

CA Foundation
Paper 2 - Business Law

Chapter 2 - ICA
The Indian Contract Act, 1872

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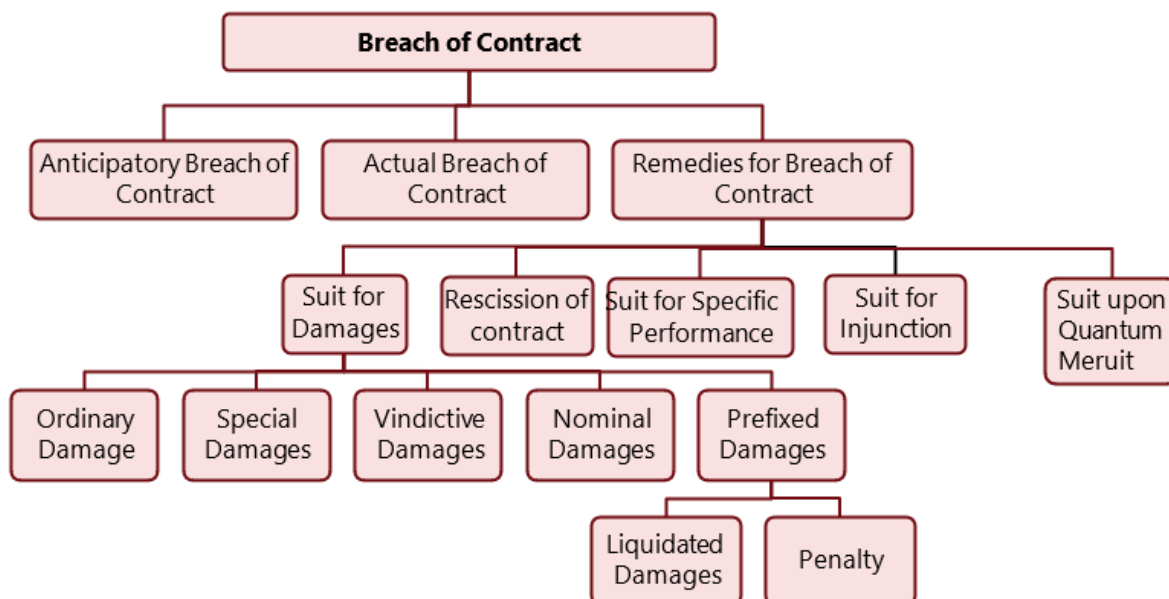
The Indian Contract Act, 1872

Unit 5 - Breach of Contract & Its Remedies

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Unit 5 - Breach of Contract & Its Remedies



Already done -

- How a contract is made,
- the essential of a valid contract and
- also how a contract is to be performed as well as
- how a contract may be put to an end.

- We shall now discuss the breach of contract and
- the mode in which compensation for breach of contract is estimated.

Breach means -

- Failure of
- A party
- to perform his or her obligation
- under a contract.

Breach of contract may arise in two ways:

1. Actual breach of contract

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2. Anticipatory breach of contract

ANTICIPATORY BREACH OF CONTRACT

Section 39 -

- An anticipatory breach of contract is a breach of contract occurring
- **before the time fixed for performance has arrived.**
- When the promisor refuses **altogether** to perform his promise and
- signifies his unwillingness
- even **before the time for performance has arrived**, it is called
- **Anticipatory Breach.**

Anticipatory breach of a contract may take either of the following two ways:

1. **Expressly by words spoken or written, and**
2. **Impliedly by the conduct of one of the parties.**

Example 1: Where A contracts with B on 15th July, 2022 to supply 10 bales of cotton for a specified sum on 14th August, 2022 and on 30th July informs B, that he will not be able to supply the said cotton on 14th August, 2022, there is an express rejection of the contract.

Example 2: Where A agrees to sell his white horse to B for ` 50,000/- on 10th of August, 2022, but he sells this horse to C on 1st of August, 2022, the anticipatory breach has occurred by the conduct of the promisor.

Explanation -

- When a party to a contract has refused to perform or
- disable himself from performing,
- his promise in its **entirety**,
- the **promisee** may put an end to the contract,
- **unless** he has **signified**, but **words** or **conduct**, his acquiescence in its continuance."

Effect of anticipatory breach:

The promisee is excused from performance or from further performance.
Further he gets an option:

1. To either **treat the contract as rescinded** -
 - a. **Sue** the other party for **damages** from breach of contract **immediately**
 - b. **without** waiting until the due date of performance;

OR
2. He may elect not to rescind but to treat the contract **as still operative**,
 - a. **Wait** for the time of **performance** and
 - b. then **hold** the **other party responsible** for the consequences of non-performance.
 - c. But in this case, he will **keep the contract alive** for the **benefit** of the other party as well as his own,
 - d. and the guilty party, if he so decides on re-consideration,
 - e. may still perform his part of the contract and can also take advantage of any supervening impossibility
 - f. which may have the effect of discharging the contract.

ACTUAL BREACH OF CONTRACT

- In contrast to anticipatory breach,
- it is a case of refusal to perform the promise **on the scheduled date**.

- The parties to a lawful contract are bound to perform their respective promises.
- But when one of the parties breaks the contract by refusing to perform his promise,
- he is said to have committed a breach
- In that case, the other party to the contract obtains a **right of action** against the one who has refused to perform his promise.

- Actual breach of contract may be committed-

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1. **At the time** when the performance of the contract is due.

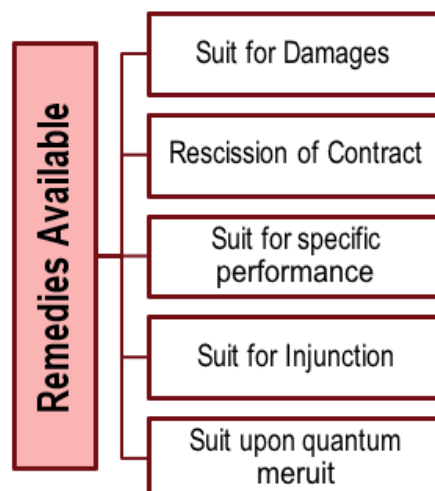
Example 3: A agrees to deliver 100 bags of sugar to B on 1st February 2022. On the said day, he failed to supply 100 bags of sugar to B. This is actual breach of contract. The breach has been committed by A at the time when the performance becomes due.

