



Damages Under Law of Contract: A Remedy or Penalty

Saroj Saini

Research Scholar, Department of Law, K.U.K., Distt. S.A.S. Nagar,
Pin: 160104

ABSTRACT

"Ubi Jus Ibi Remedium" is a Latin legal maxim which means "where there is a right there is a remedy", which means that, when a person's right is violated the victim will have an equitable remedy under law. This article is aimed at making an analysis of the two most important words used in Sections 73 and 74 of Indian Contract Act, 1872 i.e. "Damages" and "Penalty". In this article, an effort has been made to analyse all the perspectives and all the ways in which these words can be construed so that one can easily conclude the real meaning and sense of these sections. These two words are not defined under the same as to what does they mean or include.

KEYWORDS

CONTRACT, REMEDY, DAMAGES, PENALTY.

INTRODUCTION:-

"**Ubi Jus Ibi Remedium**" is a Latin legal maxim which means "where there is a right there is a remedy". The basic principle contemplated in the maxim is that, when a person's right is violated the victim will have an equitable remedy under law. The maxim also states that the person whose right is being infringed has a right to enforce the infringed right through any action before a court. This article is aimed at making an analysis of the two most important words used in Sections 73 and 74 of Indian Contract Act, 1872 i.e. "Damages" and "Penalty". These two words are not defined under the same as to what does they mean or include. Actually, what exactly these sections mean and includes and what are the interpretation of said sections is a matter of understanding and moreover the interpretation of said sections may differ in different cases. So, in this article an effort has been made to analyse all the perspectives and all the ways in which these words can be construed so that one can easily conclude the real meaning and sense of these sections. Reason being provisions of law should be used, not misused.

MEANING OF REMEDY:-

The manner in which a right is enforced or satisfied by a court when some harm or injury, recognized by society as a wrongful act, is inflicted upon an individual, it is called remedy. According to the purpose of remedy, the four basic types of judicial remedies are:-

- (1) Damages
- (2) Restitution
- (3) Coercive remedies; and
- (4) Declaratory remedies.

Remedies may be considered in relation to:

1. The enforcement of contracts.
2. The redress of torts or injuries.

The main focus of this paper is in relation to the enforcement of contracts. The remedies for the enforcement of contracts are generally by action. The form of these remedies depends upon the nature of the contract.

Breach of contract:-

Indian Contract Act, 1872 speaks of consequences of breach, rather than remedies for breach. Breach of contract is a legal cause of action in which a binding agreement is not honoured by one or more of the parties to the contract by non-performance or interference with the other party's performance. If the party does not fulfil his contractual promise, or has given information to the other party that he will not perform his duty as mentioned in the contract or if by his action and con-

duct he seems to be unable to perform the contract, he is said to make a breach the contract. The breach of contract may be: A) actual or B) anticipatory.

- ❖ The actual breach may take place either at the time the performance is due, or when actually performing the contract.
- ❖ The anticipatory breach, i.e., a breach before the time for the performance has arrived.

When a breach of contract takes place, the remedy of damages is the logical consequence of breach. The aggrieved party may seek compensation from the party who breaches the contract. When the aggrieved party claims damages as a consequence of breach, the court takes into account the provisions of law in this regard and the circumstances attached to the contract. The fact is that both damages and penalty are a form of economic gain which are payable by the defaulter to the innocent party that has suffered a loss due to the breach. This can be observed by:

- I. Analysis of what damages mean and ought to mean under Section 73.
- II. Analysis of what penalties mean and ought to mean under Section 74.
- III. Critically analysing as to the reason why penalty and damages are confused to mean the same and what is that point of difference between the two words and there usage. So, for the clear understanding of the above mentioned concepts, one should do intensive study of the meaning of these under law of contract as well.

Meaning of Damages: -

The theory of damages is that they are a compensation and satisfaction for the injury sustained, i.e. the sum of money to be given for reparation of the damages suffered should as nearly as possible, be the sum which will put the injured party in the same position as he would have been if he had not sustained the wrong for which he is getting damages.

