or borrowed money. Any of the shareholders may sue for an injunction to restrain them.

(d) The directors of a fire and life insurance company are about to engage in marine insurance. Any of the shareholders may sue for an injunction to restrain them.

(e) A, an executor through misconduct or insolvency, is bringing the property of the deceased into danger. The court may grant an injunction to restrain him from getting at the assets.

(f) A, a trustee for B, is about to make an important sale of a small part of the trust property. B may sue for an injunction to restrain the sale, even though compensation in money would have afforded him adequate relief.

(g) A makes a settlement (not founded on marriage or other valuable consideration) of an estate on B and his children. A then contracts to sell the estate to C. B or any of his children may sue for an injunction to restrain the sale.

(h) In the course of A's employment as a vakil, certain papers belonging to his client, B, come into his possession. A threatens to make these papers public, or to communicate their contents to a stranger. B may sue for an injunction to restrain A from so doing.

(i) A is B's medical advisor. He demands money of B which B declines to pay. A then threatens to make known the effect of B's communication to him as a patient. This is contrary to A's duty, and B may sue for an injunction to restrain him from so doing.

(j) A, the owner of two adjoining houses, lets one to B and afterwards lets the other to C. A and C begin to make such alterations in the house let to C as will prevent the comfortable enjoyment of the house let to B. B may sue for an injunction to restrain them from doing so.

The word “obligation” in Section 38(1) has been used in a wide sense and it may arise from:

- (i) Contract,
- (ii) Trust,

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*Ishwara Bhat v Annappa Naika*, AIR 1997 Ker 165, neighbour disturbing the peace of the person in possession and enjoyment of the land in question and threatened trespass, retained permanently. Also to the same effect, *Walter Louis Franklin v George Singh*, (1997) 3 SCC 503. *Madan Jena v Saraswati Jena*, AIR 2003 Ori 14, one co-sharer locked the entrance of the passage room of the other co-sharer preventing her from having access to the public road on that side. The affected sharer was granted an injunction restraining the guilty co-sharer from doing so, the latter having already admitted the right of the co-sharer to the use of the passage.

(k) A lets certain arable lands to B for purposes of husbandry, but without any express contract as to the mode of cultivation. Contrary to the mode of cultivation customary in the district, B threatens to sow the land with seed injurious thereto and requiring many years to eradicate. A may sue for an injunction to restrain B from sowing the lands in contravention of his implied contract to use them in a husbandry-like manner. [Based on *Partt v Brett*, ILR (1817) 2 Mad 62: 17 RR 187.]

(l) A, B and C are partners, the partnership being determinable at will. A threatens to do an act tending to the destruction of the partnership property. B and C may, without seeking a dissolution of the partnership, sue for an injunction to restrain A from doing the act. [Based on *Miles v Thomas*, (1839) 9 Sim 606; 47 RR 320.]

(m) [\* \* \*]

(n) A, B and C are members of an undivided Hindu family. A cuts timber growing on the family property, and threatens to destroy part of the family house and sell some of the family utensils. B and C may sue for an injunction to restrain him.

(o) A, the owner of certain houses in Calcutta, becomes insolvent. B buys them from the official assignee and enters into possession. A persists in trespassing on and damaging the houses, and B is thereby compelled, at considerable expense, to employ men to protect the possession. B may sue for an injunction to restrain further acts of trespass.

(p) The inhabitants of a village claim a right of way over A's land. In a suit against several of them, A obtains a declaratory decree that his land is subject to no such right. Afterwards each of the other villagers sues A for obstructing his alleged rights of way over the land. A may sue for an injunction to restrain them.

(q) A, in an administration suit to which a creditor, B, is not a party, obtains a decree for the administration of C's assets. B proceeds against C's estate for his debts. A may sue for an injunction to restrain B.

(r) A and B are in possession of contiguous lands and of the mines underneath them. A works his mines so as to extend under B's mine and threatens to remove certain pillars which help to support B's mine. B may sue for an injunction to restrain him from so doing.

(s) A rings bells or makes some other unnecessary noise so near a house as to interfere materially and unreasonably with the physical comfort of the occupier, B. B may sue for an injunction restraining A from making the noise. *Shamboo Nath Tikoo v S. Gian Singh*, 1995 Supp (3) SCC 266, injunction against causing disturbance by religious prayers.

(t) A pollutes the air with smoke so as to interfere materially with the physical comfort of B and C, who carry on business in a neighbouring house. B and C may sue for an injunction to restrain the pollution.

