IN THE HIGH COURT OF KERALA AT ERNAKULAM

PRESENT

THE HONOURABLE MR. JUSTICE P.B.SURESH KUMAR

&

THE HONOURABLE MRS. JUSTICE C.S. SUDHA

WEDNESDAY, THE 16TH DAY OF FEBRUARY 2022 / 27TH MAGHA, 1943

ARB.A NO. 29 OF 2018

AGAINST THE ORDER/JUDGMENT IN OP(ARB.) 105/2015 OF DISTRICT COURT, KASARAGOD

APPELLANT/S:

M/S. DEVCHAND CONSTRUCTION,
THOKKOTTU-PERUMANNUR POST, MANGALORE - 575017,
REPRESENTED BY ITS PROPRIETOR, MR.DINAKAR ULLAL.

BY ADVS.
SMT.SANTHA VARGHESE
SRI.RANJITH VARGHESE
SRI.RAHUL VARGHESE

RESPONDENT/S:

UNION OF INDIA,
REPRESENTED BY THE DEPUTY CHIEF ENGINEER (CONSTRUCTION), SOUTHERN RAILWAY, KANNUR-670001.

BY ADV SRI.S.ANANTHAKRISHNAN, SC, RAILWAYS

THIS ARBITRATION APPEALS HAVING COME UP FOR ADMISSION ON 16.02.2022, THE COURT ON THE SAME DAY DELIVERED THE FOLLOWING:

"C.R."

P.B. SURESH KUMAR & C.S. SUDHA, JJ.

Arb. Appeal No.29 of 2018

Dated this the 16th day of February, 2022

JUDGMENT

C.S.Sudha, J.

This appeal filed under Section 37 of the Arbitration and Conciliation Act, 1996 (the Act), is against the order dated 04.12.2017 in O.P.(Arb.) No.105/2015 of the District Court, Kasaragod.

2. The appellant herein is the petitioner before the court below and the claimant before the Arbitral Tribunal (AT). The respondent herein is the respondent before the court below and the respondent before the AT. The parties in this appeal will be referred to as described in the arbitral proceedings.

3. The respondent awarded the work of 'doubling of track between Shornur and Mangalore, Cannanore-Uppala section: collection and stacking of 50mm size machine crushed hard stone ballast alongside the alignment/station yards/ on top of the new formation between Kottikulam

and Kasaragod stations (Balance works)' to the claimant on 19.09.2000 for a value of ₹ 1,19,39,274/-. Letter of Acceptance (LoA) was issued on 19.09.2000. The work was to be completed within a period of nine months, that is, by 18.06.2001. Alleging breach on the part of the claimant, the contract was terminated by the respondent before the expiry of the completion period. Disputes arose between the parties. Arbitration proceedings was initiated. The AT consisting of three Arbitrators passed an award on 24.04.2015. The AT disallowed all the claims of the claimant except claim no. 1 for release of an amount of ₹ 3,46,959/-, which amount had been forfeited by the respondent towards risk liability amount. This claim was partly allowed to the tune of ₹ 46,959/-. All the other claims including the prayer for return of the Earnest Money Deposit (EMD) was rejected. Aggrieved, the claimant/contractor took up the matter before the District Court. The said Original Application filed under s.34 of the Act was dismissed by the impugned order.

4. Heard Shri.Rahul Varghese, the learned counsel for the appellant and Shri.Ananthakrishnan, the learned Standing Counsel for the Railways.

5. In the appeal memorandum it is stated that during the pendency

of the proceeding before the court below, the respondent released the EMD amounting to ₹50,000/-. This according to the claimant has been done when the respondent realized that it was illegal for them to have withheld the same, especially when they had not suffered any loss or damage. Therefore, the only point to be decided in this appeal is whether there is any infirmity in the finding of the AT that the respondent is entitled to forfeit the security deposit of ₹ 3 lakhs towards risk liability in the absence of any loss or damage. According to the AT, the claimant had failed to execute the work and hence the contract had been terminated at his risk and cost in terms of Clause 62 of the General Conditions of Contract. An amount of ₹ 3 lakhs deposited as security deposit and an amount of ₹ 46,959/- towards advertisement charges had been deducted by the respondent from the final bill as the amount towards risk liability. The AT concluded that since the breach of the contract had been committed by the claimant/contractor, the security deposit of ₹ 3 lakhs is liable to be forfeited and therefore out of the total amount of ₹3,46,959/- claimed by the claimant, only an amount of ₹ 46,959/- was allowed. However, in the award itself it is stated that no loss/damage had been caused to the respondent. Therefore, it is submitted by the learned counsel for the claimant/contractor that in such circumstances