2. **During** the performance of the contract:

Actual breach of contract also occurs when during the performance of the contract, **one party fails or refuses to perform his obligation** under it by express or implied act.

Aspect	Anticipatory Breach	Actual Breach
Definition	Breach before performance date	Breach on the due date or during performance
Types	Express and Implied	At Due Date and During Performance
Effect on Promisee	Can sue immediately or wait and hold liable	Can take action for breach on the due date
Example	Informing inability to perform in advance	Failing to deliver goods on the agreed date

REMEDIES FOR BREACH OF CONTRACT

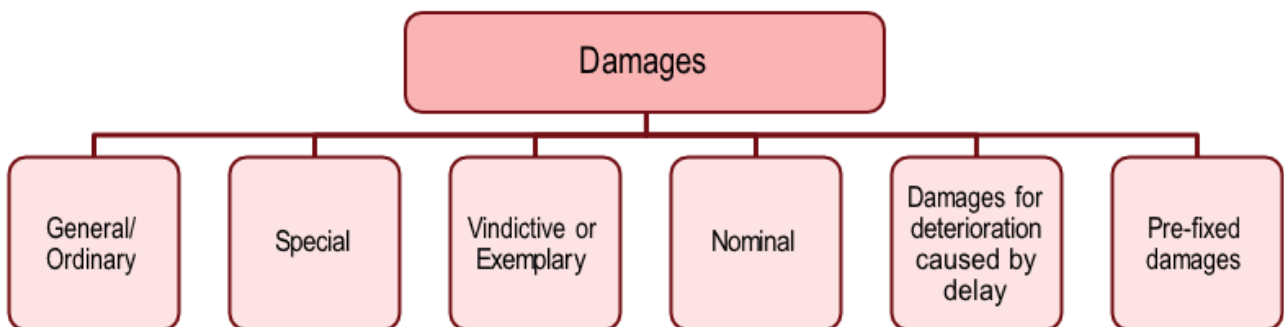


SUIT FOR DAMAGES

Section 73,

- How the amount of compensation is to be determined.
- On the breach of the contract, the party who sues from such a breach is
- **entitled to receive**, from the party who has broken the contract,
- **compensation for any loss or damage caused to him by breach**

- Compensation can be claimed for -
 - Any **loss or damage which naturally arises** in the usual course of events.
 - A compensation can also be claimed for any loss or damage **which the party knew** when they entered into the contract, as likely to result from the breach.
 - That is to say, special damage can be claimed **only on a previous notice**. But the party suffering from the breach is bound to take reasonable steps to minimise the loss.
 - **No compensation is payable** for any remote or indirect loss.



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TYPES OF DAMAGES		
Type of Damages	Definition	Example
Ordinary Damages	Compensation for loss naturally arising from the breach or known to the parties at the time of contract.	B can claim Rs. 500 from A for the difference in rice price due to A's refusal to deliver.
Special Damages	Compensation for losses arising from special circumstances known to the breaching party at the time of contract.	A can claim lost profits from B due to the delay of a machine, but not for the lost Government contract.
Vindictive or Exemplary Damages	Awarded for breach of promise to marry or wrongful dishonor of a cheque, often for emotional distress or reputational harm.	A businessman can claim exemplary damages for loss of credit due to wrongful cheque dishonor.
Nominal Damages	Awarded when there is a breach but no actual damage suffered; establishes the right to a decree.	Awarded a small sum like Rs. 1 or 10 paise when no real damage is proven.
Damages for Deterioration	Compensation for deterioration of goods due to delay; includes physical damage and loss of sale opportunity.	Carrier liable for damages if goods deteriorate due to delay, even without notice.
Pre-fixed Damages	Damages stipulated in the contract, either as liquidated damages (reasonable estimate) or a penalty (arbitrary amount).	If the penalty is Rs. 1,00,000 but actual loss is Rs. 70,000, only Rs. 70,000 is recoverable.

1. Ordinary damages:

- When a contract has been broken,
- the party who suffered by such breach is **entitled to receive**,
- from the party who has broken the contract,
- **compensation for any loss or damage** cause to him thereby,
- which naturally arose in the usual course of things from such breach, or
- which the parties know, 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 reasons of the breach.

(Section 73 of the Contract Act and the rule in Hadley vs. Baxendale).

Example 4: A agrees to sell to B bags of rice at Rs. 5,000 per bag, delivery to be given after two months. On the date of delivery, the price of rice goes up to Rs. 5,500 per bag. A refuse to deliver the bags

to B. B can claim from A Rs. 500 as ordinary damages arising directly from the breach.

2. Special damages:

- Where a party to a contract receives a notice of special circumstances affecting the contract,
- he will be liable not only for damages arising naturally and directly from the breach but also for **special damages**.

Example 5: 'A' delivered a machine to 'B', a common carrier, to be conveyed to 'A's mill without delay. 'A' also informed 'B' that his mill was stopped for want of the machine. 'B' unreasonably delayed the delivery of the machine, and in consequence 'A' lost a profitable contract with the Government. In this case, 'A' is entitled to receive from 'B', by way of compensation, the average amount of profit, which would have been made by running the mill during the period of delay. But he cannot recover the loss sustained due to the loss of the Government contract, as 'A's contract with the Government was not brought to the notice of 'B'.

3. Vindictive or Exemplary damages

These damages may be awarded only in two cases -

- a. for breach of promise to marry because it causes **injury to his or her feelings**; and
- b. for **wrongful dishonour** by a banker of his customer's cheque because in this case the injury due to wrongful dishonour to the drawer of cheque is so heavy that it causes loss of credit and reputation to him.

A business man whose credit has suffered will get exemplary damages even if he has sustained no pecuniary loss. But a non-trader cannot get heavy damages in the like circumstances, unless the damages are alleged and proved as special damages. (Gibbons v West Minister Bank)

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4. Nominal damages:

- Nominal damages are awarded where the plaintiff has proved
- that there has been a **breach of contract** but
- he has not in fact suffered any real damage.
- It is awarded just to establish the **right to decree** for the breach of contract.
- The amount may be a rupee or even 10 paise.