(u) A infringes B's patent. If the court is satisfied that the patent is valid and has been infringed, B may obtain an injunction to restrain the infringement.

(v) A pirates B's copyright. B may obtain an injunction to restrain the piracy, unless the work of which copyright is claimed is libellous or obscene.

(w) A improperly uses the trade mark of B. B may obtain an injunction to restrain the user, provided that B's use of the trade mark is honest.

- (iii) Tort,<sup>385</sup>
- (iv) Any other legal obligation.

Section 38 expressly states that where such obligation arises from a contract, the court shall be guided by the principles and rules given in connection with the specific performance of contracts. Thus a permanent injunction will be granted to prevent breach of contract only in those cases where the contract is capable of specific performance. It is again made clear by the language of Section 41(e) which says that an injunction will not be granted to prevent breach of a contract which is not capable of specific performance. Section 42, however, says that where a contract comprising of a positive agreement to do a certain act is coupled with a negative agreement not to do a certain act, whether expressly or impliedly, the fact that positive part is not capable of specific performance will not preclude the court from enforcing the negative part of the agreement by means of an injunction, provided that the plaintiff performs his part of the contract. For example, A contracts to sing at B's theatre for one year and not to sing elsewhere. "To sing at B's

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(x) A, a tradesman, holds out B as his partner against the wish and without the authority of B. B may sue for an injunction to restrain A from so doing. [Based on *Routh v Webster*, (1847) 10 Beav 561: 50 ER 698.]

(y) A, a very eminent man, writes letters on family topics to B. After the death of A and B, C, who is B's residuary legatee, proposes to make money by publishing A's letters. D, who is A's executor, has a property in the letters, and may sue for an injunction to restrain C from publishing them.

(z) A carries on a manufactory and B is his assistant. In the course of his business, A imparts to B a secret process of value. B afterwards demands money of A, threatening, in case of refusal, to disclose the process to C, a rival manufacturer. A may sue for an injunction to restrain B from disclosing the process. *Daewoo Motors India Ltd v Brijendra Prasad*, AIR 2003 Del 2, defendant was an employee of the plaintiff company and after severing relationship he started vilification campaign against the company. He, with his brother, started issuing notices to the company imputing violation of 23 statutes. The court said that there were statutory authorities to take care of the violations. The court issued an injunction restraining the defendants from harming reputation and goodwill of the plaintiff company.

(zz) A person who had played a role in the production of a serial film but his name was not included in the title was allowed to have an order for such inclusion. *Suresh Jindal v Rizsoli Corriere Della Sera*, 1991 Supp (2) SCC 3: AIR 1991 SC 2092. Award of damages would not have been an adequate remedy.

385. In a case before the Supreme Court an injunction was prayed for directing the Municipal Corporation, not to issue a licence for running or operating a "bhatti" (baking oven) for a bakery. The court said: "Insofar as the Municipal Corporation is concerned, the dismissal of the suit against it by the trial court was not challenged by the plaintiffs by filing an appeal. Grant of licence is a statutory function to be discharged by the Municipal Corporation. The licence having already been issued by the Municipal Corporation to appellant-Defendant 1, the trial court rightly observed that the plaintiffs were at liberty to approach the Municipal Corporation and seek cancellation of licence or pray for withholding the renewal thereof by making out a case for the grant of such relief within the framework of the legal provisions governing the grant and renewal of such licence. In the event of the plaintiffs being illegally or unreasonably denied relief by the Municipal Corporation, they would be at liberty to pursue the remedy of appeal or approach the superior authorities within the framework of the Punjab Municipal Corporation Act or such other remedy as may be available to them in accordance with law. *Kuldip Singh v Subhash Chander Jain*, (2000) 4 SCC 50: AIR 2000 SC 1410. *Hari Ram v Jyoti Prasad*, (2011) 2 SCC 682: (2011) 1 SCC (Civ) 540: AIR 2011 SC 952, the Supreme Court restrained the encroachment of a public street.

theatre for one year" is a contract which depends upon the personal qualifications or volition of the parties and hence cannot be specifically enforced. But the negative part of this contract that *A* will not sing elsewhere can be specifically enforced. Hence *A* can be compelled by injunction not to sing elsewhere. Section 42 corresponds with Section 57 of the earlier Specific Relief Act and that provision carried certain illustrations which are reproduced below.<sup>386</sup>

The essence of the section is that where a contract contains both affirmative and negative agreements and although it may be beyond the powers of the court to compel specific performance of the affirmative part, a party may be restrained from committing a breach of the negative part, provided that the plaintiff has performed his part of the contract.

