The Special Officer, Amaravathi ... vs D.V. Thirumalaswamy And Ors. on 16 April, 1970

Equivalent citations: (1973)2MLJ361

ORDER

M.M. Ismail, J.

1. The petitioner herein is the Special Officer of the Amaravathi Cooperative Sugar Mills, Krishnapuram, Coimbatore District, a society registered under the Madras Co-operative Societies Act, 1932. The first respondent herein is a member of the society. On the allegation that the first respondent herein failed to supply to the petitioner-society sugarcane as required by Bye-law No. 39 of the bye-laws of the society and therefore he was liable to pay to the society a sum of Rs. 25 per tonne for 360 tonnes, which he was bound to supply, the petitioner-society filed a claim against the first respondent under Section 73 of the Madras Co-operative Societies Act, 1961, before the Co-operative Sub-Registrar, the third respondent herein The said Co-operative Sub-Registrar, by his order dated 8th December, 1967, decreed the claim of the petitioner herein against the first respondent. It appears that the petitioner preferred similar claims against several other members and all those claims were also decreed. The first respondent as well as the other members preferred appeals under Section 96 of the Madras Co-operative Societies Act 1961, to the Tribunal (District Judge) constituted as appellate authority under Section 95 of the said Act. Before the appellate authority several objections were taken to the claim of the petitioner herein, some of them being of procedural nature and some of them being objections relating to the validity and interpretation of Bye-law No. 39. The Tribunal namely, the second respondent herein, by its order dated 24th August, 1968, allowed the appeals and remanded the matter to the Co-operative Sub-Registrar. The Tribunal rejected all the contentions advanced by the first respondent herein against the procedure followed before the Co-operative Sub-Registrar as well as against the validity of Bye-law No. 39 except in one respect, namely, that Bye-law No. 39 was not in conformity with Section 74 of the Indian Contract Act. On this basis, the Tribunal took the view that before the petitioner can claim any amount from the first respondent, it must prove before the Co-operative Sub-Registrar that it had actually suffered damages, as a result of the breach on the part of the first respondent herein and also prove the quantum of damages and it can recover only the quantum of damages so proved. The Tribunal was of the opinion that the amount fixed in the Bye-law No. 39 itself as being the amount payable on the breach committed by a member was a penalty and the clause itself was in terrarium and therefore it could not be enforced. For the purpose of understanding the reasoning of the Tribunal, it is necessary to refer to the said bye-law itself. The said Bye-law No. 39 is as follows:

> Every cane grower member shall grow or cause to grow sugarcane every year on at least 2/3 acre of land for every share held by him and supply to the society the entire cane grown thereon or such quantities as may be prescribed by the Board. If any

grower-member fails to supply sugarcane accordingly, the Board shall have power to fine him at the rate of Rs. 25 per every tonne of sugarcane not supplied by him, besides recovering a non-refundable share deposit of Rs. 3-50 per every tonne of cane not supplied by him. All fines imposed under this bye-law shall be recoverable as debts due to the society.

With regard to this bye-law and the argument referred to above, the Tribunal pointed out: ' Though I have disagreed, with the several contentions raised by the appellants, I have to concede as far as one contention of theirs is concerned, viz., that Bye-law No.39 is not in conformity with Section 74 of the Contract Act. It is well-known that if one of the contracting parties institutes proceedings against the other for damages or compensation, the aggrieved party must factually prove that he had sustained damages due to the breach by the other party. In addition, he must also prove the quantum of damages suffered by him. Unless these things are proved, a party cannot seek damages from the defaulting party.

The Tribunal again stated:

The Counsel appearing for the appellants contended that the stipulation for damages provided in Bye-law N0.39, is nothing but a clause in terrorem and that as such it is not enforceable, while the Counsel for the respondent would contend that the damages stipulated in Bye-law No. 39 is a genuine pre-estimate of damages. On a consideration of all factors, I have to concur on this aspect of the case with the arguments of the appellant's Counsel. The respondent is said to pay only about Rs. 55 per tonne of sugarcane supplied by its members. On the other hand, the respondent claims as a penalty of Rs. 28-50 from its members for every tonne of sugarcane not supplied by them. The penalty levied works out to about 50 per cent. of the cost of sugarcane. In the very nature of things, it would appear that the stipulation for penalty is more a clause in terrorem than a genuine pre-estimate of damages. In fact, the wording that has been used in By -law No. 39 is that the sum of Rs. 28-50 shall be imposed as fines and recovered from the members. The sum is therefore Intended to be demanded by way of penalty and not as mere compensation for loss or damages suffered by the respondent. If the stipulation is a clause in terrorem, it is needless to say that it cannot be legally upheld.

The conclusion of the Tribunal is:

Even for argument's sake that the provision for damages stipulated in Bye-law No. 39 is not a clause in terrorem and penal in nature the respondent (petitioner herein) would still not be entitled automatically to a decree in its favour for the sums claimed against the several appellants, (one of whom is the first respondent herein). By virtue of a provision having been made in the by -laws for damages being paid by the defaulting members, it is open (sic) to the respondent (petitioner herein) to straight away ask for damages from the defaulting members. However, the respondent

