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Damages for Breach of Contract: A Critical Analysis of Laws and Judicial Trend in the Present Regime

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The present legal regime's laws and judicial trends regarding damages for breach of contract are critically analysed in this article. This study aims to investigate the dynamic characteristics of contractual damages, taking into account their theoretical underpinnings and practical implementation in modern legal frameworks. This study assesses the criteria utilised by courts in granting compensatory awards by examining pertinent legal precedents and legislative enactments. The principles of foreseeability, causation, and mitigation are scrutinised in this analysis. The article delves into the different categories of damages that are at one's disposal, including compensatory, consequential, and nominal damages. Additionally, it examines the nascent notion of non-pecuniary damages. The present analysis illuminates the difficulties encountered by courts in precisely quantifying damages and evaluating their sufficiency in fulfilling the goals of contractual remedies. The article provides valuable insights into the present state of damages for breach of contract by identifying significant judicial trends. Additionally, it brings to light potential areas that could benefit from reform.

Keywords: *damages, breach of contract, legal regime, judicial trends, contractual remedies.*

INTRODUCTION

The breach of a contract occurs when the stipulations of the agreement are disregarded or when the obligation undertaken is not fulfilled. The occurrence of a breach of contract is a necessary prerequisite for pursuing a claim for damages, regardless of whether the damages are liquidated, unliquidated, or of another nature. Hence, irrespective of the quantum of profit accruing to the defendant from the contractual arrangement, the absence of a breach of contract precludes any claim for damages. In order to establish a violation, it is imperative that it be adjudicated and proven, rather than merely agreed upon by the parties involved.

THE LAW OF DAMAGES UNDER INDIAN CONTRACT ACT, 1872

Provisions pertaining to the violation of contractual obligations are encompassed in Sections 73 and 74 of the aforementioned Act. Section 73 of the Act deals with damages arising upon breach of a contractual obligation, resulting in losses to the aggrieved party. This section pertains to the awarding of unliquidated damages to the injured party, which are determined based on an assessment of the losses and injuries incurred. It is important to note that such damages do not cover indirect or remote losses resulting from the breach in question. Section 74 pertains to liquidated damages in instances where the contract specifies the amount of damages to be paid in the event of a breach of contract.

LIQUIDATED DAMAGES

According to the Black's Law Dictionary, “a liquidated damages clause is a contractual provision that pre-determines the extent of damages in the event of a breach of the agreement by one of the parties. In cases where a contract is legitimately terminated without any breach of its terms, the issue of seeking damages should not arise as there is no inherent violation. The absence of a legal injury to a party precludes the possibility of any compensation being awarded.”

In the case of *Kailash Nath Associates v Delhi Development Authority and Another*¹, the Supreme Court noted that in contracts that include provisions for liquidated damages, the full amount can only be recovered if the damages suffered by the affected party are commensurate with the predetermined amount of damages. The court made an additional observation that the

¹ *Kailash Nath Associates v Delhi Development Authority and Anr* (2015) 4 SCC 136

monetary compensation granted by the court must not surpass the sum specified in the agreement as liquidated damages.²

In cases where the court encounters challenges in determining the appropriate amount of liquidated damages to be awarded, the injured party is required to demonstrate the extent of damages incurred due to the breach of contract. Upon establishment of such a loss, the court awards appropriate recompense. In the case of *Haryana Telecom Ltd. v Union of India (2006)*, it was observed that the contractor's delay in supplying cables resulted in the Government procuring the same from alternative sources at a lower cost. As a result, the arbitrator's decision to award damages for the breach was overturned on the grounds that no actual loss was incurred.

Despite the existence of a predetermined sum of reward as liquidated damages, the court will consider various factors, including the mitigation of losses, the reasonableness of the sum, and other relevant facts and circumstances. The objective is to ensure that the injured party is adequately compensated, without experiencing any undue profit resulting from the breach of the contract.⁵ The fundamental aim of compensatory damages arising from a breach of contractual obligation is to restore the injured party to the same position they would have been in had the contractual obligation been fulfilled, rather than providing them with a windfall gain.

PROOF OF DAMAGE FOR A CLAIM OF LIQUIDATED DAMAGES

Initially, it is imperative to note that the pursuit of damages is contingent upon the occurrence of a breach of contract, irrespective of the magnitude of the resultant harm. In the absence of any contractual violation between the involved parties, the claim for damages cannot be substantiated. Moreover, in order to pursue compensation, the claimant must demonstrate that they have incurred a detriment.