The conditions essential to the applicability of this section are—

- (1) the contract must contain two agreements, that is, (*i*) an affirmative agreement to do a certain act, and (*ii*) a negative agreement (express or implied) not to do a certain act and the negative part must be capable of being separated from the rest of the contract; and
- (2) the applicant must have fully carried out his part of the contract.

The court is not bound to grant an injunction in every case. An injunction to enforce a negative covenant would be refused if it would indirectly compel the employee either to idleness or to serve the employer.<sup>387</sup>

386. *Ramesh Kumar v Chaman Lal*, AIR 2003 Del 202, the property in question belonged to the purported seller and his sister, the seller by misrepresenting his exclusive right received advance, buyer could not get any right, he was allowed refund of his earnest money and compensation for his loss.

#### *Illustrations*

(*a*) *A* contracts to sell to *B* for Rs 1000 the goodwill of a certain business unconnected with business premises, and further agrees not to carry on that business in Calcutta. *B* pays *A* the Rs 1000 but *A* carries on the business in Calcutta. The Court cannot compel *A* to send his customers to *B*, but *B* may obtain an injunction restraining *A* from carrying on business in Calcutta.

(*b*) *A* contracts to sell to *B* the goodwill of a business. *A* then sets up a similar business close by *B*'s shop and solicits his old customers to deal with him. This is contrary to his implied contract, and *B* may obtain an injunction to restrain *A* from soliciting the customers, and from doing any act whereby their goodwill may be withdrawn from *B*.

(*c*) *A* contracts with *B* to sing for twelve months at *B*'s theatre and not to sing in public elsewhere. *B* cannot obtain specific performance of the contract to sing, but he is entitled to an injunction restraining *A* from signing at any other place of public entertainment. [Based on *Lumley v Wagner*, (1852) 1 De GM & G 604.]

(*d*) *B* contracts with *A* that he will serve him faithfully for twelve months as a clerk. *A* is not entitled to a decree for specific performance of this contract. But he is entitled to an injunction restraining *B* from serving a rival house as clerk.

(*e*) *A* contracts with *B* that, in consideration of Rs 1000 to be paid to him by *B* on a day fixed, he will not set up a certain business within a specified distance. *B* fails to pay the money. *A* cannot be restrained from carrying on the business within the specified distance. (But see S. 27 of the Indian Contract Act, 1872.)

387. *Gujarat Bottling Co Ltd v Coca Cola Co*, (1995) 5 SCC 545; AIR 1995 SC 2372; (1995) 84 Comp Cas 618. *Panchu Pradhan v Ramachandra Sethi*, AIR 2003 NOC 88 (Ori), suit for declaration of sale deed to be null and void, declaration made appealed against, order of restoration of possession not passed because a temple had already been constructed on the

Again, where the defendant invades or threatens to invade the plaintiff's right to or enjoyment of property, the court may grant permanent injunction in the following cases:

- (i) Where the defendant is a trustee of the property for the plaintiff. For example, in the course of A's employment as an advocate, certain papers belonging to his client B, came into his possession. A threatens to make these papers public or communicate their contents to a stranger. B may sue for an injunction to restrain A from so doing. A legal practitioner is under an obligation in the nature of trust not to disclose secrets of his clients.<sup>388</sup>
- (ii) Where there exists no standard for ascertaining the actual damage caused, or likely to be caused by the invasion:

For example, A pollutes the air with smoke so as to interfere materially with the physical comfort of B and C, who carry on business in the neighbourhood. B and C may sue for an injunction to restrain A from polluting the air. The installation of an electric transformer in front of the plaintiff's land causing nuisance, hindrance and obstruction to free access to the highway was restraint by issuing a permanent injunction. There was nothing to show that consent of the landowner was taken or sanction of any statutory authority was arranged.<sup>389</sup>

- (iii) Where the invasion is such that compensation in terms of money will not afford adequate relief, for example, A, a professor of law, delivers lectures to his students, the lectures being his own literary composition, he does not communicate such lectures to the whole world. These lectures are the property of the professor and not of the students. A is entitled to restrain the students from publishing the notes without his consent.

- (iv) Where it is necessary to prevent a multiplicity of judicial proceedings.

