SUPREME COURT OF INDIA

M/S. Construction & Design Services

Vs.

Delhi Development Authority

C.A.Nos.1440-1441 of 2015

(T.S.Thakur and Adarsh Kumar Goel JJ.)

04.02.2015

JUDGMENT

ADARSH KUMAR GOEL, J.

1. Leave granted.

2. These appeals have been preferred against final judgment and order dated 10th February, 2012 in RFA(OS) No.35 of 2010 and dated 1st June, 2012 in R.P. No.369 of 2012 in RFA (OS) No.35 of 2010 passed by the High Court of Delhi at New Delhi.

3. The question raised for our consideration is when and to what extent can the stipulated liquidated damages for breach of a contract be held to be in the nature of penalty in absence of evidence of actual loss and to what extent the stipulation be taken to be the measure of compensation for the loss suffered even in absence of specific evidence. Further question is whether burden of proving that the amount stipulated as damages for breach of contract was penalty is on the person committing breach.

4. The respondent - Delhi Development Authority awarded a contract vide agreement dated 4th October, 1995 to the appellant for constructing a sewerage pumping station at CGHS area at Kondli Gharoli at Delhi. Clause 2 in the agreement provided as follows:

> "the contractor shall comply with the said time schedule. In the event of the contractor failing to comply with this condition, he shall be liable to pay as compensation an amount equal to one percent or such smaller amount as the

Superintending Engineer Delhi Development Authority (whose decision shall be final) may decide on the said estimated cost of the whole work for everyday that the due quantity of work remains incomplete; provided always that the entire amount of compensation to be paid under the provisions of this clause shall not exceed ten percent of the estimated cost of work as shown in the tender."

Since the work proceeded at slow pace and the appellant-defendant failed to complete the same, the contract was terminated on 17th September, 1999. Under Clause 2 of the agreement, the Superintending Engineer of the respondent levied compensation of Rs.20,86,446/- for delay in execution of the project by an order of penalty dated 21st July, 1999 and called upon the appellant to deposit the same. The said order reads thus : "The work was being executed by you at extremely slow pace. You had to complete the job by 7.1.97. You had failed to complete the work even after expiry of 2 years six months after stipulated date of completion. Despite the clear direction from Hon'ble Supreme Court to expedite the work and complete the job by June-99, you have failed to comply the direction of Court and have rather abandoned the work since 6.4.99 and you failed to complete the work till date.

In exercise of the power conferred on me under clause-2 of the agreement, I, R.C. Kinger, the SE/CC-10/DDA decide and determine that you are liable to pay Rs.20,86,446/- (Rs. Twenty lacs eighty six thousand four hundred forty six only) as and by way of compensation as stipulated in clause-2 of the agreement."

5. On failure of the appellant to respond to the above order, the respondent filed suit No.1311 of 2002 before the Delhi High Court for recovery of the said amount with interest. The appellant-defendant failed to contest the suit inspite of service but made an application raising objection to the maintainability of the suit on the ground that vide order dated 19th December, 2001, a former Judge of Delhi High Court had been appointed arbitrator to decide the disputes arising out of the contract. The said application was, however, dismissed on the ground that the matter in the suit was not within the purview of the arbitration. The Court proceeded to decide the suit on merits.

6. Learned single Judge dismissed the suit holding that the plaintiff had not treated the time fixed for performance of the contract as of essence and the compensation stipulated in Clause 2 of the agreement was in the nature of penalty. The basis for

levy of compensation had not been indicated so as to determine whether the compensation claimed was reasonable. Reliance was placed on the judgment of this Court in M/s. Arosan Enterprises Ltd. vs. Union of India and another[1] in support of the view that the time stipulated in the agreement was not treated to be of essence. It was further observed that since the claim for compensation was based on sole discretion and not on the basis of loss suffered, the same was in the nature of penalty and thus, the said Clause could not be enforced in view of Section 74 of the Contract Act as laid down in Fateh Chand vs. Bal Kishan Das[2], Maula Bux vs. Union of India[3], M.L. Devendra Singh vs. Syed Khaja[4], P. D'Souza vs. Shondrilo Naidu[5] and Oil and Natural Gas Corporation Ltd. vs. Saw Pipes Ltd.[6]. Learned single Judge concluded as follows:-