5. Damages for deterioration caused by delay:

- In the case of deterioration caused to **goods by delay**,
- damages can be recovered from the carrier even **without notice**.
- The word 'deterioration' not only implies physical damages to the goods
- but it may also mean loss of special opportunity for sale.

6. Pre-fixed damages:

BASIS	Liquidated Damages	Penalty
Definition	A pre-estimated amount agreed upon by the parties to cover potential losses from a breach.	An excessive amount set to coerce performance, not a fair estimate of loss.
Effectiveness	Valid and recoverable if it represents a genuine estimate of loss.	Not enforceable; the injured party can only recover actual loss.
Purpose	To compensate for the breach based on a reasonable forecast of potential damages.	To penalize the breaching party, which is deemed unreasonable.

Example 6: If the penalty provided by the contract is Rs. 1,00,000 and the actual loss because of breach is Rs. 70,000, only Rs. 70,000 shall be available as damages, i.e., the amount of actual loss and not the amount stipulated. But if the loss is, say, Rs. 1,50,000, then only, Rs. 1,00,000 shall be recoverable.

Example 7: X promised Y, a priest, to pay Rs. 10,000 as charity. The priest on X's promise incurred certain liabilities towards the repairing of the temple to the extent of Rs. 7,500. Y, the priest, can

recover from X Rs. 7,500.

PENALTY AND LIQUIDATED DAMAGES (SECTION 74)

The parties to a contract may provide beforehand the amount of compensation payable in case of failure to perform the contract. In such cases, the question arises whether the courts will accept this figure as the measure of damage.

English Law:

According to English law, The sum so fixed in the contract may be interpreted either as liquidated damages or as a penalty.

- If the sum fixed in the contract represents a genuine pre-estimate by the parties of the loss,
- which would be caused by a future breach of the contract,
- it is liquidated damages.
- It is an assessment of the amount which in the opinion of the parties will compensate for the breach.
- Such a clause is effective and the amount is recoverable.

- But where the sum fixed in the contract is unreasonable and is used to force the other party to perform the contract; it is a penalty.
- Such a clause is disregarded and the injured party cannot recover more than the actual loss.

Indian Law:

Indian law makes no distinction between 'penalty' and liquidated damages

- The Courts in India award only a reasonable compensation
- not exceeding the sum so mentioned in the contract.
- Section 74 of the Contract Act lays down if the parties have fixed what the damages will be, the courts will never allow more.
- But the court may allow less.

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- A decree is to be passed only for reasonable compensation **not exceeding the sum** named by the parties
- Thus, Section 74 entitles a person complaining of breach of contract to get **reasonable compensation and does not entitle him to realise anything by way of penalty.**

Exception:

Where any person gives any bond to the Central or State government for the performance of any public duty or act in which the public are interested, on breach of the condition of any such instrument, he shall be **liable to pay the whole sum mentioned therein.**

Example 8: A contracts with B, that if A practices as a surgeon in Kolkata, he will pay B Rs. 50,000. A practice as a surgeon at Kolkata, B is entitled to such compensation not exceeding Rs. 50,000 as the court considers reasonable.

Example 9: A borrows Rs. 10,000 from B and gives him a bond for Rs. 20,000 payable by five yearly instalments of Rs. 4,000 with a stipulation that in default of payment, the whole shall become due. This is a stipulation by way of penalty.

Example 10: A undertakes to repay B, a loan of Rs. 10,000 by five equal monthly instalments with a stipulation that in default of payment of any instalment, the whole shall become due. This stipulation is not by way of penalty and the contract may be enforced according to its terms.

Distinction between liquidated damages and penalty

Breach of Contract & Its Remedies ◀ 2.5

DIFFERENCE B/W LIQUIDATION DAMAGES AND PENALTY		
BASIS	Liquidated Damages	Penalty
Common Feature	Both are payable upon breach of contract.	Both are payable upon breach of contract.
Amount	Reflects a genuine pre-estimate of potential damages.	Excessive amount, far beyond probable damages.
Additional Sums	Not generally applicable.	Additional sums for default may indicate a penalty.
Court's Role	Courts assess if the sum is a reasonable estimate of loss.	Courts will disregard if the sum is extravagant or excessive, even if labeled as liquidated damages.
Essence	A genuine pre-estimate of damage.	A sum to intimidate or coerce the offending party.
Treatment in India	No distinction; courts award actual loss up to the fixed sum.	Courts award reasonable compensation, not exceeding the fixed sum.

REMEDIES OTHER THAN CLAIMING DAMAGES

Besides claiming damages as a remedy for the breach of contract, the following remedies are also available:

"Really Quick Solution Incoming"

- R - Rescission of contract
- Q - Quantum Meruit
- S - Specific Performance
- I - Injunction

a. Rescission of contract:

- When a contract is broken by one party,
- the other party may treat the contract as rescinded.
- In such a case he is absolved of all his obligations under the contract and
- is entitled to compensation for any damages that he might have suffered.

Example 11: A promises B to deliver 50 bags of cement on a certain

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day. B agrees to pay the amount on receipt of the goods. A failed to deliver the cement on the appointed day. B is discharged from his liability to pay the price.

b. Quantum Meruit:

- Where one person has rendered service to another
- in circumstances which indicate an understanding between them
- that it is to be paid for although no particular remuneration has been fixed,
- the law will infer a promise to pay.

Quantum Meruit i.e. as much as the party doing the service has deserved.

- It covers a case where the party injured by the breach
- had at time of breach done part
- but not all of the work
- which he is bound to do under the contract and
- seeks to be compensated for the value of the work done.
- For the application of this doctrine, two conditions must be fulfilled:
 1. It is only available if the original contract has been discharged.
 2. The claim must be brought by a party not in default.
- The object of allowing a claim on quantum meruit is to **recompensate the party** or person for value of work which he has done.
- Damages are **compensatory in nature** while quantum merit is **restitutory**.
- It is but reasonable compensation awarded on implication of a contract to remunerate.
- Where a person orders from a wine merchant 12 bottles of a whiskey and 2 of brandy, and the purchaser accepts them, the purchaser must pay a reasonable price for the brandy.