The suit was for an injunction simpliciter. The ownership of the plaintiff was not disputed. But the defendants threatened to invade the plaintiff's right to enjoy his plot. The court said that a simpliciter suit for an injunction without praying for declaration was maintainable.<sup>390</sup>

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land and the deity installed. The court said that the suit about the land was maintainable, the decree for permanent injunction was to be set aside. *Mohd Abdullah Butuk v Zainab Begum*, AIR 2004 AP 474, judgment based on misinterpretation of documentary evidence and ignoring material evidence, set aside. *Yamuna Nagar Improvement Trust v Khariati Lal*, (2005) 10 SCC 30: AIR 2005 SC 2245, the plaintiff in the first proceedings failed to prove his case, his suit was liable to be dismissed, by the time of the second proceedings, the land had become vested in the State free from all encumbrances and the plaintiff had no right, title or interest in it, his second suit was also liable to be dismissed.

388. *S. Ganapathy v Kunjammal*, AIR 2004 NOC 436 (Mad): 2004 AIHC 2611 (Mad), property belonged to *Samadhayam* of the village, handed over to village carpenter, after his death to successor carpenter, injunction issued in his favour for uninterrupted possession and use.

389. *HPSEB v Hari Chand*, AIR 2009 HP 30.

390. *Prembai v Ghanshyam*, AIR 2011 MP 1.

The grant of discretionary relief, such as an injunction, is equitable in nature. It must be granted, inter alia, on considerations of equity and justice. The appellant who was himself guilty of inequitable conduct could not claim such relief. He obtained possession under the order of an Authority that had no jurisdiction. The respondent deserved in equity to be put back into possession so as to restore the *status quo ante*. The order of restoration deserved no interference.<sup>391</sup>

An injunction cannot be issued in favour of a trespasser against the true owner.<sup>392</sup> Where the plaintiff fails to establish his legal right to the property or his legal right to continue in possession, he could not be granted perpetual injunction against the owner or the manager of the property.<sup>393</sup> The fact that a trespasser has established his possession and, therefore, cannot be thrown out except by court orders does not entitle him to an injunction.<sup>394</sup>

Where two persons were in joint possession and enjoyment of property, one of them was not allowed to seek a mandatory injunction to exclude the other from the property and leave it for exclusive enjoyment of the plaintiff. The title to the property was in dispute. The court would have to determine the title to the property first after giving opportunity to both parties. The plaintiff was not entitled to final relief merely on the basis of possession.<sup>395</sup>

### Injunction to restrain possession

If an issue relating to a flaw in the title of the person in possession is not raised, the parties to the suit or those claiming under them would be estopped from challenging the flawed title in any future suit based on title. The title to the suit property in this case was flawed for not being written or registered. The person who claimed a permanent title to restrain his possession had not challenged his title on that basis. Accordingly, when he sold the suit property to a third person, the latter was also estopped from challenging the flawed title on the ground of non-registration in the suit filed for declaration of title and possession. The court said that the unregistered title of the allottee of the suit from a Cooperative Housing Society is better than the claim based on an unregistered relinquishment of ownership of the suit property.<sup>396</sup>

391. *Kanchusthabam Satyanarayana v Namuduri Atchutaramayya*, (2005) 11 SCC 109: AIR 2005 SC 2010.

392. *Kishan Lal v Radhey Shyam*, AIR 2002 All 271.

393. *Municipal Board v Abdul Hammed*, 1981 All LJ 376.

394. *Ram Rattan v State of U.P.*, (1977) 1 SCC 188: AIR 1977 SC 619; *Krishna Ram Mahale v Shobha Venkat Rao*, (1989) 4 SCC 131: AIR 1989 SC 2097.

395. *Venkataswamy v A. Narayana*, AIR 2002 Kant 326.

396. *Annathimuthu Thevar v Alagammal*, (2005) 6 SCC 202. *Maria Colaco v Alba Flora Herminda D'Souza*, (2008) 5 SCC 268, plaintiff was in possession of property after owner's death, the defendant assumed control and started construction for some time. This showed that the defendant was not sure of his title or rights, grant of an injunction restraining the defendant was not improper. *Jayanti Kar v Dillip Kumar Patnaik*, AIR 2016 Ori 44, a property was sold to more than one buyer with a common passage. One of them attempted to put

### *Suppression of material facts*

Where the vendor seeking the relief of permanent injunction against the vendee suppressed the material fact that he was still under dues towards the vendee, the court said that he was not entitled to the discretionary relief of permanent injunction.<sup>397</sup>

### **Order for rescuing arbitration process**

Where one of the parties was attempting to sabotage the arbitration process, the court emphasised its role in providing underlying support. The power to grant an injunction by way of a specific relief is covered by the 1963 Act. Specific relief is one of the types of relief available for preventing breach of an obligation.<sup>398</sup>