(petitioner herein) will not be entitled to a decree in its favour unless it proves that it has suffered damages as a matter of fact and in addition, it must also prove the ?extent of damage suffered. The respondent (petitioner herein) must show that the Mill did not get the required quantity of sugercane for crushing every day or that the Mills had to be closed in advance of the usual period of operation for want of sugarcane. If sugarcane had been purchased from third parties and for higher rates, the respondent (petitioner herein) must show that such sugarcane had been purchased and that thereby the respondent (petitioner herein) had to incur losses. Without adducing proof of any of those things. It is not open to the respondent (petitioner herein) to ask for decrees or awards against the appellants (before the Tribunal) merely on the ground that they had not honoured their commitments as per the by -laws and merely on the ground that the bye-laws provide a certain amount as penalty leviable on the defaulting members. The respondent (petitioner herein) would contend that the Government of Madras, the Industrial Investment Corporation and some banks have advanced huge amounts to the Sugar Mills and that unless all the members contribute their due quota of sugarcane to enable the Mill to work regularly year after year, the Mill will not be able to discharge its liabilities. I do not. for a moment, dispute the reasonableness of this contention. However, these factors cannot be deemed adequate consideration for the respondent (petitioner herein) failing to adduce proof of sustainment of loss by it, if it seeks to recover damages or compensation from the defaulting members. In this view of the matter, I think the appeals have to be remanded to the Arbitrator for fresh consideration. The respondent (petitioner herein) will have to adduce proof of sustainment of damages by it and the quantum of damages suffered by it. Several of the Counsel for the appellants (before the Tribunal) pleaded that the matter need not be remanded and that this Court itself can fix some reasonable compensation. I am afraid, this request cannot be complied with. In the absence of any details, I would be acting purely in the realm of conjecture if I were to fix any figure as damages or compensation payable by the appellants (before the Tribunal). No doubt it would involve a lot of time and energy for the parties and the Arbitrator if evidence is to be recorded regarding the quantum of damages suffered by the respondent (petitioner herein) on account of the default by the appellants (before the Tribunal) and like members. This however cannot be helped. Large sums are claimed as compensation from several of the appellants. Their rights as well as the rights of the respondent (petitioner herein) have to be protected in these proceedings, which have to be decided according to principles of law, justice and equity. As such, any consideration of involvement of time and energy cannot be a factor to give a go-by to established principles of law and legal procedure.

It is to quash this order of the second respondent-Tribunal the present writ petition under Article 226 of the Constitution of India has been filed.

2. Mr. K. K. Venugopal, learned Counsel for the petitioner, contended in the first place that the Co-operative Sub-Registrar (third respondent) as well as the Tribunal (second respondent) are

creatures of the statute, namely, the Madras Co-operative Societies Act, 1961, and therefore they had no jurisdiction to go into the validity of a particular bye-law and their duty is simply to enforce the bye-laws as they stand and consequently the second respondent Tribunal exceeded its jurisdiction in coming to the conclusion that By-law No 39 providing for payment of a fine is in terrorem and therefore not enforceable. The second contention of the learned Counsel for the petitioner is that so long as the bye-laws remain registered, a member of the Society like the first respondent cannot question the validity of the by -laws before the second respondent. The argument is that under Section 9(1) of the Madras Co-operative Societies Act, 1961, the Registrar registers the bye-laws if he is satisfied that the proposed bye-laws are not contrary to the Act or the Rules of the Co-operatives Societies or to co-operative principles and on such satisfaction when the Registrar has registered the by -laws, the only remedy open to a member of the Society aggrieved by such registration is to prefer an appeal against the order of registration, under Section 96 (2) of that Act or to apply to have the bye-law amended and the amendment registered as provided for in Section 11 of the aid Act or to move the Registrar himself to call upon the Society to amend the bye-law as contemplated by Section 12 of the said Act. The third contention of the learned Counsel for the petitioner is that Section 74 of the Indian Contract Act cannot be invoked in the present case, since the bye-law in question cannot be said to be a contract entered into under the provisions of the Indian Contract Act. The fourth contention is that in any event, the conclusion of the second respondent that the provision for payment of Rs. 25 per tonne is a clause in terrorem and is a penalty is unwarranted.

3. Mr. M. S. Venkatarama Iyer, learned Counsel for the first respondent, countered these arguments by contending that what the second respondent did was not to go into the validity of the bye-law but merely to construe the bye-law for the purpose of finding out whether the amount of Rs. 25 per tonne mentioned therein was a genuine pre-estimate of damages or was in the nature of penalty and the second respondent was competent to do so. The next contention of the learned Counsel for the first respondent is that a clause in a contract providing for penalty is not enforced by Courts on grounds of public policy and therefore even though the Co-operative Sub-Registrar and the Tribunal are functioning under the Madras Co-operative Societies Act, 1961, they are equally bound by the principle of public policy and consequently the second respondent was justified in coming to the conclusion that the clause in question was not enforceable. Mr. Venkatarama Iyer, further contended that the amount of Rs. 25 per tonne was definitely in the nature of penalty and the second respondent was right in coming to the said conclusion and the fact that the bye-law in question itself describes the amount as a fine, prima facie shows that it was intended to be a penalty and therefore the burden is on the petitioner to show that though called a fine, it is not a penalty but only a genuine pre-estimate of damages.

4. In my opinion, because of certain considerations to which I shall draw attention immediately, it is not necessary to deal with these arguments independently since all of them are intimately or intergrally connected and the entire thing depends upon the applicability and construction of Section 74 of the Indian Contract Act.

5. The first question that has to be considered is as to the nature and status of the bye-laws of a co-operative society. Balakrishna Iyer, J., had to consider this question in his judgment dated 30th April, 1969, in W.P. No. 965 of 1958 and W.P. Nos. 212, 302 and 312 of 1959. The learned Judge

referred to the two different senses in which the expression 'bye-law' is being used-firstly, where a body like a municipality or a local authority frames bye-laws which will have the effect of affecting the rights and interests of the public, and secondly, where a company or a co-operative society frames bye-laws which will regulate the relationship between the corporate body on the one hand and its members on the other and as between members inter se--and came to the conclusion that the bye-laws of a co-operative society are only in the nature of a contract, they having been termed in the second sense referred to above. The same view was taken by Veeraswami, J., as he then was, in his judgment dated 13th March, 1961, in W.P. No. 23 of 1962, by Srinivasan J., in his judgment dated 22nd January 1965, in W.P. No. 782 of 1964. and by Sadasivam, J , in his judgment dated 21st March, 1969, in WP No 4139 of 1968. The Supreme Court in a very recent judgment, namely, Co-operative Central Bank Ltd. and Ors. v. Additional Industrial Tribunal, Andhra Pradesh, Hyderabad , has also held to the same effect. The Supreme Court has pointed out:

> We are unable to accept the submission that the bye-laws of a co-operative society framed in pursuance of the provisions of the Act can be held to be law or to have the force of law. It has no doubt been held that, if a statute gives power to Government or other authority to make rules, the rules so framed have the force of statute and are to be deemed to be incorporated as a part of the statute. That principle, however does not apply to bye-laws of the nature that a co-operative society is empowered by the Act to make The bye-laws that are contemplated by the Act can be merely those which govern the internal management, business or administration of a society. They may be binding between the persons affected by them, but they do not have the force of a statute. In respect of bye-laws laying down conditions of service of the employees of a society, the bye-laws would be binding between the society and the employees just in the same manner as conditions of service laid down by contract between the parties. In fact, after such bye-laws laying down the conditions of service are made and any person enters the employment of a society those conditions of service will have to be treated as conditions accepted by the employee when entering the service and will thus bind him like conditions of service specifically forming part of the contract of service. The bye-laws that can be framed by a society under the Act are similar in nature to the articles of association of a company incorporated under the Companies Act and such articles of association have never been held to have the force of law.
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> Thus it is clear that the bye-laws of a co-operative society have no higher status than that of a contract entered into between the two parties. I am unable to see any substance in the contention of Mr. Venugopal that these bye-laws are not contracts entered into under the Indian Contract Act 1872, and therefore the provisions of Section 74 of that Act cannot be applied in the present case. There is no such thing as a contract entered into under the Indian Contract Act, 1872, and a contract not so entered into. The Indian Contract Act 1872, lays down certain general principles regarding formation of contracts, performance of the contracts, the consequence of breach of contracts etc., as applicable to all kinds of contracts. Though the said enactment does not purport to deal exhaustively with any particular chapter or

> sub-division of the law relating to contracts or to cover the whole field of Contract Law, none the less the extent to which provisions have been made in the Act, those provisions apply to all kinds of contracts. As a matter of fact, in a case like the present one, when a person becomes a member of a cooperative society, he offers to become a member of the society only on the understanding that he will be bound by the bye-laws of the society and once he is admitted as a member of the co-operative society, there comes into existence a concluded contract between the society and the said member in terms of the bye-laws. Therefore, there is no substance in the contention of Mr. K.K. Venugopal, learned Counsel for the petitioner. Once it is held that the bye-laws of the petitioner-society constitute a contract between the society on the one hand and its members like the first respondent on the other, naturally the law of contract in this behalf is attracted.

6. Mr. M. S. Venkatarama Iyer, learned Counsel for the first respondent, contended that according to the principles of the law of contract, whenever a contract contains a stipulation as to payment of a certain sum of money by a person guilty of breach of the contract to the other party, naturally the Court will have to consider whether such sum represents a genuine pre-estimate of damages or merely a penalty, and if it is a penalty, the Court is bound to refuse to enforce the stipulation for payment of penalty in the interests of public policy. No doubt, it is true that even when the parties have entered into a contract providing for a stipulation for payment of a penalty in the event of the breach of the contract, there is nothing to preclude the party in the breach from seeking the protection of the Court against enforcement of the stipulation for payment of the penalty. As pointed out by Lord Raddliffe in Bridge v. Campbell Discount Company Ltd. (1962) 1 All E.R. 385 at 395:

> If it does not amount to such a pre-estimate then it is to be regarded as a penalty, and I do not myself think that it helps to identify a penalty to describe it as in the nature of a threat "end in terrorem" (to use Lord Halsbury's phrase) in Lord Elphinstone v. Monkland Iron and Coal Company (1886) 11 A.C. 332, I do not find that description adds anything of substance to the idea conveyed by the word "penalty" itself, and it obscures the fact that penalties may quite readily be undertaken by parties who are not in the least terrorised by the prospect of having to pay them and yet are, as I understand it, entitled to claim the protection of the Court when they are called on to make good their promises. The refusal to sanction legal proceedings for penalties is, in fact, a rule of the Court's own, produced and maintained for purposes of public policy (except where imposed by positive statutory enactment, as in 8 and 9 Wm. c. 11; 4 and 5 Anne c.16). The intention of the parties themselves is never conclusive, and may be overruled or ignored if the Court considers that even its clear expression does not represent 'the real nature of the transaction' or what 'in truth' it is to be taken to be.
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> Thus, it is clear that the fact that the parties have agreed upon a particular sum to be payable by the party in breach to the other party is no ground for holding that the party in breach must be compelled to pay the same to the other solely on this ground. Hence, in English law, it had always been the task of the Court to find out whether

> the particular sum agreed upon in the contract, in such circumstances, was a genuine pre-estimate of the damages arrived at by the parties or a penalty provided for in terrorem.

7. Lord Dunedin in Dunlop Pneumatic Tyre Company Ltd. v. Mew Garage and Motor Co Ltd. (1915) A.C. 79 at 86-87 attempted to lay down various propositions, which were deducible from the decisions which ranked as authoritative as follows:

> 1. Though the parties to a contract who use the words 'penalty' or 'liquidated damages' may prima facie be supposed to mean what they say, yet the expression used is not conclusive. The Court must find out whether the payment stipulated is in truth a penalty or liquidated damages. This doctrine may be said to be found passim in nearly every case.