The claim for quantum meruit arises in the following cases:

1. **Void Agreement or Void Contract:** When an agreement is found to be void, or a valid contract becomes void later.
2. **Gratuitous Work:** When someone does something without intending to do it for free, they can claim payment.
3. **No Fixed Remuneration:** If services are provided with no clear agreement on payment, the person providing the service can still claim payment.
4. **Contract Abandonment:** When one party refuses to continue or abandons the contract.
5. **Divisible Contract:** If part of a divisible contract is performed, the party not in breach can enjoy that benefit.
6. **Bad Work in an Indivisible Contract:** If a lump-sum contract is completed poorly, the performing party can claim the payment, but the other party may deduct for poor quality

Example 12: X wrongfully revoked Y's (his agent) authority before Y could complete his duties. Held, Y could recover, as a quantum meruit, for the work he had done and the expenses he had incurred in the course of his duties as an agent.

Example 13: A agrees to deliver 100 bales of cottons to B at a price of Rs. 1000 per bale. The cotton bales were to be delivered in two instalments of 50 each. A delivered the first instalment but failed to supply the second. B must pay for 50 bags.

c. **Suit for specific performance:**

- Where damages are **not an adequate remedy**
- in the case of breach of contract,
- the court may in its discretion on a suit for a specific performance direct party in breach,
- to carry out his promise **according to the terms of the contract.**

d. **Suit for injunction:**

- Where a party to a contract is negating the terms of a contract,

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- the court may by issuing an 'injunction orders',
- restrain him from doing what he promised not to do.

Example 14: N, a film star, agreed to act exclusively for a particular producer, for one year. During the year she contracted to act for some other producer. Held, she could be restrained by an injunction.

Example 15: A, a singer, agreed with B to perform at his theatre for two months, on a condition that during that period, he would not perform anywhere. In this case, B could move to the Court for grant of injunction restraining A from performing in other places.

Party rightfully rescinding contract, entitled to compensation (Section 75)

- A person who rightfully rescinds a contract is entitled to compensation for any damage which he has sustained through non-fulfilment of the contract

Example 16: A, a singer, contracts with B, the manager of a theatre, to sing at his theatre for two nights in every week during the next two months, and B engages to pay her Rs. 10000 for each night's performance. On the sixth night, A wilfully absents herself from the theatre, and B, in consequence, rescinds the contract. B is entitled to claim compensation for the damage which he has sustained through the non-fulfilment of the contract.

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“ PROBLEM KYA HAI ? - Unit 5 ”

Question Bank

ICA

*This section is complied with questions and suggested answers
for the chapter - ICA*

- ❖ *ICAI Study material*
- ❖ *Previous year Question Papers (PYQPs)*
- ❖ *Mock Test Papers (MTPs)*
- ❖ *Revision Test Papers (RTPs)*

Compiled by - CA Chaitanya Jain

Question 1

"Liquidated damage is a genuine pre-estimate of compensation of damages for certain anticipated breach of contract whereas Penalty on the other hand is an extravagant amount stipulated and is clearly unconscionable and has no comparison to the loss suffered by the parties". Explain.

(Module)

Answer 1

Liquidated damage is a genuine pre-estimate of compensation of damages for certain anticipated breach of contract. This estimate is agreed to between parties to avoid at a later date detailed calculation and the necessity to convince outside parties.

Penalty on the other hand is an extravagant amount stipulated and is clearly unconscionable and has no comparison to the loss suffered by the parties.

In terms of Section 74 of the Act "where 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 damages or loss is proved to have been caused thereby, to receive from the other party who has broken the contract, a reasonable compensation not exceeding the amount so named, or as the case may be the penalty stipulated for.

Explanation to Section 74

A stipulation for increased interest from the date of default may be a stipulation by way of penalty.

In terms of Section 74, courts are empowered to reduce the sum payable on breach whether it is 'penalty' or "liquidated damages" provided the sum appears to be unreasonably high.

Sri Chunnilal vs. Mehta & Sons Ltd (Supreme Court)

Supreme Court laid down the ratio that the aggrieved party should not be allowed to claim a sum greater than what is specific in the written agreement.

But even then, the court has powers to reduce the amount if it considers it reasonable to reduce.

Question Bank → Chap 2 (Unit 5) - ICA, 1872

Question 2

'X' entered into a contract with 'Y' to supply him 1,000 water bottles @ Rs. 5.00 per water bottle, to be delivered at a specified time. Thereafter, 'X' contracts with 'Z' for the purchase of 1,000 water bottles @ Rs. 4.50 per water bottle, and at the same time told 'Z' that he did so for the purpose of performing his contract entered into with 'Y'. 'Z' failed to perform his contract in due course and market price of each water bottle on that day was & 5.25 per water bottle. Consequently, 'X' could not procure any water bottle and "Y' rescinded the contract. Calculate the amount of damages which 'X' could claim from "Z' in the circumstances? What would be your answer if 'Z' had not informed about the 'Y's contract? Explain with reference to the provisions of the Indian Contract Act, 1872.

Answer 2

Breach of Contract-Damages: Section 73 of the Indian Contract Act, 1872 lays down that 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.

The leading case on this point is "Hadley vs. Baxendale" in which it was decided by the Court that the special circumstances under which the contract was actually made were communicated by the plaintiff to the defendant, and thus known to both the parties to the contract, the damages resulting from the breach of such contract which they would reasonably contemplate, would be the amount of injury which would ordinarily follow from the breach of contract under these special circumstances so known and communicated.

The problem asked in this question is based on the provisions of Section 73 of the Indian Contract Act, 1872.

In the instant case 'X' had intimated to 'Z' that he was purchasing water bottles from him for the purpose of performing his contract with Y'. Thus, 'Z' had the knowledge of the special circumstances.

Therefore, "X' is entitled to claim from 'Z' Rs. 500/- at the rate of 0.50 paise i.e. 1000 water bottles x 0.50 paise (difference between the procuring price of water bottles and contracted selling price to Y) being the amount of profit 'X' would have made by the performance of his contract with Y'.