### **Refusal of injunctive relief**

Section 41 lays down the circumstances when perpetual injunction will be refused by the court. In other words, Section 41 lays down the defences that can be raised against the prayer for grant of an injunction. It provides:

#### **S. 41. Injunction when refused.**—An injunction cannot be granted—

- (a) to restrain any person from prosecuting a judicial proceeding pending at the institution of the suit in which the injunction is sought, unless such restraint is necessary to prevent a multiplicity of proceedings;<sup>399</sup>
- (b) to restrain any person from instituting or prosecuting any proceeding in court not subordinate to that from which the injunction is sought;<sup>400</sup>
- (c) to restrain any person from applying to any legislative body;
- (d) to restrain any person from instituting or prosecuting any proceeding in a criminal matter;<sup>401</sup>

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up an iron gate and boundary wall. This amounted to infringement of the right of passage of others. An injunction was granted against him.

397. *M. Hari Narayana v P. Swaroopa Rani*, AIR 2009 NOC 257 (AP).

398. *Abhunik Steels Ltd v Orissa Manganese Minerals (P) Ltd*, (2007) 7 SCC 125.

399. *Kukkala Balakrishna v Vijaya Oil Mills*, AIR 2009 NOC 648 (AP), immovable property sought to be sold in execution of decree. Perpetual injunction sought to stay execution. Declaration of title was sought on the basis of unregistered will, which was also suspicious and not genuine. But the defendant became successful in putting the property in execution of the decree and the other defendant became successful bidder. The court declined interference.

400. *SBI v Madhumita Construction (P) Ltd*, AIR 2003 Cal 7, the expression "court" does not include the Debts Recovery Tribunal either for purposes of appeal or revision. The High Court cannot stay further proceedings pending before the Tribunal in the exercise of the power under S. 9 of the CPC or cl. 12 of the Letters Patent. *Export Credit Guarantee Corp of India Ltd v Annamma Philips*, AIR 2011 Bom 18, Small Cause Court constituted under Presidency Small Cause Courts Act, 1882 [S. 6], Letters Patent (Bombay), cl. 13, 36, is a court subordinate to the Bombay High Court in exercise of ordinary original civil jurisdiction, to restrain a party to a suit before it from instituting any proceeding in a small cause court.

401. *Sangram Singh v State of U.P.*, AIR 2010 All 65, no injunction can be issued restraining any person or authority from lodging an FIR. A temporary injunction cannot be issued where permanent is not possible.

- (e) to prevent the breach of a contract the performance of which would not be specifically enforced;
- (f) to prevent, on the ground of nuisance, an act of which it is not reasonably clear that it will be a nuisance;
- (g) to prevent a continuing breach in which the plaintiff has acquiesced;
- (h) when equally efficacious relief can certainly be obtained by any other usual mode of proceeding except in case of breach of trust;<sup>402</sup>
- (i) when the conduct of the plaintiff or his agents has been such as to disentitle him to the assistance of the court;<sup>403</sup>
- (j) when the plaintiff has no personal interest in the matter.

*Illustrations in preceding 1877 Act*

This section corresponds with Section 56 of the repealed Specific Relief Act, 1877. That section carried the following illustrations:

- (a) A seeks an injunction to restrain his partner, B, from receiving the partnership debts and effects. It appears that A had improperly possessed himself of the book of the firm and refused B access to them. The Court will refuse the injunction.
- (b) A manufactures and sells crucibles, designating them as "patent plumbago-crucibles", though in fact they have never been patented. B pirates the designation. A cannot obtain an injunction to restrain the piracy.
- (c) A sells an article called "Mexican Balm", stating that it is compounded of divers rares essences, and has sovereign medicinal qualities. B commences to sell a similar article to which he gives a name and description such as to lead people into a belief that they are buying A's Mexican Balm. A sues B for an injunction to restrain the sale. B shows that A's Mexican Balm consists of nothing but scented hog's lard. A's use of his description is not an honest one and he cannot obtain an injunction. [Based on *Perry v Truefitt*.<sup>404</sup>]

In a suit by a coparcener for a permanent injunction for restraining the *Karta* or manager of the joint Hindu Family from transferring the joint family property in pursuance of a sale agreement with a third party, it was held

402. Thus where a wrong can be compounded in money, compensation will be an equally efficacious relief. But in such a case also if the defendant is an insolvent or pauper, a decree for damages would be a mere mockery and therefore the court may grant injunction. *R. Ramani v Shanthi Damodaran*, AIR 2011 Mad 60, acquisition of ownership on the basis of unprobated Will, transfer by such a person not valid, no question of ordering specific performance against him.