> "20. The Court is of opinion that the plaintiff having not treated the contract as of the essence, and having extended the time for performance on several occasions, cannot now fall back on a presumptive condition to impose the maximum compensation leviable; enforcement of such action would be giving effect to a penalty clause. As far as granting reasonable compensation is concerned, the plaintiff has not shown even the basis for levying the compensation that it did in this case. As said earlier, this aspect assumes significance, because the plaintiff was aware what extent of the contract was performed, as well as what was the exact extent of loss, in monetary terms, either by way of payment to another contractor, or the amount spent for completing the work. In the circumstances, the Court is of opinion that the relief sought cannot be granted."
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> 7. On appeal, the Division Bench reversed the view taken by the learned single Judge. It was held that delay in a contract of construction of a public utility service could itself be a ground for compensation without proving the actual loss. Accordingly, the suit was decreed for payment of Rs.20,86,446/- with pendente lite and future interest @ 9% per annum. It was observed:
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> > "5. The respondent had been proceeded against ex-parte at the trial and has chosen not to appear even before us. The evidence led by the appellant has remained unrebutted.
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> > 6. Suffice would it be to state that the observations of the Supreme Court in para 68 of the decision reported as AIR 203 SC 2629 ONGC v. Saw Pipes Ltd. are squarely applicable in the instant case as per which delayed constructions such as completing construction of road or bridges within stipulated time would be difficult to be linked with actual loses suffered by

the State and in such cases the pre-estimated damages envisaged in the contract have to be paid.

7. Now, a Sewage Pumping Station is not something from which Revenue would be generated by the State. It is a public utility service and has a role to play in maintaining or preserving clean environment. If Sewage Pumping Station are not set up, sewage would stagnate as cess pools in low lying areas and would cause environmental degradation, both air and soil. That apart, in a delayed project, interest on blocked capital would obviously be a measure of damages.

8. The learned Single Judge has ignored as aforesaid and held that in the absence of proof of damages, compensation levied under clause-2 cannot be recovered. The learned Single Judge is incorrect in view of the law declared by the Supreme Court and thus we allow the appeal and set aside the impugned decree. Suit filed by the appellant is decreed in sum of Rs.20,86,446/- with pendente lite and future interest @ 9% per annum from date of suit till realization and the suit filed by the appellant is disposed of accordingly with costs all throughout."

8. The appellant filed a review petition which was dismissed.

9. We have heard learned counsel for the parties.

10. On 19th November, 2012 notice was issued subject to the appellant depositing the entire decretal amount in this Court and by a subsequent order, the amount was directed to be kept in term deposit for a period of one year to ensure for the benefit of the successful party. Accordingly, the amount of Rs.20,86,500/- is said to have been deposited which has been kept in FDR which is going to mature on 8th February, 2015.

11. Learned counsel for the appellant submitted that the Division Bench erred in holding that the entire amount of stipulated damages was genuine measure of compensation when instead of any fixed amount, only the maximum amount of compensation was stipulated. The contract in question only envisaged the upper limit of damages which could be claimed. It is submitted that the agreement quoted in earlier part of the order clearly shows that what is stipulated is that the compensation shall not exceed 10% of the estimated cost and the amount to be recovered as compensation was required to be determined by the Superintending Engineer. The respondent- plaintiff has failed to show the actual amount of loss

suffered in getting the work executed from any other contractor. In these circumstances, at best a part of it could be taken to be compensation and the remaining penalty. He submitted that the judgment of this Court in Saw Pipes Ltd. (supra) relied upon by the High Court is distinguishable in the fact situation of the present case. Without determining that the stipulated compensation was reasonable, the maximum amount stipulated could not be treated as compensation.

12. Learned counsel for the respondent-plaintiff on the other hand submitted that even though in the order passed by the Superintending Engineer no specific basis has been shown, notice was duly issued to the appellant defendant before determining the reasonable amount of compensation and claiming 10% of the project cost which was stipulated to be the maximum compensation, on account of delay in execution of the project. On failure of the appellant to respond, the entire amount has been rightly held to be the estimate of damages for the loss. Burden was on the defendant to show that no loss or lesser loss was suffered by the plaintiff.

13. We have given due consideration to the rival submissions.

14. There is no dispute that the appellant failed to execute the work of construction of sewerage pumping station within the stipulated or extended time. The said pumping station certainly was of public utility to maintain and preserve clean environment, absence of which could result in environmental degradation by stagnation of water in low lying areas. Delay also resulted in loss of interest on blocked capital as rightly observed in para 7 of the impugned judgment of the High Court. In these circumstances, loss could be assumed, even without proof and burden was on the appellant who committed breach to show that no loss was caused by delay or that the amount stipulated as damages for breach of contract was in the nature of penalty. Even if technically the time was not of essence, it could not be presumed that delay was of no consequence.

15. Thus, even if there is no specific evidence of loss suffered by the respondent-plaintiff, the observations in the order of the Division Bench that the project being a public utility project, the delay itself can be taken to have resulted in loss in the form of environmental degradation and loss of interest on the capital are not without any basis.

16. Once it is held that even in absence of specific evidence, the respondent could be held to have suffered loss on account of breach of contract, and it is entitled to compensation to the extent of loss suffered, it is for the appellant to show that

stipulated damages are by way of penalty. In a given case, when highest limit is stipulated instead of a fixed sum, in absence of evidence of loss, part of it can be held to be reasonable, compensation and the remaining by way of penalty. The party complaining of breach can certainly be allowed reasonable compensation out of the said amount if not the entire amount. If the entire amount stipulated is genuine pre-estimate of loss, the actual loss need not be proved. Burden to prove that no loss was likely to be suffered is on party committing breach, as already observed.