If 'X' had not informed 'Z' of 'Y's contract, then the amount of damages would have been the difference between the contract price and the market price on the day of default. In other words, the amount of damages would be Rs. 750/- (i.e. 1000 water bottles × 0.75 paise).

(MTPs, RTPs and PYQPs)

Question 1

Seema was running a boutique in New Delhi. She has to deliver some cloth to her friend Kiran who was putting up an exhibition at Mumbai. Seema delivered the sewing machine and some cloth to a railway company to be delivered at a place where the exhibition was to be held. Seema expected to earn an exceptional profit from the sales made at this exhibition however she did not bring this fact to the notice of the railway's authorities. The goods were delivered at the place after the conclusion of the exhibition. On account of such breach of contract by railways authorities, can Seema recover the loss of profits under the Indian Contract Act, 1872?

(RTP May' 22)

Answer 1

As per Section 73 to 75 of Indian Contract Act, 1872, Damage means a sum of money claimed or awarded in compensation for a loss or an injury. Whenever a party commits a breach, the aggrieved party can claim the compensation for the loss so suffered by him. General damages are those which arise naturally in the usual course of things from the breach itself. (Hadley Vs Baxendale). Therefore, when breach is committed by a party, the defendant shall be held liable for all such losses that naturally arise in the usual course of business. Such damages are called ordinary damages. However, special damages are those which arise in unusual circumstances affecting the aggrieved party and such damages are recoverable only when the special circumstances were brought to the knowledge of the defendant. If no special notice is given, then the aggrieved party can only claim the ordinary damages.

In the given case, Seema was to earn an exceptional profit out of the sales made at the exhibition, however she never informed about it to the railway authorities.

Question Bank —> **Chap 2 (Unit 5) - ICA, 1872**

Since the goods were delivered after the conclusion of the exhibition, therefore Seema can recover only the losses arising in the ordinary course of business. Since no notice about special circumstances was given to railways authorities, she could not recover the loss of profits.

Question 2

"An anticipatory breach of contract is a breach of contract occurring before the time fixed for performance has arrived". Discuss stating also the effect of anticipatory breach on contracts.

(RTP May' 22) (SM) (MTP 7 Marks, Oct'21)

Answer 2

An anticipatory breach of contract is a breach of contract occurring before the time fixed for performance has arrived. When the promisor refuses altogether to perform his promise and signifies his unwillingness even before the time for performance has arrived, it is called Anticipatory Breach. The law in this regard has very well summed up in *Frost v. Knight* and *Hochster v. DelaTour*.

Section 39 of the Indian Contract Act, 1872 deals with anticipatory breach of contract and provides as follows: "When a party to a contract has refused to perform or disable himself from performing, his promise in its entirety, the promisee may put an end to the contract, unless he has signified, but words or conduct, his acquiescence in its continuance."

Effect of anticipatory breach: The promisee is excused from performance or from further performance.

Further he gets an option:

1. To either treat the contract as "rescinded and sue the other party for damages from breach of contract immediately without waiting until the due date of performance; or
2. He may elect not to rescind but to treat the contract as still operative and wait for the time of performance and then hold the other party responsible for the consequences of non-performance. But in this case, he will keep the contract alive for the benefit of the other party as well as his own, and the guilty party, if he so decides on re - consideration, may still perform his part of the contract and can also take advantage of any supervening impossibility which may have the effect of discharging the contract.

Question 3

In the light of the provisions of the Indian Contract Act, 1872, answer the following:
Give the circumstances as to when "Vindictive or Exemplary Damages" may be awarded for breach of a contract.

(RTP Nov 22)

Answer 3

Vindictive or Exemplary damages

These damages may be awarded only in two cases?

1. for breach of promise to marry because it causes injury to his or her feelings; and
2. for wrongful dishonour by a banker of his customer's cheque because in this case the injury due to wrongful dishonour to the drawer of cheque is so heavy that it causes loss of credit and reputation to him.

A business man whose credit has suffered will get exemplary damages even if he has sustained no pecuniary loss. But a non-trader cannot get heavy damages in the like circumstances, unless the damages are alleged and proved as special damages. (Gibbons v West Minister Bank)

Question 4

Shital was a classical dancer. She entered into an agreement with Sharad Vidya Mandir for 50 dance performances. As per the contract, she was supposed to perform every weekend and she will be paid \$ 8,000/- per performance. However, after a month, she was absent without informing, due to her personal reasons. Answer the following questions as per the Indian Contract Act, 1872.

1. Whether the management of Sharad Vidya Mandir has right to terminate the contract?
2. If the management of Sharad Vidya Mandir informed Shital about its continuance, can the management still rescind the contract after a month on this ground subsequently?
3. Can the Sharad Vidya Mandir claim damages that it has suffered because of this breach in any of the above cases?

(RTP Nov 23)

Question Bank → Chap 2 (Unit 5) - ICA, 1872

Answer 4

Section 39 of the Indian Contract Act, 1872 provides that when a party to a contract has refused to perform or disabled himself from performing his promise in its entirety, the promisee may put an end to the contract unless he has signified, by words or conduct his acquiescence in its continuance. Further, in terms of Section 40, the promisee shall be required to perform personally, if there is such an apparent intention of the parties.

Also, as per Section 75 of the Act, a person who rightfully rescinds a contract is entitled to compensation for any damage which he has sustained through non-fulfilment of the contract.

Therefore, in the instant case,

1. Since, Shital could not perform as per the terms of contract, Sharad Vidya Mandir can terminate the contract.
2. In the second situation, the management of Sharad Vidya Mandir informed Shital about the continuance of the contract. Hence, the management cannot rescind the contract after a month on this ground subsequently.
3. As per Section 75, Sharad Vidya Mandir can claim damages that it has suffered because of this breach in part (i).

Question 5

Rahul was a Disk Jockey at a five-star hotel. As per the contract, he is supposed to perform every weekend. (i.e. twice a week).

Rahul will be paid Rs. 2,500 per day. However, after a month, Rahul willfully absents himself from the performance. Taking into account the provisions of the Indian Contract Act, 1872, answer the following:

1. Does the hotel have the right to end the contract?
2. If the hotel sends out a mail to Rahul that they are interested to continue the contract and Rahul accepts, can the hotel rescind the contract after a month on this ground subsequently?
3. In which of the case - (termination of contract or continuance of contract) can the hotel claim damages

that it had suffered as a result of this breach?