403. This clause incorporates the maxim: "He who comes to equity must come with clean hands." For example, where an article name as "Mexican Balm" is said to be consisting of rare medicinal qualities, but which really is nothing but an ordinary ointment, the vendor's description being dishonest no injunction can be issued to restrain another dealer from selling a similar article under the same name in order to misguide the people. *Premji Ratnsey Shah v Union of India*, (1994) 5 SCC 547 at p. 550, no injunction can be issued in favour of a trespasser or a person who gained unlawful possession as against the true owner. *S. Jaffarval v B. Pedda Siddaiah*, AIR 2003 NOC 219 (AP) no injunction was granted to a person about whom the official report was that he was not in possession of the land in question. This report was verified by the court finding of fact. The finding was not interfered with. *M.S. Madhusoodhanan v Kerala Kaumudi P Ltd*, (2004) 9 SCC 204: AIR 2004 SC 909, application for permanent injunction against obstruction to peaceful enjoyment of office premises, suit filed two years after the obstruction began. Refusal of injunction was held to be improper. The right to enjoyment of property could not be taken to be extinguished by inaction for two years.

404. (1842) 6 Beav 66: 49 ER 749.

that such an injunction could not be granted. The court said that though in the case of waste or ouster an injunction may be granted against the manager but a blanket injunction restraining permanently from alienating the family property, even in the case of legal necessity, cannot be granted. The court further said that Section 38 of the Act has to be read with Section 41. As the coparcener has an adequate remedy to impeach the alienation under the family law, he cannot, in view of Section 41(b) move the court for an injunction restraining the *Karta* from alienating the coparcenary property.<sup>405</sup>

A suit was filed by the occupant corporation for restraining demolition and dispossession. The corporation had already been dispossessed. The land in question was required by the owner railways for its own public purposes. The corporation having not opposed the notice of termination, accepted its correctness be it termination of rights as lessee or licensee. The court said that even if the dispossession was wrongful, the right and entitlement of the corporation to continue in possession had come to an end. No injunction could be granted.<sup>406</sup>

### Mandatory injunctions

**S. 39. Mandatory injunctions.**—When, to prevent the breach of an obligation, it is necessary to compel the performance of certain acts which the court is capable of enforcing, the court may in its discretion grant an injunction to prevent the breach complained of, and also to compel performance of the requisite acts.

The injunction which commands the defendant to do something is termed as “Mandatory Injunction”. Salmond defines mandatory injunction as “an order requiring the defendant to do a positive act for the purpose of putting an end to a wrongful state of things created by him, or otherwise, in fulfilment of the legal obligations, for example, an order to pull down a building which he has already erected to the obstruction of the plaintiff’s lights”.<sup>407</sup>

Section 39 of the Specific Relief Act, 1963, reads: “When, to prevent the breach of an obligation, it is necessary to compel the performance of certain acts which the court is capable of enforcing, the court may in its discretion grant an injunction to prevent the breach complained of, and also to compel performance of the requisite acts.”

### Illustrations in old Act of 1877

This section corresponds with Section 55 of the repealed Specific Relief Act, 1877. That section carried the following illustrations:

- (a) *A*, by new buildings, obstructs lights to the access and use of which *B* has acquired a right under the Indian Limitation Act, [now Limitation Act, 1963] Part IV. *B* may obtain

405. *Sunil Kumar v Ram Prakash*, (1988) 2 SCC 77: AIR 1988 SC 576.

406. *Pradeep Oil Corpn v Union of India*, AIR 2012 Del 56.

407. Salmond, THE LAW OF TORTS (13th Edn, 1961, changed in later editions) 186.

an injunction, not only to restrain A from going on with the buildings, but also to pull down so much of them as obstruct B's lights.

- (b) A builds a house with eaves projecting over B's land. B may sue for an injunction to pull down so much of the eaves as so project.
- (c) In the case put as Illustration (i) to Section 54, the Court may also order all written communications made by B, as patient, to A, as medical adviser, to be destroyed.
- (d) In the case put as Illustration (y) to Section 54, the Court may also order A's letters to be destroyed.
- (e) A threatens to publish statements concerning B which would be punishable under Chapter XXI of the Indian Penal Code. The Court may grant an injunction to restrain the publication, even though it may be shown not to be injurious to B's property.
- (f) A, being B's medical adviser, threatens to publish B's written communications with him, showing that B has led an immoral life. B may obtain an injunction to restrain the publication.
- (g) In the cases put as Illustrations (v) and (w) to Section 54 and as Illustrations (e) and (f) to this section, the Court may also order the copies produced by piracy, and the trade marks, statements and communications, therein respectively mentioned, to be given up or destroyed.