Definitions:-

- Black's law dictionary: "Damages are the sum of money claimed by or ordered to be paid to a person as compensation for loss or injury."
- Acc. to Frank Graham: "Damages are the sum of money which a person wronged is entitled to receive from the wrong doer as compensation for the wrong."

Judicial interpretation of damages:-

In *Sohm v. Dixie Eye*, Justice Greenwood of the Court of Ap-

peals of Utah adopted these words: "damages" generally refers to money claimed by, or ordered to be paid to, a person as compensation for loss or injury. "The term injury is sometimes used in the sense of damage, as including the harm or loss for which compensation is sought, and has been defined as damage resulting from an unlawful act; but in strict legal significance, there is, properly speaking, a material distinction between the two terms, in that injury means something done against the right of the party, producing damage, whereas damage is the harm, detriment, or loss sustained by reason of the injury."

Damages under Law of Contract in India:-

The Indian Contract Act, 1872 uses the words loss or damage under Section 73 as: 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 of damage sustained by reason of the breach. The law is well settled that a claim for unliquidated damages does not give rise to a debt until the liability is adjudicated and damages assessed by a decree or order of a court or other adjudicatory authority. The only right which the party aggrieved by the breach of the contract is the right to sue for damages. That is not an actionable claim.

Penalty:-

Penalty under law of contract does not mean punishment to the wrong doer. It is used in quite different sense. It is totally different from punitive damages. As punitive damages means monetary compensation awarded to an injured party that goes beyond which is necessary to compensate the individual for losses and that is intended to punish the wrongdoer. The purposes of punitive damages are to punish the defendant for outrageous misconduct and to deter the defendant and others from similar misbehaviour in the future. While it is not so, in case of penalty stipulated for under sec. 74 of Indian Contract Act 1872. The Indian Contract Act, 1872 uses the words penalty under section 74 as: "Compensation of breach of contract where penalty stipulated for :-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 or 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." In section 74 the words that have to be emphasized upon are "sum is named". The term 'sum is named' gives out the clear meaning that the amount that becomes payable in the event of any breach is pre-estimated and is provided for in the contract. It is determined in the form of either damages or a stipulated penalty. Further, they sum that is so specified is the reasonable compensation for the breach and in no case the amount can be exceeded from what has been specified in the contract. Thus, in short section 74 talks about liquidated damages and not other kind of damages. Liquidated damages: (not defined in the Indian Contract act, 1872) If the sum fixed represents a genuine pre-estimate of the probable damages that is likely to result from the breach, it is liquidated damages.

Liquidated Damages and Penalty:-

Where the contract itself addresses the issue of consequences of a breach and stipulated a penalty, Section 74 of the Indian Contract Act will come into play. When such a contract has been broken, if a sum is named in the contract as the amount to be paid in case of such breach, the party complaining of breach is entitled, to receive from the party who has broken the contract a reasonable compensation not exceeding the amount so named.

Judicial Interpretation of Damages and Penalty:-

An amount contractually stipulated as a reasonable estimate of actual damages to be recovered by one party if the other party breaches. It means that it shall be taken as the sum which the parties have by contract assessed as damages to be paid whatever maybe the actual damage. The Hon'ble Supreme court in *Fateh Chand v. Balkishan Das* held that the jurisdiction of the court to award compensation under section 73 in case of breach of contract is unqualified except as to the maximum stipulated, and compensation has to be reasonable. This section has to be read in conjunction with section 74, which emphasizes that in case of breach of contract, the party complaining of the breach is entitled to receive reasonable compensation whether or not the actual loss is proved. A fixed figure of damages, which is not assessed for all circumstances, but is graduated to correspond with passage of time between the making of contract and of its breach, is a proper estimate of the damage to be anticipated from the breach, and is recoverable as liquidated damages. In *Oil and Natural Gas Corporation Ltd. v. Saw Pipes Ltd.* the Supreme court laid down the following guidelines:-