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. "Cyldebank Engineering and Ship Building Company v. Don Jose Ramos Yzquiredo v. Castaneda (1905) A.C. 6, 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, judged of as at the time of the making of the contract, not as at the time of the breach. Public Works Commissioner v. Hills (1906) A.C. 368, and Webster v. Bosanquet (1912) A.C. 394, To assist this task of construction various tests have been suggested, which if applicable to the case under consideration may prove helpful or even conclusive. Such are:

> 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. (Illustration given by Lord Halsbury in Clydebank case (1905) A.C. 6).
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> (b) It will be held to 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 (Kemble v. Ferren 6 Bing. 141, This though one of the most ancient instances is truly a corollary to the last test. Whether it had its historical origin in the doctrine of the common law that when A promised to pay B a sum of money on a certain day and did not do so, B could only recover the sum with, in certain cases, interest, but could never recover further damages for non-timeous payment, or whether it was a survival of the time when equity reformed bargains merely because they were unconscionable-a subject which much exercised Jessel, M.R. in Wallis v. Smith 21 Ch.D. 243 is probably more interesting than material.
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> (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 serious and others but trifling damage' (Lord Watson in Lord Elphinstone v. Monkland Iron and Coal Company) 11 A.C. 332.

On the other hand:

(d) It is no obstacle to the sum stipulated being a genuine pre-estimate of damage, that the consequences of the breach are such that to make precise pre-estimation is almost an impossibility. On the contrary, that is just the situation when it is probable that pre-estimated damage was the true bargain between the parties (Clydebank case (1905) A.C. 6 at p. 11, Lord Halsbury, Webster v. Bosanquet (1912) A.C. 394 at p. 398, Lord Mersey.).

Though Mr. M.S. Venkatarama Iyer, realised the position that the nomenclature given by the parties as "liquidated damage or penalty", is not conclusive and in every case it is open to the Court and in fact it is the duty of the Court to decide whether the particular amount agreed upon between the parties really constituted a genuine pre-estimate of damages or a penalty, still he contended, relying upon the decision of the Court of Appeal in Willson v. Love (1896) 1 Q.B. 626, that the use of the word 'fine' in the bye-law in question prima facie showed that it was intended to be a penalty and therefore the burden is on the petitioner-society to show that it was intended really to be a genuine pre-estimate of damages. Lord Esher, M. R., in Willson v. Love (1896) 1 Q.B. 626, relied on by Mr. M. S. Venkatarama Iyer, has observed:

Therefore the parties have themselves called this sum a penalty. That circumstances is not in itself decisive of the question. A succession of Judges have held that the use of the term 'penalty' or 'liquidated damages' is not conclusive; but no case, I think decides that the term used by the parties themselves is to be altogether disregarded, and I should say that, where the parties themselves call the sum made payable a 'penalty' the onus lies on those who seek to show that it is to be payable as liquidated damages.

I am of the opinion that none of these considerations has any relevancy to the law in India, in view of the specific provision contained in Section 74 of the Indian Contract Act.

8. The Supreme Court in Fateh Chand v. Balkrishna Dass , after extracting Section 74 of the Indian Contract Act, has observed:

The section 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. Under the common law a genuine pre-estimate of damages by mutual agreement is regarded as a stipulation naming liquidated damages and binding between the parties; a stipulation in a contract in terrorem is a penalty and the Court refuses to enforce it, awarding to the aggrieved party only reasonable compensation. The Indian Legislature has 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 amounts to be paid in case of breach, and stipulations by way of

penalty.

In view of this pronouncement of the Supreme Court, it is unnecessary to go into the various decisions bearing on English law in this behalf and we shall have to consider the position as emerges from the provisions contained in the Indian Contract Act. Chapter VI of that Act under the caption, "Of the consequences of Breach of Contract", consists of three sections, namely, Sections 73, 74 and 75. It is necessary to extract those three sections in full for the purpose of appreciating the point involved in the present case. Those sections are:

73. 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 hint 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.

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.

74. 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 stipulations 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 Central Govern-ment or of any 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 the 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.

75. 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.

Thus, it will be seen that Section 73 talks of compensation for any loss or damage caused to a party to the contract by the breach of the contract committed by the other party. Therefore, so far as Section 73 is concerned, a party to a contract can claim compensation from the other party who has broken the contract only if he proves that he has sustained loss or damage and that too only to the extent of such loss or damage suffered by him. This conclusion flows from the language used in the section itself, namely, "compensation for any loss or damage caused to him thereby". Similar is the expression used in Section 75 too. That section refers to "compensation for any damage which he has sustained through the non-fulfilment of the contract". Consequently, both under Section 73 and under Section 75, a person will be entitled to recover compensation only if he has sustained loss or damage and the amount of compensation will be only to the extent of such loss or damage. On the other hand, Section 74 is intended to meet a different situation altogether and it provides for a different consequence. That section clearly and categorically states that the party complaining of breach is entitled to compensation, whether or not actual damage or loss is proved to have been caused by the breach of the contract. Again, as distinct from the use of the expression, "compensation for any loss or damage caused to him thereby" in Section 73 and the use of the expression "compensation for any damage which he has sustained through the non-fulfilment of the Contract" in Section 75, Section 74 uses the expression, "reasonable compensation". Therefore, Section 74 is more or less in the nature of an exception to Section 73. Hence, where a case falls within the scope of Section 74, a claimant will be entitled to reasonable compensation, irrespective of the fact whether actual loss or damage is proved to have been caused to him or not. However, Section 74 will apply only if in the contract a sum has been named as the amount to be paid in case of breach or if the contract contains any other stipulation by way of penalty. If this test is not satisfied, Section 74 will not be attracted. When this test is satisfied and Section 74 is attracted, the reasonable compensation cannot exceed the amount named in the contract or the penalty stipulated for. In other words, in such circumstances, the amount named in the contract or the penalty stipulated for will be the maximum which a party will be entitled to by way of reasonable compensation. From the very nature of the case, it is the duty of the Court to assess and arrive at the reasonable compensation and if the reasonable compensation so arrived at exceeds the sum named in the contract or the penalty stipulated for, the successful party will be entitled only to the sum so named or the penalty stipulated for. On the other hand, if the reasonable compensation arrived at by the Court is less than the sum so named in the contract or the penalty stipulated for, the successful party will be entitled to the amount assessed by the Court.