When a mandatory injunction is granted under this section, two elements have to be taken into consideration: In the first place, the court has to determine what acts are necessary in order to prevent a breach of the obligation; in the second place, the requisite acts must be such as the Court is capable of enforcing.<sup>408</sup> These acts may assume a variety of forms, e.g. pulling down of a building as in Illustration (a) above, the pulling down of eaves as in Illustration (b), the destruction of written communications and letters as in Illustrations (c) and (d), destruction of copies produced by piracy of copyright and of trade marks improperly used by the defendant as in Illustrations (v) and (w) of former Section 54, set out under Section 38 above, and Illustration (g) above.

A mandatory injunction for eviction of a gratuitous licensee or a person in permissive possession upon revocation of permission by the owner is possible. Its grant by the trial court was held to be proper.<sup>409</sup> Such person in possession is entitled to an order for retaining his possession or claim for repossession.<sup>410</sup>

### When not granted

Mandatory injunction, however, will not be granted in the following cases:

- (i) Where compensation in terms of money would be an adequate relief to the plaintiff.
- (ii) Where the balance of convenience is in favour of the defendant.

408. *Madho Singh v Abdul Qaiyum Khan*, AIR 1950 All 505. *Lakshmi Narain Banerjee v Tara Prosonna Banerjee*, ILR (1904) 31 Cal 944, 949; *Khazan Singh v Ralla Ram*, AIR 1937 Lah 839.

409. *Gowri v Shanthi*, (2014) 11 SCC 664: (2014) 4 SCC Civ 250.

410. *Maria Margarida Sequeira Fernandes v Erasmo Jack de Sequeira*, (2012) 5 SC 370: (2012) 3 LW 111 (SC).

- (iii) Where the plaintiff is guilty of allowing the obstructions to be completed before coming to the court, i.e. where plaintiff has shown acquiescence in the acts of the defendant.
- (iv) Where it is desired to create a new state of things. Mandatory injunction, as is clear, is granted to restore *status quo*. It cannot be granted to create a new state of things. Thus, it was held by the Allahabad High Court in *Sheo Nath v Ali*,<sup>411</sup> that where the defendant constructed a structure which interfered with the privacy of the plaintiff's house, he could not be ordered to erect a wall on the roof, so as to prevent a view of the plaintiff's house from the roof.

In a dispute between a brother and his sister, the background was that the sister constructed a house adjacent to that of her brother and the brother actively participated in the construction activity and also allowed her to take the support of his wall. He never objected. Two years later, he changed his mood and claimed removal or demolition of the construction. The trial court refused to order demolition but granted an order against further construction. Such order was held to be proper. The order of the appellate court for demolition by resorting to the Easements Act, 1882 was held to be not proper since an easementary right was never claimed.<sup>412</sup>

#### Damages in lieu of or in addition to injunction [S. 40]

**S. 40. Damages in lieu of, or in addition to, injunction.**—(1) The plaintiff in a suit for perpetual injunction under Section 38, or mandatory injunction under Section 39, may claim damages either in addition to, or in substitution for, such injunction and the court may, if it thinks fit, award such damages.

(2) No relief for damages shall be granted under this section unless the plaintiff has claimed such relief in his plaint:

Provided that where no such damages have been claimed in the plaint, the court shall, at any stage of the proceedings, allow the plaintiff to amend the plaint on such terms as may be just for including such claim.

(3) The dismissal of a suit to prevent the breach of an obligation existing in favour of the plaintiff shall bar his right to sue for damages for such breach.

This section provides that the plaintiff in a suit for perpetual injunction under Section 38, or mandatory injunction under Section 39, may claim damages either in addition to, or in substitution for, such injunction, and the court may, if it thinks fit, award such damages. The plaintiff has specifically to include in his plaint a claim for damages also. If he has not done so, he may seek permission of the court for the amendment of his pleadings. But where a suit, in which damages were not claimed, is dismissed, a subsequent separate suit for damages would not lie. The court can award damages in lieu of injunction where the injury is threatened though not yet caused. The

411. 80 All 70.

412. *Dhaniya Bai v Jiwan*, AIR 2003 MP 71.