In the case of *Fateh Chand v Balkishan Dass*, the Supreme Court mandated that ‘the involved parties provide evidence to establish the extent of the loss or damage incurred due to the breach of contract.’³

² *ONGC v Saw Pipes (2003)* 5 SCC 705

³ *Fateh Chand v Balkishan Dass* AIR 1963 SCC 1405

In the case of *Maula Bux v Union of India*⁴, the esteemed Supreme Court of India established that it possesses the authority to grant equitable compensation in the event of a breach of contract, even in the absence of demonstrated actual damages resulting from the breach. Nonetheless, the court determined that certain contracts may present challenges in quantifying damages resulting from a breach. If the parties' designated sum is deemed a legitimate pre-estimate, it may serve as a basis for determining fair compensation. However, if the designated sum is considered a penalty, it cannot be used as a measure of reasonable compensation. In cases where financial loss is at issue, the claimant is required to provide evidence of the loss incurred in order to seek compensation.

The legal case of *Oil & Natural Gas Corporation v Saw Pipes Ltd.* resulted in a ruling by the Supreme Court. The ruling stated that 'if a claimant fails to provide evidence or an honest estimate of damages, the court is obligated to award damages that are lower than the predetermined liquidated damages. This award should be based on a reasonable evaluation of the potential outcomes resulting from the breach of contract.'⁵

The Supreme Court, in the case of *Board of Trustees of Port v Pioneer Engineer And Anr. (2006)*, held that 'there was no deviation by the court in the ONGC judgement from the precedents established in the Fateh Chand and Maula Bux cases. The conclusions reached by the Supreme Court in this particular case cannot be deemed to be inconsistent with the pronouncements made by the Supreme Court in the cases of Fateh Chand and Maula Bux.'

BREACH OF CONTRACT DOESN'T RESULT IN DAMAGES

In the case of *Raheja Universal Pvt. Ltd. v B.E. Bilimoria & Co. Ltd. (2016)*, the Bombay High Court affirmed the decision of a Single Judge who had invalidated an arbitral award due to the absence of evidence supporting the award for liquidated damages. The court found that no proof of loss or damages had been presented.

The Division Bench referred to the legal precedent established in Kailash Nath's case, wherein the Supreme Court established two key principles. Firstly, the sum specified as liquidated damages must be a fair and justifiable compensation that accurately reflects the estimated

⁴ *Maula Bux v Union of India* (1969) 2 SCC 554

⁵ *Oil & Natural Gas Corporation v Saw Pipes Ltd* (2003) 5 SCC 705

damages agreed upon by both parties and subsequently approved by the court. Secondly, any damages awarded must not surpass the specified amount or the penalty mandated by the agreement. The Division Bench made reference to the case of Kailash Nath, wherein the Supreme Court provided an interpretation of the phrase ‘whether or not actual damage or loss is proved to have been caused thereby’ as used in Section 74 of the Contract Act. The court held that the pre-determined liquidated amount would only be considered in situations where it is impossible to prove or calculate the actual damage resulting from a breach of contract. In the event that damages are capable of being estimated, it is imperative that they are explicitly articulated in the pleadings and accurately quantified.

The court held ‘in case of liquidated damages that even if it does not prove the actual loss/damage suffered by it, is entitled to reasonable damages unless it is proved that no loss or damage was caused on account of breach of the contract.’⁶

DIFFERENTIATING BETWEEN LIQUIDATED DAMAGES AND PENALTIES

Broadly speaking, liquidated damages refer to predetermined estimates of losses and corresponding compensation that must be paid in the event of a contract breach. Conversely, penalties are typically disproportionate to the losses incurred and exceed the actual damages resulting from the breach. They are intended to ensure compliance with contractual obligations. The interpretation of the provision outlined in the contractual conditions is frequently subject to a dispute regarding its classification as either a penalty or liquidated damages. The differentiation between liquidated damages and penalty is imperative due to the fact that the inclusion of a penalty provision does not prevent the plaintiff from pursuing unliquidated damages. However, if a provision for liquidated damages is included, no additional remedy in the form of unliquidated damages can be sought.

TRAVELLING BEYOND PRE-DETERMINED AMOUNTS IN THE EVENT OF ANY BREACH

In the case of *Steel Authority of India Limited v Gupta Brother Steel Tubes Limited*, the Supreme Court acknowledged the presence of uncertainty in liquidated damages when the contract fails to explicitly address all breaches of the agreement. The court made an observation

⁶ *M/s. Herbicides (India) Ltd. v M/s. Shashank Pesticides P. Ltd* (2011)

that -There is currently no known principle that mandates the inclusion of all types of breaches under a liquidated damages clause in a contract, even if the parties did not explicitly intend or provide for compensation for all types of breaches.⁷

REMOTENESS OF DAMAGE

Section 73 of the aforementioned Act encompasses a duo of regulations established in the legal case of *Hadley & Anor v Baxendale & Ors*⁸, which transpired in the year 1854. The non-breaching party is entitled to obtain compensation that is proportionate to the losses that naturally emerge from the breach of contract, following the usual course of events. Moreover, it may be fairly inferred that the compensation was anticipated by both parties when they entered into the contract as the probable consequence of a violation.