9. Hence a combined reading of Sections 73 and 74 of the Indian Contract leads to the following result:

> Whenever a contract has been broken, the party who has suffered by such breach is entitled to recover from the party in breach, compensation for loss or damage caused

> to him by such breach. This naturally assumes that the claimant has suffered loss or damage and therefore before claiming anything by way of compensation, he must prove that he has suffered loss or damage. The quantum of compensation will depend upon the extent of the loss or damage caused to him and in other words, the compensation will be only to cover the loss or damage suffered by him. This will be the position in respect of a contract where the parties themselves have not mentioned any amount as being the amount payable in the event of a breach or have not stipulated for payment of any penalty. On the other hand, where the parties to a contract have named an amount as being payable in the event of a breach or stipulated for payment of penalty, the party not in breach will be entitled to recover from the party in breach a reasonable compensation and for recovering this reasonable compensation, it is not necessary for the claimant to prove that he has actually suffered any loss or damage. The reasonable compensation to be awarded by the Court cannot exceed the amount named by the parties to the contract or the penalty stipulated for, the same being treated to be the maximum to which the party not in breach is entitled.

10. No decision of any Court was brought to my notice interpreting the above provisions differently. Bhai Panna Singh and Ors. v. Firm Bhai Arjan Singh-Bhajan Singh-Surjan and Anr. 57 M.L.J. 323 : 117 I.C. 485 : A.I.R. 1929 P.C. 179, is a ?decision of the Privy Council. In that case, the contract provided for payment of a sum of Rs. 10,000 as damages, and a claim for that amount was made. Dealing with that situation, the Privy 'Council observed:

> The effect of the Indian Contract Act of 1872, Section 74, is to disentitle the plaintiffs to recover simpliciter the sum of Rs. 10,000 whether penalty or liquidated damages. The plaintiffs must prove the damages they have suffered. The only evidence of loss is that of the loss on re-sale by Rs. 1,000.
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> After referring to this judgment of the Privy Council as well as other decisions a Bench of the Lahore High Court in Mool Chand Behari Lai v. S.D. Chand and Company A.I.R. 1947 Lah. 112, observed:
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> On a review of all these authorities, I think it is quite clear that whether some amount is paid by way of earnest money or kept in deposit for the due performance of any obligation under the contract, it is always for the Court to determine what amount if any, would be 'reasonable compensation' under the circumstances of a particular case. Section 74 is applicable in all cases where a sum is fixed as the amount payable in case of breach, regardless of the fact whether any actual loss was or was not caused. If the Court considers that the sum named is not excessive or unreasonable it shall allow it, or otherwise reduce it to the figure it considers reasonable to allow. In cases where there is no data to estimate the amount of damages actually caused, the discretion of the Court is unfettered in allowing what it considers 'reasonable compensation', subject, of course, to the maximum fixed by the parties. Where a party asserts that the amount mentioned as payable in case of a breach, is a ' genuine

pre-estimate of damages', calculated by the contracting parties, and should not on that account be disturbed, it might be established that this is so and the Court, if satisfied, will adopt it as reasonable compensation to be awarded. But the final say is with the Court and not with the litigant.

In Hardip Singh v. Hira Films , a Bench of the Punjab High Court had this to say on the subject:

This section (section 74 of the Indian Contract Act) relates to contracts wherein on breach thereof liability to pay a specified amount as damages is mentioned or there is a stipulation by way of penalty. The section lays down that the person entitled to get damages is to receive reasonable compensation not exceeding the amount specified in the contract. What is reasonable compensation in a given case depends on the facts and circumstances of each case and to determine it a Court must take into consideration the entire material on the record and also consider the circumstances of the case. This section does not make any distinction between the amount mentioned in the contract as liquidated damages based on genuine pre-estimate or as a security for due performance thereof.

In either case it is incumbent on Courts of law to compute reasonable compensation and it is not for the parties concerned to determine the figure. If the amount of reasonable compensation exceeds the amount mentioned in the contract then the amount so mentioned therein must be treated as reasonable. Now this amount may have been fixed by the parties as a genuine pre-estimate of the loss or it may be that the amount fixed is an essential term of the contract and the parties may not have entered into agreement at all if the compensation had not been fixed at that figure or the amount may have been fixed as limiting the liability of the guilty party where actual damages are expected to exceed that figure. There is no reason why Courts should not take those factors into consideration when calculating reasonable compensation. After all it is hardly ever (sic) that reasonable compensation can be calculated with mathematical exactness and in a given case Courts may well come to the conclusion that the amount mentioned in the contract as damages represents reasonable compensation in the circumstances of the case. It is, however, clear that in all cases covered by Section 74, Indian Contract Act, the amount is to be decreed as reasonable compensation and not by virtue of its mention in the contract.

It is obviously for the party claiming compensation to bring the necessary material on the record. Section 74 lays down that it is the duty of Courts to award reasonable compensation even when the aggrieved party has failed to prove that it had suffered any actual damage of loss. In such a case I take it that the Courts will award nominal or in flagrant cases even substantial compensation. It therefore, follows that in substance the only effect of naming a sum as compensation in a contract is that the decree is in no case to exceed that amount which operate* as a maximum in the case.