17. It is not necessary to refer to all the judgments on the point in view of categorical pronouncement of this Court in Saw Pipes (supra), laying down as follows:-

> "64. It is apparent from the aforesaid reasoning recorded by the Arbitral Tribunal that it failed to consider Sections 73 and 74 of the Indian Contract Act and the ratio laid down in Fateh Chand case wherein it is specifically held that jurisdiction of the court to award compensation in case of breach of contract is unqualified except as to the maximum stipulated; and compensation has to be reasonable. Under Section 73, when a contract has been broken, the party who suffers by such breach is entitled to receive compensation for any loss caused to him which the parties knew when they made the contract to be likely to result from the breach of it. This section is to be read with Section 74, which deals with penalty stipulated in the contract, inter alia (relevant for the present case) provides that 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, the party complaining of breach is entitled, whether or not actual 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. Section 74 emphasizes that in case of breach of contract, the party complaining of the breach is entitled to receive reasonable compensation whether or not actual loss is proved to have been caused by such breach. Therefore, the emphasis is on reasonable [pic]compensation. If the compensation named in the contract is by way of penalty, consideration would be different and the party is only entitled to reasonable compensation for the loss suffered. But if the compensation named in the contract for such breach is genuine pre-estimate of loss which the parties knew when they made the contract to be likely to result from the breach of it, there is no question of proving such loss or such party is not required to lead evidence to prove actual loss suffered by him. Burden is on the other party to lead evidence for proving that no loss is likely to occur by

such breach. Take for illustration: if the parties have agreed to purchase cotton bales and the same were only to be kept as a stock-in-trade. Such bales are not delivered on the due date and thereafter the bales are delivered beyond the stipulated time, hence there is breach of the contract. The question which would arise for consideration is - whether by such breach the party has suffered any loss. If the price of cotton bales fluctuated during that time, loss or gain could easily be proved. But if cotton bales are to be purchased for manufacturing yarn, consideration would be different.....

67. Take for illustration construction of a road or a bridge. If there is delay in completing the construction of road or bridge within the stipulated [pic]time, then it would be difficult to prove how much loss is suffered by the society/State. Similarly, in the present case, delay took place in deployment of rigs and on that basis actual production of gas from platform B-121 had to be changed. It is undoubtedly true that the witness has stated that redeployment plan was made keeping in mind several constraints including shortage of casing pipes. The Arbitral Tribunal, therefore, took into consideration the aforesaid statement volunteered by the witness that shortage of casing pipes was only one of the several reasons and not the only reason which led to change in deploym7ent of plan or redeployment of rigs Trident II platform B-121. In our view, in such a contract, it would be difficult to prove exact loss or damage which the parties suffer because of the breach thereof. In such a situation, if the parties have pre-estimated such loss after clear understanding, it would be totally unjustified to arrive at the conclusion that the party who has committed breach of the contract is not liable to pay compensation. It would be against the specific provisions of Sections 73 and 74 of the Indian Contract Act. There was nothing on record that compensation contemplated by the parties was in any way unreasonable. It has been specifically mentioned that it was an agreed genuine pre-estimate of damages duly agreed by the parties. It was also mentioned that the liquidated damages are not by way of penalty. It was also provided in the contract that such damages are to be recovered by the purchaser from the bills for payment of the cost of material submitted by the contractor. No evidence is led by the claimant to establish that the stipulated condition was by way of penalty or the compensation contemplated was, in any way, unreasonable. There was no reason for the Tribunal not to rely upon the clear and unambiguous terms of agreement stipulating pre-estimate damages because of delay in supply of goods. Further, while extending the time for delivery of the goods, the respondent was informed that it would be required to pay stipulated damages."

18. Applying the above principle to the present case, it could certainly be presumed that delay in executing the work resulted in loss for which the respondent was entitled to reasonable compensation. Evidence of precise amount of loss may not be possible but in absence of any evidence by the party committing breach that no loss was suffered by the party complaining of breach, the Court has to proceed on guess work as to the quantum of compensation to be allowed in the given circumstances. Since the respondent also could have led evidence to show the extent of higher amount paid for the work got done or produce any other specific material but it did not do so, we are of the view that it will be fair to award half of the amount claimed as reasonable compensation.

19. Accordingly, this appeal is partly allowed and the decree granted by the High Court is modified to the effect that the respondent-plaintiff is entitled to half of the amount claimed with rate of interest as awarded by the High Court. Out of the amount deposited in this Court, the respondent will be entitled to withdraw the said decretal amount and the appellant will be entitled to take back the remaining .

20. The appeals are disposed of accordingly.

[1] (1999) 9 SCC 449
[2] (1964) 1 SCR 515
[3] (1969) 2 SCC 554
[4] (1973) 2 SCC 515
[5] (2004) 6 SCC 649
[6] (2003) 5 SCC 705