Commercial law must be certain and predictable. **

It is my privilege to join this Seminar organised by the National School of India University, Bengaluru in association with the Ministry of Law and Justice, Department of Justice, Government of India about the theme "Strengthening Legal Provisions for the Enforcement of Contracts". The discussions over two days will throw light on the problems afflicting enforcement of commercial contracts, and give solutions.

If the main concern of these discussions is promoting the ease of doing business, we must give primary importance to certainty and predictability of law relating to contract enforcement. I touch upon this theme in my short speech.

Businessmen wish for, and would like to operate, in a legal system that is certain and predictable. They can contract and perform with confidence if the legal system will give effect to their transaction, and will offer a strong and quick resolution, or enforcement, to deal with problems and disputes arising from their transactions.

They can plan, and can anticipate liability. This is even more important in transactions across borders.

I propose to explain this subject from the point of view of a person making a contract.

I want to write a clause in my contract for liquidated damages that the contractor Y, the other party, must pay @ Rs 5000 per day for delay in completing a work.

I must assume that the legislation is quite clear, simple.

Under section 74 of the Indian Contract Act, I am entitled to receive the amount specified "whether or not actual damage or loss is proved to have been caused thereby." If I have such a clause, and Y delays, I must only prove (i) breach, (ii) injury. I need not prove actual damage or loss. I will get the agreed amount unless it is not reasonable, something that Y will have to show. This is good. I will have such a clause. Such simple analysis allows me to make this provision with great confidence.

In *Chunilal Mehta vs. Century Spinning and Weaving Mills*[1] decided in 1962, Mudholkar J for the constitutional bench of six judges, upheld the order of the High Court awarding an amount calculated on the basis of the specified amount of Rs 6000, even though actual loss was not proved.

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[1] AIR 1962 SC 1314

In *Fateh Chand v. Balkishan Das*,[2] decided in 1963, the Supreme Court again held that the section dispenses with proof of actual loss or damage, but legal injury must be proved.

I am assured that the amount stipulated will be ordered.

In *Maula Bux v Union of India*,[3] the Supreme Court divided contracts (stipulating LD) into two classes. The one where it may be impossible for a court to assess compensation arising from breach, and the other where compensation can be so calculated. In the first case, the court can award the stipulated sum as 'reasonable compensation' if it is regarded as a genuine pre-estimate, but not if it is a penalty. In the latter case, the party aggrieved must prove the loss.

If I am drafting an LD clause, I must first think whether my case falls in the first or the second category, bearing in mind that this categorisation will eventually be decided by a court. Even if it falls in the first category (where compensation is impossible to calculate) I must make a genuine pre-estimate of compensation, bearing in mind again that a court will decide many years after the contract whether my calculation has been a genuine pre-estimate. If my case falls in the second category, I will need to prove the loss.

Perhaps I might get around by stating in the clause itself (i) that compensation cannot be calculated (even if my contract is a purchase of goods easily available in the market), and (ii) that the amount is a genuine pre-estimate.

I can see a shift of burden. Earlier I could claim the amount, and Y had to show that the amount was not reasonable. Now, I must show the nature of my contract, and that the amount was a genuine pre-estimate when the contract was made. I must preserve and show and convince the judge of the calculations I made when I made the contract.

I am less confident now of having LD provision, and must start looking for an alternative to protect my interests.

In *Oil and Natural Gas Corporation Ltd v SAW Pipes*,[4] the Supreme Court stated that the terms of the contract would decide whether the party claiming LD is entitled to it. In cases where it is impossible to assess compensation, and it is not in nature of penalty or unreasonable, it can be awarded if it is a genuine pre-estimate by parties as measure of

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[2] AIR 1963 SC 1405

[3] AIR 1970 SC 1955

[4] AIR 2003 SC 2629

reasonable compensation. This observation begs the question: if it is impossible to assess compensation, how can parties make a genuine pre-estimate of compensation?

I am happy. I need not prove loss, and yet the court will grant me reasonable compensation. I must expressly state in my provision two contradictory statements: that it is difficult to calculate compensation, and that the amount is a genuine pre-estimate. I must also expressly state that the amount is not a penalty.