Consequently, my conclusion is that, having regard to the express language contained in Section 74 of the Indian Contract Act and the various decisions of the Courts referred to above, in a case to which Section 74 of the Indian Contract Act applies, the party claiming; compensation need not prove that he has; actually suffered any loss or damages, and he is entitled to claim reasonable compensation solely because breach of the; contract has been committed by the other party and the parties themselves have; agreed to the payment of a particular sum, whether it is called 'damage or 'penalty' in the event of a breach and that the only restriction which the law imposes is that the reasonable compensation to be assessed or computed by the Court cannot exceed the amount agreed to by the parties, whether by way of damages or by way of penalty. To contend that even in such circumstances, the party claiming compensation must prove that he has actually suffered loss or damage is to fly at the face of the express language contained in Section 74 of the Indians Contract Act and to ignore the same altogether. If the plaintiff actually proves the extent of loss or damage sustained by him as a, result of the breach committed by the other party, it would certainly constitute relevant material to be taken into account by the Court in assessing the reasonable compensation. But it is far different from saying that he is not entitled to any compensation at all unless he proves that he has actually sustained loss or damage. Where it is established that the plaintiff has not suffered any loss or damage at all, the Court may not award him any substantial amount. But that is far different from denying him the right to claim, reasonable compensation as provided for by Section 74 of the Indian Contract Act on the ground that he has not actually suffered any loss or damage. This conclusion of mine derives support from the following observations of the Supreme Court in Fateh Chand v. Balkishan Das referred to already:

The measure of damages in the case of breach of a stipulation by way of penalty is by Section 74 reasonable compensation not exceeding the penalty stipulated for. In assessing damages the Court has subject to the limit to the penalty stipulated jurisdiction to award such compensation as it deems reasonable having regard to all the circumstances of the case. Jurisdiction of the Court to award compensation in case of breach of contract is un-qualified except as to the maximum stipulated; but compensation has to be reasonable and that imposed upon the Court duty to award -compensation according to settled principles. The section undoubtedly says that the aggrieved party is entitled to receive compensation from the party who has broken the contract whether or not actual -damage or loss is proved to have been caused by the breach. Thereby, it merely dispenses with proof of 'actual loss or damage'; it does not justify the award of compensation when in consequence of the breach no legal injury at all resulted because compensation for breach of contract can be awarded to make good loss or damage which naturally arose in the usual course of things, or which the parties knew when they made the contract, to be likely to result from the breach.

11. If the impugned order of the second respondent Tribunal is examined against the background of the above legal position. it clearly follows that the Tribunal committed errors of law apparent on the face of the record. In the first place the Tribunal expressed its view that Bye-law No. 39 of the bye-laws of the petitioner is not in conformity with Section 74 of the Indian Contract Act and that it cannot be legally upheld. I am of the opinion that this view of the Tribunal is incorrect. Section 74 of the Indian Contract Act itself contemplates and takes into account the parties to a contract stipulating for payment of penalty in the event of a breach of the contract. Therefore, any stipulation contained in a contract providing for payment of penalty in the case of a breach cannot be said to be contrary to Section 74 of the Indian Contract Act and therefore the question of such provision not being legally upheld cannot possibly arise. All that Section 74 of the Indian Contract Act says is that with reference to such a contract, the aggrieved party will be entitled only to a reasonable compensation which in no case can exceed the penalty stipulated for in the contract itself. This is the first error of law which the second respondent-Tribunal has committed.

12. The second error of law is found in the conclusion of the Tribunal. The Tribunal has stated that the petitioner herein has to factually prove that it has sustained damages due to the breach committed by the other party and unless it proves that it has actually sustained damages and further proves the extent of the damages suffered by it, it will not be entitled to claim any compensation from the first respondent herein. This again is clearly opposed to the provisions of Section 74 of the Indian Contract Act, as pointed out above. Section 74 of the Indian Contract Act, categorically states that in a case to which that section applies, the aggrieved party will be entitled to a reasonable compensation irrespective of the fact whether he has actually suffered any loss or damage or not. Therefore, from both these points of view, the conclusion of the Tribunal is erroneous and the order of remand based on such erroneous assumption of law cannot be sustained.

13. In my opinion, the duty of the Tribunal is to see whether the sum of Rs. 25 per tonne mentioned in Bye-law No. 39 can be said to be a 'reasonable compensation' taking into account all the circumstances of the case. If the second respondent-Tribunal comes to the conclusion that the said sum of Rs. 25 per tonne is a reasonable compensation, no further question will arise and the petitioner will be entitled to recover the same from the first respondent. Even if the second respondent-Tribunal comes to the conclusion that the reasonable compensation will be in excess of the sum of Rs. 25 per tonne mentioned in Bye-law No. 39, then also no further question will possibly arise and the petitioner herein will be entitled to the sum of Rs. 25 per tonne only as mentioned in Bye-law No. 39. Only if the Tribunal comes to the conclusion that the sum of Rs. 25 per tonne fixed in Bye-law No. 39 is in excess of the reasonable compensation, the question of assessing the quantum of compensation will arise, and that has to be determined with reference to all the circumstances of the case.

14. It is in this context I wanted to refer to one more error which the second respondent-Tribunal has committed. The Tribunal has pointed out that the petitioner must show that the Mills did not get the required quantity of sugarcane for crushing every day or that the Mills had to be closed in advance of the usual period of operation for want of sugarcane and if sugarcane had been purchased from third parties and for higher rates, the petitioner must show that such sugarcane had been purchased and that thereby the Mills had to incur losses and that without adducing proof of any of