1. Terms of the contract are required to be taken into consideration before arriving at the conclusion whether the party claiming is entitled to the same.
2. If the terms are clear and unambiguous stipulating liquidated damages in case of the breach of the contract, unless it is held that such estimate of damages/compensation is unreasonable or is by way of penalty, the party who has committed the breach is required to pay such compensation and that is what is provided in section 73 of the Contract Act.
3. Section 74 to be read along with section 73 and, therefore, in every case of breach of contract, the person aggrieved by the breach is not required to prove actual loss or damage suffered by him before he can claim a decree. The court is competent to award reasonable compensation in case of breach even if no actual damage is proved to have been suffered in consequences of the breach of the contract.
4. In some contracts, it would be impossible for the court to assess the compensation arising from breach and if the compensation contemplated is not by way of penalty or unreasonable, the court can award the same if it is a genuine pre-estimate by the parties as the measure of reasonable compensation.

In *Steel Authority of India v. Gupta Brothers Steel Tubes Ltd.* it was held by the Apex court that there is no impediment or any obstacle for the parties to a contract to make provisions of liquidated damages for specific breaches only, leaving other types of breaches to be dealt with as unliquidated damages. *Bhuley Singh v. Khazan Singh and Ors* the Supreme Court held that Section 74 declares the law as to liability upon breach of contract where compensation is by agreement of the parties pre-determined, or where there is a stipulation by way of penalty. But the application of the enactment is not restricted to cases where the aggrieved party claims relief as a plaintiff. The section does not confer a special benefit upon any party; it merely declares the law that notwithstanding any term in the contract predetermining damages or providing for forfeiture of any property by way of penalty, the court will award to the party aggrieved only reasonable compensation not exceeding the amount named or penalty stipulated. The jurisdiction of the court is not determined by the accidental circumstance of the party in default being a plaintiff or a defendant in a suit. Use of the expression "to receive from the party who has broken the contract" does not predicate that the jurisdiction of the court to adjust amounts which have been paid by the party in default cannot be exercised in dealing with the claim of the party complaining of breach of contract. The court has to adjudge in every case reasonable compensation to which the plaintiff is entitled from the defendant on breach of the contract. Such compensation has to be ascertained having regard to the conditions existing on the date of the breach. High amounts called earnest money

will be in the nature of penalty and thus hit by Section 74 of the Indian Contract Act, 1872 in view of Fateh Chand's case. The principles laid down in Fateh Chand's case; that forfeiture of a reasonable amount is not penalty but if forfeiture is of a large amount the same is in the nature of penalty attracting the applicability of Section 74; have been recently reiterated by the Supreme Court in the case of V. K. Ashoka v. CCE .

CONCLUSION:-

Due to the aggressive growth in the field of technology, the parties entering into commercial transactions are more cautious than ever, thus making the parties deliberate even on the minute details or specifications so as they can best secure their interest. Therefore, contents of a contract have become highly detailed and elaborate. Particularly, as a measure of safeguarding, securing and protecting their respective interests in an event of breach of the terms of the contract, parties

generally negotiate and agree upon the various remedies that the injured party can invoke to mitigate and compensate for the losses it may suffer on account of such breach. Therefore, with regard to liquidated damages and penalties, the primary conclusions of the court appear to be that liquidated damages should be regarded as reasonable compensation, while penalties should not. Further, it also appears to have concluded that in case of a penalty, damages will have to be proved. The courts in India should interpret the above mentioned sections i.e. sec.73 and 74 very carefully, so that the ordinary man can be benefited by these principles. Moreover, the law is made to facilitate the people, not to harass them. So, these principles should be used, not misused.

REFERENCES

ARTICLES: | Contract Interpretation Redux Schwartz, Alan; Scott, Robert E. The Yale Law Journal, Vol. 119, No. 5, March 2010 | Wood, Robert W. 2003. "Proposed Non deductibility for Punitive Damages: Will It Work?" Tax Notes (July 7). | BOOKS: | "Contract Law", Pathak, Akhileshwar, IIM, Ahmadabad, Oxford University Press: 2011 | "Law Relating to Damages, Claims & Compensation", Mitra, S.C., Orient Publishing Co., 2013. | ELECTRONIC RESOURCES: | www.manupatra.com | <http://www.allindia reporter.com/> | www.west.net/~smith/damages.html | books.google.com > Law > Contracts |