Kailash Nath Associates v DDA,[5] of 2015 created some confusion. The Supreme Court observed that where it is possible to prove actual damage or loss, such proof is not dispensed with. But where damage or loss is difficult or impossible to prove that the liquidated amount named in the contract, if a genuine pre-estimate of damage or loss, can be awarded. This observation is obiter because it held that in the case there was no breach of contract.

I face the same dilemma now. How can I pre-estimate the loss if it is difficult or impossible to prove.

In *Construction and Design Services v Delhi Development Authority*[6] decided in 2015, the Supreme Court awarded half of the stipulated amount even when the aggrieved party had not given any specific evidence of loss, holding that a court can find the loss suffered and its extent even if there is no specific evidence of loss. If the entire amount is genuine pre-estimate of loss, actual loss need not be proved. Burden of proving lies on the breaking party that no such loss suffered or that it is a penalty.

Now, my provision cannot be a simple statement of Rs 5000 per day. I must say many more things as statements of facts. – that loss cannot be calculated or is difficult to calculate. That Rs 5000 per day is genuine pre-estimate (with supporting facts and calculations as a backup of this provision). That this amount is not a penalty. That this amount is reasonable.

Yet I am not sure I will get this amount. Nor can I directly deduct it from any security deposit that Y will keep with me.

This development seeks to protect interests of Y, the contract breaker. Concerns about my interests as the party aggrieved by breach are of no consequence.

I find a better solution. This is strict. It will work unfairly on Y. But my concern is my risk. I will ask Y to give me a bank guarantee such that even if he commits one day's delay, I can

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[5] AIR 2015 SC (Supp) 780

[6] AIR 2015 SC 1282

call the bank to pay. Neither Y can stop its payment, nor will any court restrain it. Section 74 will not apply.

Thankfully I am quite certain about this position, at least for today.

There Is a need for certainty in judge-made law

A judgment in commercial dispute resolves it for the parties, yet any significant change in the established law has wider ramifications. It affects other agreements, relationships, underlying financial transactions, insurance etc.

But there are occasions when courts will attempt to be creative and give new interpretations to principles that are developed and settled over a period of time.

In his lecture titled "Certainty v Creativity…"[7], Sir Geoffrey Vos, Chancellor of the High Court of England and Wales suggests that while deciding new situations, judges without a commercial background might place greater emphasis on the justice of the outcome in particular case without being concerned that the outcome becomes less predictable when it turns on judicial discretion.

Parties make provisions in their contract on the expectation that the settled position will continue. The essential question is whether when a position of law is settled, a court should create a new rule or a deviation merely to meet the demands of the case in hand. If courts will want to deviate in the interest of justice in a particular case, every case can yield a different outcome. Any such decision deviating from settled position affects parties in many ways: Firstly, it is stated in respect of the impugned contract that was made on the basis of settled position, and hence the judgment unsettles the parties', or at least one party's, expectations whose contract is under litigation. Secondly, other parties who have contracted on the basis of the settled position can no longer rely on the provisions of their own contract. Thirdly, parties who wish to make contracts face uncertainty whether the settled position will apply to the particular facts of their case, or the deviation; or even worse, whether any court will make another deviation from the settled position.

What results from lack of certainty and predictability?

If law is uncertain, or its application based on discretion of courts, parties will not turn to courts for resolving their disputes. They will prefer arbitration. This means that new principles will not develop.

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[7] Certainty v Creativity: Some pointers towards the development of the common law", Sir Geoffrey Vos

When the outcome of litigation is not predictable, more appeals will be filed in the hope that the highest courts will depart from the clear current position of law. Litigation will increase, so will costs.

This also means that the party who has the strength and stamina to file appeals will do so hoping to have a view partial to his position.

How can certainty be achieved?

Settled legal rules should not be easily changed. Essential core issues in any particular case today are not any more complex than they used to be. If facts are distilled, the core can be reached. Any development must be on incremental basis.

Avoid obiter-dicta because the principles stated in such manner are not tested against real situations.

Judges must consider the effect of their judgment on future cases.

Thank you