those things, it is not open to the petitioner to ask for decrees or awards against first respondent and others merely on the ground that they had not honoured their commitments as per the bye-laws and merely on the ground that the bye-laws provide a certain amount as penalty leviable on the defaulting members. In so stating, in addition to committing the errors which I have already referred to, the second respondent-Tribunal has committed another error. The Tribunal construed Bye-law No. 39 in isolation as if it constituted an independent contract between a buyer and a seller. The question of the aggrieved party purchasing the goods in open market and thereby suffering losses will arise only in a contract for sale and purchase. Here, Bye-law No. 39 is only a term in a contract entered into between the society and its members, the entirety of the bye-laws constituting the contract. Therefore, for the purpose of arriving at a conclusion as to what would be the reasonable compensation to which the society will be entitled, on the admitted case of a breach on the part of the first respondent, the Tribunal should prominently bear in mind this fact, namely, that the entirety of the bye-laws constituted the contract between the petitioner-society and the first respondent conferring rights and imposing obligations and governing their relations and Bye-law No. 39 is only one of the terms of the contract. The bye-laws of the society make it clear that only a person who owns or cultivates lands fit for sugarcane cultivation is eligible for admission as a member. The bye-laws also provide for the board of directors of the society giving money advances to members not exceeding Rs. 500 per acre of their lands planted with sugarcane for supply to the society and that money being recovered in a particular manner.. The bye-laws further provide for sharing of the net profits of the society in a particular manner and also provide for several other facilities to be made available to the members concerned. Bye-law No. 39 having imposed an obligation on the sugarcane grower member to supply cane to the society at the rate mentioned therein, Bye-law No. 40 imposes an obligation on the board of directors to buy outright the sugarcane delivered to the society by the members in accordance with Bye-law No. 39 at the price, if any, fixed by the Government or where no price has been fixed by the Government at the rate fixed by the board with reference to the prevailing market rate. One other thing that should not be ignored is that the petitioner happens to be a cooperative society and the profit earned or the loss sustained by the society will have to be ultimately shared by the members of the society and by the default committed by one or more of the members in the performance of their obligations under Bye-law No. 39, the other members should not be subjected to loss or difficulties. The second respondent-Tribunal itself has pointed out that the Government of Madras, the Industrial Investment Corporation and some banks had advanced huge amounts to the petitioner and that unless all the members contribute their due quota of sugarcane to enable the Mills to work regularly year after year, the Mills would not be able to discharge the liabilities. It was also pointed out that the cane was being purchased at Rs. 55 per tonne and therefore the amount of Rs. 25 per tonne would not have been a genuine pre-estimate of damages. But the Tribunal forgot to note that this amount of Rs. 25 per tonne fixed in Bye-law No. 39 is irrespective of the price of the sugarcane and even when the price of sugarcane goes up, still it is the the amount of Rs. 25 per tonne that will be recoverable by the society. One other aspect of the matter is that Bye-law No. 39 merely enables the board of directors to recover compensation of Rs. 25 per tonne and taking into account if the circumstances of a particular year the board of directors may not claim anything in that year or may claim a sum less than Rs. 25 per tonne. As far as the present claim for Rs. 25 per tonne is concerned, the affidavit filed in support of this writ petition points out that the amount was originally fixed at Rs. 10 in the bye-law in question and since it was found that it was not sufficient to cover the loss

sustained by the society, the society at its general body meeting on 20th August, 1965, passed a resolution unanimously to enhance the amount from Rs. 10 to Rs. 25 per tonne. The affidavit further points out that for the year 1966-67 the petitioner-society suffered a loss of Rs. 7,07,551-18 (said to be a tentative figure) and for the year 1967-68 it suffered a loss of Rs. 9,20,874-73 (said to be tentative figure). All these factors should be taken into account in coming to the conclusion as to what would be the reasonable compensation to which the petitioner-society will be entitled, in respect of the breach committed by the first respondent with reference to Bye-law No. 39.

15. It should be also be noticed that the bye-law in question might have provided for the payment of Rs. 25 per tonne as compensation or fine for breach committed by a member, only because the precise determination of the actual loss or damage that would be caused to the society was impossible. When, out of the numerous members of the society, one or two alone commits or commit default with reference to Bye-law No. 39, it may be that the society has not suffered any loss by such default. On the other hand, if several of the members commit breach of their obligation under Bye-law No. 39, the loss suffered by the society may be subsantial. In such a case it will be impossible for the society to establish the actual loss of damage sustained by it with reference to the breach committed by each one of the members independently. The society can claim compensation only from each-one of the members individually with reference to the breach committed by him and cannot claim any compensation collectively against all the members who are guilty of the breach. All these circumstances may be indicative of the difficulty of establishing the actual loss or damage caused to the society by the breach committed by any one member. Mr. M. S. Venkatarama Iyer, learned Counsel for the first respondent, contended that the society must prove the loss or damage sustained by it, as a result of the breach committed by several of the members of the society and apportion the loss as between the several members and the loss so apportioned alone can be recovered from the first respondent herein. I am unnable to accept this contention and there is nothing in law to support such a contention. As Lord Dunedin has pointed out in Dunlop Pneumatic Tyre Company Ltd. v. New Garage and Motor Co. Ltd. (1915) A.C. 79, which I have extracted already:

> It is no obstacle to the sum stipulated being a genuine pre-estimate of damage, that the consequences of the breach are such that as to make precise pre-estimation almost an impossibility. On the contrary, that is just the situation when it is probable that pre-estimated damage was the true bargain between the parties.
>
> In that case, the Dunlop Company supplied tyres to the defendants under an agreement headed "Price Maintenance Agreement", by which the defendant bound themselves not to tamper with the marks on the goods, not to sell or offer the goods to any private customers or to any co-operative society at less than the appellant's current list prices, not to supply to persons whose supplies the appellants had decided to suspend, not to exhibit or export without the consent of the appellants, and to pay the sum of 5£ by way of liquidated damages for every tyre, cover, or tube sold or offered in breach of the agreement. It was held in that case that the sum of 5£ was liquidated damages and that the plaintiffs were entitled to recover the same. Really speaking, if the defendants had sold any tyre or tube or cover below the listed

price, the plaintiffs had not actually suffered any damage because they had received the price from the defendants. But the damage consisted in underselling their product and their trade reputation being affected. In such a situation, it would be impossible to make a precise estimate of the actual damage or loss sustained by the Dunlop Company. It is because of this Lord Dunedln, pointed out:

But though damage as a whole from such a practice would be certain, yet damage from any one sale would be impossible to forecast. It is just, therefore, one of those cases where it seems quite reasonable for parties to contract that they should estimate that damage at a certain figure, and provided that figure is not extravagant there would seem no reason to suspect that it is not truly a bargain to assess damages, but rather a penalty to be held in terrorem.