the forfeiture of ₹3 lakhs deposited as security deposit is patently wrong, illegal and perverse. Reference was made to the decisions in **Fateh Chand vs. Balkishan Dass [1963 SC 1405]; State of Kerala vs. United Shippers and Dredgers Ltd. [AIR 1982 Ker 281]; Abdulla vs. State of Kerala [2001 KHC 822]** and **Kailash Nath Associates vs. Delhi Development Authority [(2015)4 SCC 136]** in support of this argument.

6. Here we need to refer to Sections 73 and 74 of the Indian Contract Act, 1872. Section 74 of reads thus -

> *"74* ***Compensation for 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 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."*

7. As laid down in the aforesaid decisions, in a case coming under Section 74, it is not necessary for the party claiming compensation under this Section to prove that actual damage or loss has been caused. Then the question is whether even in the absence of legal injury, compensation is liable to be paid for breach simplicitor. Under Section 74, whether it is a

case of liquidated damages or penalty, what the party faced with the breach gets is only reasonable compensation, subject to the limit of the amount stipulated in the contract itself. Section 74 dispenses with proof of the extent of real or actual or factual loss or damage, but provides for grant of reasonable compensation, subject to the condition that it shall not exceed the sum stipulated as penalty in the contract. The proof of the extent of loss or damage suffered in fact, i.e., proof of the extent of actual damage or loss suffered is dispensed with in Section 74. This would not mean that there need not be any loss or damage. What is meant is only that proof of actual damage or loss is not necessary.

8. In the case on hand, it cannot be Section 74 that could have been invoked, because the Award does not say that any sum has been named in the contract as the amount to be paid in case of breach. In other words, the parties had never made a genuine pre-estimate of the amount to be paid in the event of any damage or loss likely to be caused by the breach or that there is any clause relating to liquidated damages in the contract.

9. Section 73 reads-

> *"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."*

10. The words 'loss or damage' in the aforesaid sections would necessarily indicate that the party who complains of breach must have really suffered some loss or damage apart from being faced with the mere act of breach of contract. That is because every breach of every contract need not necessarily result in actual loss or damage. Compensation payable under Section 73, 74 as also under Section 75 is only for loss or damage caused by the breach and not account of the mere act of breach. If in any case the breach has not resulted in or caused any loss or damage to a party, he cannot claim compensation.

11. Further, in **Union of India v. Rampur Distillery and Chemical Co. Ltd. (AIR 1973 SC 1098) the Apex Court** held that a party to a contract taking security deposit from the other party to ensure due performance of the contract, is not entitled to forfeit the deposit on ground of default when no loss is caused to him in consequence of such default. When the question is one of forfeiture of security deposit in case of breach of

contract, such sum does not *ipso facto* go to the respondents. If the party complaining is in a position to adduce evidence whereby the court can assess reasonable compensation, then without proof of actual loss, damages will not be awarded and amount mentioned by the contract will be penalty. In such circumstances, it has been held that the security amount is liable to be forfeited.

12. As noticed earlier, the Award in this case clearly says that no loss or damage has been caused to the respondent. That being the position, neither the provisions of Sections 73, 74 or 75 could have been invoked nor are they applicable in this case. That being the position, the AT was certainly wrong in rejecting the claim of the claimant for release of the amount of security deposit of ₹ 3 lakhs. This finding in violation of the provisions of Sections 73 to 75 of the Contract Act, is certainly in contravention of the fundamental policy of Indian Law as contemplated in Section 34(2)(b)(ii) of the Act.

In the result, the appeal is allowed. The impugned order dated 4.12.2017 in O.P.(Arb.) No.105/2015 is set aside. The Award to the extent it disallows Claim No.1 for the release of security deposit of ₹ 3 lakhs towards risk liability amount, is set aside and the said claim shall stand allowed. The

amount has been withheld without any justification and therefore the amount of ₹ 3 lakhs will be returned by the respondent to the claimant with interest @ 6% p.a. from the date of moving the claim before the AT till realisation and costs.

sd/

P.B.SURESH KUMAR, JUDGE.

sd/-

C.S.SUDHA, JUDGE.

STK