As per Section 73 of the aforementioned Act, ‘the damages are unliquidated. Consequently, the court exercises its judicial discretion in determining the quantum of damages to be awarded. The aforementioned section stipulates that the damages granted must be reasonably foreseeable and must not be remotely or indirectly caused by the breach. However, it does not provide guidelines for the computation of said damages.’

The Kerala High Court observed in *State of Kerala v K. Bhaskaran* that – “The defendant is liable only for natural and proximate consequences of a breach or those consequences which were in the parties' contemplation at the time of contract... the party guilty of breach of contract is liable only for reasonably foreseeable losses - those that a normally prudent person, standing in his place possessing his information when contracting, would have had reason to foresee as probable consequences of a future breach.”

CALCULATION OF DAMAGES

The case of *M.N. Gangappa v Atmakur Nagabhushanam Shetty & Co. and Anr.*⁹ Highlights the Supreme Court's observation that “*in the absence of a rigid protocol for the computation of damages resulting from a breach of contract, the assessment of damages would be based on the specific facts and circumstances of each case.*”

⁷ *Steel Authority of India Limited v Gupta Brother Steel Tubes Limited* (2009) 10 SCC 63

⁸ *Hadley & Anor v Baxendale & Ors* [1854] EWHC J70

⁹ *M.N. Gangappa v Atmakur Nagabhushanam Shetty & Co. and Anr* AIR 1972 SC 696

In the case of *A.T. Brij Paul Singh v State of Gujarat*¹⁰, the Supreme Court noted that ‘works contracts are typically entered into with the intention of generating profits, and as such, any party that breaches the contract would be responsible for compensating the other party for their anticipated loss of profit. During the process of adjudicating the case, the court referred Hudson's Building and Engineering Contracts, which posits that in major contracts subject to competitive tender on a national basis, the evidence given in litigation on many occasions suggests that the head office overheads and profits are between 3 to 7 per cent of the total price of cost.’ This was the first instance in which the court had relied on this particular source. Additionally, the court noted that a comprehensive assessment, rather than an in-depth analysis of the project, would suffice in resolving claims of profit loss.

In the case of *National Thermal Power Corporation Limited v Wig Brothers Builders and Engineers Limited*¹¹, the Delhi High Court referred to a decision made by the Supreme Court and concluded that arguments based solely on the inability to use a particular formula are not valid.

The Supreme Court, in the case of *Steel Authority of India Ltd. v J.C. Budharaja, Government and Mining Contractor*, noted that the Arbitration Act does not confer any authority upon the arbitrator to act in an arbitrary or capricious manner. The arbitrator's role is contingent upon the agreement and their function is to operate within the confines of the aforementioned agreement.

DAMAGES IN THE MIDST OF A FORCE MAJEURE EVENT

In the case of *M/s Halliburton Offshore Services Inc v Vedanta Limited*, ‘the Delhi High Court ruled that the mere invocation of Covid-19 as a force majeure event could not serve as a justification or excuse for any breach or non-performance.’ The Court emphasised that it was imperative to assess whether the party in question was making all reasonable efforts to fulfil its contractual obligations and whether the pandemic had rendered it incapable of performing.¹²

‘The Court of Appeal in the English case of *Classic Maritime Inc v Limbungan Makmur* determined that a mere demonstration of being prevented from performing due to a force

¹⁰ *A.T. Brij Paul Singh v State of Gujarat* (1984) 4 SCC 59

¹¹ *National Thermal Power Corporation Limited v Wig Brothers Builders and Engineers Limited* ILR (2009) IV Delhi 663

¹² *M/s Halliburton Offshore Services Inc v Vedanta Limited* (2020)

majeure event was insufficient for the parties involved. It was also necessary to establish a direct causal link between the force majeure event and the non-performance.¹³

CONCLUSION

The aforementioned analysis pertaining to damages for breach of contract underscores the complex legal terrain and dynamic judicial patterns in the contemporary framework. This research highlights the significance of strong legal structures in promoting equity and effectiveness in contractual associations. The primary focal points of scrutiny encompass the evaluation of compensatory damages, the significance of foreseeability, the extent of mitigation endeavours undertaken by the aggrieved party, and the likelihood of punitive damages in extraordinary circumstances. Furthermore, the process of conducting a critical analysis highlights the necessity of establishing clear and consistent legal criteria. This can ultimately enhance the reliability and durability of contractual arrangements.

¹³ *Classic Maritime Inc v Limbungan Makmur Sdn Bhd* [2019] EWCA Civ 1102