It is because of the features mentioned above, Lord Atkinson, also pointed out:

In the sense of direct and immediate loss the appellants lose nothing by such a sale. It is the agent or dealer who loses by selling at a price less than that at which he buys, but the appellants have to look at their trade in globo, and to prevent the setting up, in reference to all their goods anywhere and everywhere, a system of injurious undercutting.

Similarly Lord Mersey, in Webster v. Bosanquet (1912) A.C. 394 at 398, pointed out:

When making the contract it was impossible to foresee the extent of the injury which might be sustained by the plaintiff if sales of tea were made to third parties without his consent. That such sales might seriously affect his business was obvious, and the very uncertainty of the loss likely to arise made it most reasonable for the parties to agree beforehand as to what the damages should be. And, furthermore, it is well-known that damages of this kind, though very real, may be difficult of proof, and that the proof may entail considerable expense.

Tindal, C.J., in Kemble v. Farren 6 Bing. 141 at 148, said:

We see nothing illegal or unreason-able in the parties, by their mutu agreement, settling the amount damages, uncertain in their nature, any sum upon which they may agree.

In the present case also, though it is certain that the petitioner society will suffer losses as a consequence of several members of the society not honouring their commitments under Bye-law No. 39, it may be difficult to establish the actual loss or damage sustained by the petitioner society by the default committed by any one single individual member. It is precisely this aspect of the matter that has to be borne in mind by the second respondent-Tribunal in determining what would be the reasonable compensation the petitioner-society would be entitled to.

16. In this context, it is interesting to note the following statement contained in the Law of Contract, Cheshire and Fifoot, Seventh Edition, at page 565:

> In conclusion, it is well to heed the salutary warning of Diplock, L.J., in Robopkone Facilities Ltd. v. Blank (1966) 1 W.L.R. 1428 at 1447, that:
>
> 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 ".
>
> Such a stipulation reflects good business sense and is advantageous to both parties. It enables them to envisage the financial consequences of a breach; and if litigation proves inevitable it avoids the difficulty and the legal costs, often heavy, of proving what loss has in fact been suffered by the innocent party.

17. Considering all these circumstances, I am of the opinion that the second respondent Tribunal committed an error of law in remanding the matter to the Co-operative Sub-Registrar with the direction that the petitioner society must prove that it had factually suffered loss or damage and then further prove the extent of such loss or damage and it an recover only the compensation for ?h loss or damage suffered by it. On other hand, the legal position is that second respondent will have to consider, with reference to all the circumstances of the case, whether the sum of Rs. 25 per tonne provided for in Bye-law No. 39 and claimed by the society constituted reasonable compensation to which the petitioner society is entitled because of the breach committed by the first respondent. If the second respondent comes to the conclusion that the said sum of Rs. 25 per tonne is a reasonable compensation, it will have no alternative but to dismiss the appeal of the first respondent. Equally, if the second respondent comes to the conclusion that the reasonable compensation will be only in excess of Rs. 25 per tonne, then also it will have no alternative but to dismiss the appeal of the first respondent. Only if the second respondent comes to the conclusion that the reasonable compensation to which the petitioner is entitled will be less than Rs. 25 per tonne, it will be justified in interfering with the award of the Co-operative Sub-Registrar and decreeing the claim of the petitioner to the extent of the reasonable compensation determined by it. Whether the petitioner led any evidence to prove the extent of the actual damage or loss suffered by it or not could not have been the subject-matter of grievance of the first respondent, because all that the petitioner would be entitled to is only a reasonable compensation, in the determination of which the actual damage or loss suffered by the petitioner will only be a factor to be taken note of. Whether the remand in the present case is called for or not will have to be decided by the second respondent only after a consideration of all these aspects of the matter.

18. I am unable to accept the argument of Mr. Venugopal, that the principles contained in Section 74 of the Indian Contract Act, cannot be applied to the Bye-law in question. Section 74 of the Indian Contract Act, constitutes the law of the land in this behalf and every Court, every Tribunal and every Arbitrator has to apply that law and none can ignore or by pass that law. As a matter of fact, Section 1 of the Indian Contract Act itself provides:

> 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.
>
> In view of this, if the incident of Bye-law No. 39 is not consistent with Section 74 of the Indian Contract Act, then naturally that section will affect the same. As I have pointed out already, Section 74 of the Indian Contract Act, actually contemplates a contract containing a stipulation for payment of penalty and provides that even in such cases the aggrieved party will be entitled only to a reasonable compensation not exceeding the penalty so stipulated. Therefore, neither the Cooperative Sub-Registrar nor the second' respondent Tribunal can ignore Section 74 of the Indian Contract Act, and the same is binding on them. I have already held that there is no question of Bye-law No. 39 being illegal and the only question is the enforcement of that Bye-law in accordance with the provisions contained in Section 74 of the Indian Contract Act.

19. In view of this conclusion, I hold that there is no substance in the contention of Mr. Venugopal that neither the Cooperative Sub-Registrar nor the Tribunal had jurisdiction to go into the validity of the Bye-law. This is apart from the fact that the Bye-law constituted only a contract and every Tribunal will have to decide the effect and incident of the contract in accordance with the law of the land.

20. For the same reason, the first respondent cannot be precluded from contending that the petitioner herein would not be entitled to recover a sum of Rs. 25 per tonne simpliciter and would be entitled to claim only a reasonable compensation as provided for in Section 74 of the Indian Contract Act.

21. In the above circumstances, the writ petition is allowed and the impugned order of the second respondent Tribunal is quashed. The result of this will be the Tribunal will have to restore the appeal of the first respondent to its file and dispose it of afresh in accordance with law and in the light of this judgment. There will be no order as to costs.