House of Lords in *Leeds Industrial Coop Society Ltd v Slack*,<sup>413</sup> laid down that damages could be allowed to a person whose tenement is sure to suffer loss of his right to light when a planned building structure comes up. Where, for example, a person happened to raise his building to encroach upon the land of his neighbour up to three inches, the court allowed the neighbour compensation instead of an order for demolition of the building.<sup>414</sup> Damages have also been allowed under this principle where information delivered in confidence was put to use.<sup>415</sup>

413. 1924 AC 851 (HL). Non-compliance is an offence of a perpetual nature. *Jai Dayal v Krishan Lal Garg*, (1996) 11 SCC 588: AIR 1997 SC 3765.

414. *Tilokchand Nathmal v Dhundiraj Madhavurao*, AIR 1957 Nag 2, of the same kind.

415. *Fraser v Thames Television Ltd*, 1984 QB 44 (HL).

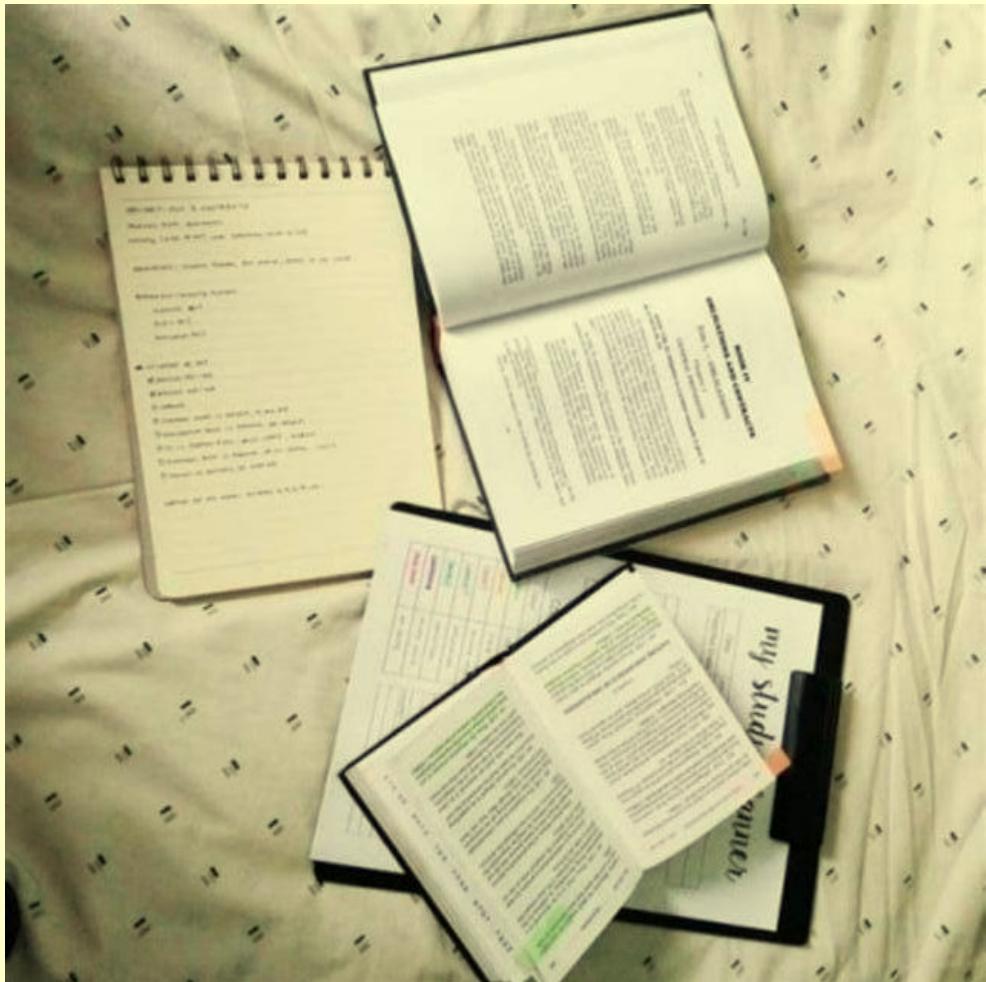
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- *Chand Rani v Kamal Rani*, (1993) 1 SCC 519: AIR 1993 SC 1742
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- *M.S. Madhusoodhanan v Kerala Kaumudi P Ltd*, (2004) 9 SCC 204

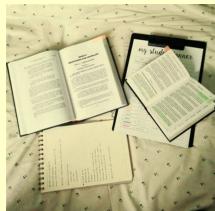




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