Answer 5

By analysing Section 39 of the Indian Contract Act, 1872, it is understood that when a party to a contract has refused to perform or disabled himself from performing his promise entirely, the following two rights accrue to the aggrieved party (promisee):

- a. To terminate the contract
- b. To indicate by words or by conduct that he is interested in its continuance.

In either of the two cases, the promisee would be able to claim damages that he suffers.

In the given case,

1. Yes, the hotel has the right to end the contract with Rahul, the DJ.
2. The hotel has the right to continue the contract with Rahul. But once this right is exercised, it cannot subsequently rescind the contract on this ground subsequently.
3. In both the cases, the hotel (promisee) is entitled to claim damages that has been suffered as a result of breach.

Question 6

Mr. Murti was travelling to Manali with his wife by bus of Himalya Travels Pvt. Ltd. Due to some technical default in the bus, the driver has to stop the bus in a mid way in cold night. Driver advised the passenger to get the shelter in nearest hotel which was at a distance of only one kilometre from that place. The wife of Mr. Murti caught cold and fell ill due to being asked to get down and she had to walk in cold night to reach hotel. Mr. Murti filed the suit against Himalya Travels Pvt. Ltd. for damages for the personal inconvenience, hotel charges and medical treatment for his wife. Explain, whether Mr. Murti would get compensation for which he filed the suit?

(MTP Mar'22 4 Marks)

Answer 6

Question Bank —> **Chap 2 (Unit 5) - ICA, 1872**

Section 73 of Indian Contract Act, 1872 provides that 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. But such compensation is not to be given for any remote and indirect loss or damage sustained by reason of the breach.

In the instant case, Mr. Murti filed the suit against Himalya Travels Pvt. Ltd. for damages for the personal inconvenience, hotel charges and medical treatment for his wife.

On the basis of above provisions and facts of the case, it can be said that Mr. Murti can claim damages for the personal inconvenience and hotel charges but not for medical treatment for his wife because it is a remote or indirect loss.

Question 7

Seema was running a boutique in New Delhi. She was to deliver some cloth to her friend Kiran who was putting up an exhibition at Mumbai. Seema delivered the sewing machine and some cloth to a railway company to be delivered at a place where the exhibition was to be held. Seema expected to earn an exceptional profit from the sales made at this exhibition however she did not bring this fact to the notice of the railway's authorities. The goods were delivered at the place after the conclusion of the exhibition. On account of such breach of contract by railways authorities, can Seema recover the loss of profits?

(MTP Nov'22 6 Marks)

Answer 7

Section 73-75 of Indian Contract Act, 1872: Damage means a sum of money claimed or awarded in compensation for a loss or an injury. Whenever a party commits a breach, the aggrieved party can claim the compensation for the loss so suffered by him. General damages are those which arise naturally in the usual course of things from the breach itself. (Hadley Vs Baxendale). Therefore, when breach is committed by a party, the defendant shall be held liable for all such losses that naturally arise in the usual course of business. Such damages are called ordinary damages. However special damages are those which arise in unusual circumstances affecting the aggrieved party and such damages are

Question Bank —> **Chap 2 (Unit 5) - ICA, 1872**

recoverable only when the special circumstances were brought to the knowledge of the defendant. If no special notice is given, then the aggrieved party can only claim the ordinary damages.

In the instant case, the goods were delivered after the conclusion of the exhibition, therefore Seema can recover only the losses arising in the ordinary course of business. Special damages are allowed only when the special circumstances are made aware. Since no notice about special circumstances was given to railway authorities, she could not recover the loss of profits.

Question 8

"An anticipatory breach of contract is a breach of contract occurring before the time fixed for performance has arrived". Also, discuss the effect of anticipatory breach of contracts under the Indian Contract Act, 1872.

(MTP Apr 23 7 Marks)

Answer 8

An anticipatory breach of contract is a breach of contract occurring before the time fixed for performance has arrived. When the promisor refuses altogether to perform his promise and signifies his unwillingness even before the time for performance has arrived, it is called Anticipatory Breach.

Effect of Anticipatory Breach: The promisee is excused from performance or from further performance.

Further he gets an option:

1. To either treat the contract as rescinded and sue the other party for damages for breach of contract immediately without waiting until the due date of performance; or
2. He may elect not to rescind but to treat the contract as still operative, and wait for the time of performance and then hold the other party responsible for the consequences of non-performance. But in this case, he will keep the contract alive for the benefit of the other party as well as his own, and the guilty party, if he so decides on re-consideration, may still perform his part of the contract and can also take advantage of any supervening impossibility which may have the effect of discharging the contract.

Question 9

Mr. Harish was travelling to Shimla with his wife by bus of Himalya Travels Pvt. Ltd. Due to some technical default in the bus, the driver has to stop the bus in a mid-way in cold night. The driver advised the passengers to get to the shelter in the nearest hotel which was at a distance of only one kilometer from that place. The wife of Mr. Harish caught cold and fell ill due to being asked to get down and she had to walk in cold night to reach hotel. Mr. Harish filed the suit against Himalya Travels Pvt. Ltd. for damages for the personal inconvenience, hotel charges and medical treatment for his wife. Explain, whether Mr. Harish would get compensation for which he filed the suit under the Indian Contract Act, 1872?

(MTP May' 23 4 Marks)

Answer 9

Section 73 of Indian Contract Act, 1872 provides that 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. But such compensation is not to be given for any remote and indirect loss or damage sustained by reason of the breach.

In the instant case, Mr. Harish filed the suit against Himalya Travels Pvt. Ltd. for damages for the personal inconvenience, hotel charges and medical treatment for his wife.

On the basis of above provisions and facts of the case, it can be said that Mr. Harish can claim damages for the personal inconvenience and hotel charges but not for medical treatment for his wife because it is a remote or indirect loss.

Question 10

"Liquidated damage is a genuine pre-estimate of compensation of damages for certain anticipated breach of contract whereas Penalty on the other hand is an extravagant amount stipulated and is clearly unconscionable and has no

Question Bank → Chap 2 (Unit 5) - ICA, 1872

comparison to the loss suffered by the parties". Explain the statement by differentiating between liquidated damages and penalty with reference to provisions of the Indian Contract Act, 1872.

(MTP Dec'23 5 Marks)

Answer 10

Liquidated damages is a genuine pre-estimate of compensation of damage for certain anticipated breach of contract. This estimate is agreed to between parties to avoid at a later date detailed calculation and the necessity to convince outside parties.

Penalty on the other hand is an extravagant amount stipulated and is clearly unconscionable and has no comparison to the loss suffered by the parties.

Distinction between liquidated damages and penalty

Penalty and liquidated damages have one thing in common that both are payable on the occurrence of a breach of contract. It is very difficult to draw a clear line of distinction between the two but certain principles as laid down below may be helpful.

1. If the sum payable is so large as to be far in excess of the probable damage on breach, it is certainly a penalty.
2. Where a sum is expressed to be payable on a certain date and a further sum in the event of default being made, the latter sum is a penalty because mere delay in payment is unlikely to cause damage.
3. The expression used by the parties is not final. The court must find out whether the sum fixed in the contract is in truth a penalty or liquidated damages. If the sum fixed is extravagant or exorbitant, the court will regard it as a penalty even if, it is termed as liquidated damages in the contract.
4. The essence of a penalty is payment of money stipulated as a *terrorem* of the offending party. The essence of liquidated damages is a genuine pre-estimate of the damage.
5. English law makes a distinction between liquidated damages and penalty, but no such distinction is followed in India. The courts in India must ascertain the actual loss and award the same which amount must not, however exceed the sum so fixed in the contract. The courts have not to bother about the distinction but to award reasonable compensation not exceeding the sum so fixed.

Question 11

Sheena was a classical dancer. She entered into an agreement with Shital Vidya Mandir for 60 dance performances. As per the contract, she was supposed to perform every weekend and she will be paid \$ 10,000/- per performance. However, after a month, she was absent without informing, due to her personal reasons. Answer the following questions as per the Indian Contract Act, 1872.

1. Whether the management of Shital Vidya Mandir has right to terminate the contract?
2. If the management of Shital Vidya Mandir informed Sheena about its continuance, can the management still rescind the contract after a month on this ground subsequently?
3. Can the Shital Vidya Mandir claim damages that it has suffered because of this breach in any of the above cases?

(PYP May 22 4 Marks)

Answer 11

Section 39 provides that when a party to a contract has refused to perform or disabled himself from performing his promise in its entirety the promisee may put an end to the contract unless he had signified, by words or conduct his acquiescence in its continuance. Further, in term of Section 40, the promisee shall be required to perform personally, if there is such an apparent intention of the parties.

Also, as per Section 75 of the Act, a person who rightfully rescinds a contract is entitled to compensation for any damage which he has sustained through non-fulfilment of the contract.

Therefore, in the instant case,

1. Since, Sheena could not perform as per the terms of contract, Shital Vidya Mandir can terminate the contract.
2. In the second situation, the management of Shital Vidya Mandir informed Sheena about the continuance of the contract. Hence, the management cannot now rescind the contract after a month on this ground subsequently.
3. As per Section 75, Shital Vidya Mandir can claim damages that it has suffered because of this breach in part (i).

Question 12

"Liquidated damage is a genuine pre-estimate of compensation of damages for certain anticipated breach of contract whereas Penalty on the other hand is an extravagant amount stipulated and is clearly unconscionable and has no comparison to the loss suffered by the parties". Explain the statement by differentiating between liquidated damages and penalty with reference to provisions of the Indian Contract Act, 1872.

(PYP May'22 5 Marks)

Answer 12

Liquidated damages is a genuine pre-estimate of compensation of damage for certain anticipated breach of contract. This estimate is agreed to between parties to avoid at a later date detailed calculation and the necessity to convince outside parties.

Penalty on the other hand is an extravagant amount stipulated and is clearly unconscionable and has no comparison to the loss suffered by the parties.

Distinction between liquidated damages and penalty

Penalty and liquidated damages have one thing in common that both are payable on the occurrence of a breach of contract. It is very difficult to draw a clear line of distinction between the two but certain principles as laid down below may be helpful.

1. If the sum payable is so large as to be far in excess of the probable damage on breach, it is certainly a penalty.
2. Where a sum is expressed to be payable on a certain date and a further sum in the event of default being made, the latter sum is a penalty because mere delay in payment is unlikely to cause damage.
3. The expression used by the parties is not final. The court must find out whether the sum fixed in the contract is in truth a penalty or liquidated damages. If the sum fixed is extravagant or exorbitant, the court will regard it as a penalty even if, it is termed as liquidated damages in the contract.
4. The essence of a penalty is payment of money stipulated as a *terrorem* of the offending party. The essence of liquidated damages is a genuine pre-estimate of the damage.

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5. English law makes a distinction between liquidated damages and penalty, but no such distinction is followed in India. The courts in India must ascertain the actual loss and award the same which amount must not, however exceed the sum so fixed in the contract. The courts have not to bother about the distinction but to award reasonable compensation not exceeding the sum so fixed.

Question 13

On 1st March 2023, T Readymade Dress Garments, Shimla enters into a contract with J Readymade Garments, Jaipur for the supply of different sizes of shirts 'S' (Small), 'M' (Medium), and 'L' (Large). As per the terms of the contract, 300 pieces of each category i.e. 'S' @ Rs. 900; 'M' Rs. 1,000 and 'L' Rs. 1,100 per piece have to be supplied on or before 31st May, 2023.

However, on 1st May, 2023, T Readymade Dress Garments, Shimla informed J Readymade Garments, Jaipur that the firm is not willing to supply the shirts at the above rate due to the rise of prices in the raw material cost. In the meantime, prices for similar shirts have gone up in the market to the tune of Rs. 1,000; Rs. 1,100; and Rs. 1,200 for 'S', 'M' and 'L' sizes respectively.

Examine the rights of J Readymade Garments, Jaipur in this regard as per the provisions of the Indian Contract Act, of 1872.

(PYP Dec 23 3 Marks)

Answer 13

As per the provisions of Section 39 of the Indian Contract Act, 1872, when a party to a contract has refused to perform, or disabled himself from performing, his promise in its entirety, the promisee may put an end to the contract, unless he has signified, by words or conduct, his acquiescence in its continuance.

J Readymade Garments in the given situation has two options, out of which he has to select any one:

1. Either to treat the contract as rescinded and sue T Readymade Dress Garments for damages from breach of contract immediately without waiting until the due date of performance or
2. He may elect not to rescind but to treat the contract as still operative and wait for the time of performance and then hold the other party responsible for the consequences of non-performance.

Question Bank —> **Chap 2 (Unit 5) - ICA, 1872**

Important Note: The answer can also be given as per Section 73 of the Indian Contract Act, 1872 which lays down that 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.

In the instant case, J Readymade Garments,

Jaipur would be entitled to get the damages i.e. difference between the contract price and the market price on the day of default from T Readymade Dress

Garments, Shimla. In other words, the amount of damages would be Rs. 90,000 [300 piece @ Rs. 100 (Small), 300 piece @ Rs. 100 (Medium) and 300 piece Rs. 100 (Large)].

Question 14

"Liquidated damage is a genuine pre-estimate of compensation of damages for certain anticipated breach of contract whereas Penalty on the other hand is an extravagant amount stipulated and is clearly unconscionable and has no comparison to the loss suffered by the parties". Explain.

(RTP May' 21)

Answer 14

Liquidated damage is a genuine pre-estimate of compensation of damages for certain anticipated breach of contract. This estimate is agreed to between parties to avoid at a later date detailed calculation and the necessity to convince outside parties.

Penalty on the other hand is an extravagant amount stipulated and is clearly unconscionable and has no comparison to the loss suffered by the parties.

In terms of Section 74 of the Act "where 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 damages or loss is proved to have been caused thereby, to receive from the other party who has broken the contract, a reasonable compensation not exceeding the amount so named, or as the case may be the penalty stipulated for

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Explanation to Section 74

A stipulation for increased interest from the date of default may be a stipulation by way of penalty. In terms of Section 74, courts are empowered to reduce the sum payable on breach whether it is 'penalty' or "liquidated damages" provided the sum appears to be unreasonably high.

Sri Chunnilal vs. Mehta & Sons Ltd (Supreme Court)

Supreme Court laid down the ratio that the aggrieved party should not be allowed to claim a sum greater than what is specific in the written agreement. But even then, the court has powers to reduce the amount if it considers it reasonable to reduce.

Question 15

A & B entered into a contract to supply unique item, alternate of which is not available in the market. A refused to supply the agreed unique item to B. What directions could be given by the court for breach of such contract?

(RTP May'21)

Answer 15

Where there is a breach of contract for supply of a unique item, mere monetary damages may not be an adequate remedy for the other party. In such a case the court may give order for specific performance and direct the party in breach to carry out his promise according to the terms of contract. Here, in this case, the court may direct A to supply the item to B because the refusal to supply the agreed unique item cannot be compensated through money.

Question 16

Mr. X was a Disk Jockey at a five star hotel bar. As per the contract, he is supposed to perform every weekend (i.e. twice a week). Mr. X will be paid & 1500 per day. However, after a month, Mr. X willfully absents himself from the performance. Does the hotel have the right to end the contract? If the hotel sends out a mail to X that they are interested to continue the contract and X accepts, can the hotel rescind the contract after a month on this ground subsequently? In which of the cases - (termination of contract or continuance of

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contract) can the hotel claim damages that it has suffered as a result of this breach?

(RTP Nov' 21)

Answer 16

By analyzing Section 39 of the Indian Contract Act 1872, it is understood that when a party to a contract has refused to perform or disabled himself from performing his promise entirely, the following two rights accrue to the aggrieved party (promisee)

- a. To terminate the contract
- b. To indicate by words or by conduct that he is interested in its continuance.

In either of the two cases, the promisee would be able to claim damages that he suffers. In the given case,

1. Yes, the hotel has the right to end the contract with Mr. X, the DJ.
2. The hotel has the right to continue the contract with X. But once this right is exercised, they cannot subsequently rescind the contract on this ground subsequently.
3. In both the cases, the hotel (promisee) is entitled to claim damages that has been suffered as a result of breach.

Question 17

"When a party to a contract has refused to perform, or disabled himself from performing his promise in its entirety, the promisee may put an end to the contract". Explain.

(MTP 5 Marks, Mar'21)

Answer 17

Effect of a Refusal of Party to Perform Promise

According to Section 39, when a party to a contract has refused to perform, or disabled himself from performing his promise in its entirety, the promisee may put an end to the contract, unless he has signified, by words or conduct, his acquiescence in its continuance.

From language of Section 39 it is clear that in the case under consideration, the following two rights accrue to the aggrieved party, namely, (a) to terminate the

Question Bank —> Chap 2 (Unit 5) - ICA, 1872

contract; (b) to indicate by words or by conduct that he is interested in its continuance.

In case the promisee decides to continue the contract, he would not be entitled to put an end to the contract on this ground subsequently. In either case, the promisee would be able to claim damages that he suffers as a result on the breach.

Question 18

"An anticipatory breach of contract is a breach of contract occurring before the time fixed for performance has arrived". Explain and also discuss the effect of anticipatory breach on contracts.

(MTP 7 Marks, Apr'21)

Answer 18

Section 39 of the Indian Contract Act deals with anticipatory breach of contract and provides as follows:

"When a party to a contract has refused to perform or disable himself from performing, his promise in its entirety, the promisee may put an end to the contract, unless he has signified, but words or conduct, his acquiescence in its continuance."

Effect of anticipatory breach: The promisee is excused from performance or from further performance.

Further he gets an option:

1. To either treat the contract as "rescinded and sue the other party for damages from breach of contract immediately without waiting until the due date of performance; or
2. He may elect not to rescind but to treat the contract as still operative, and wait for the time of performance and then hold the other party responsible for the consequences of non performance. But in this case, he will keep the contract alive for the benefit of the other party as well as his own, and the guilty party, if he so decides on reconsideration, may still perform his part of the contract and can also take advantage of any supervening impossibility which may have the effect of discharging the contract.

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