**IN THE HIGH COURT OF DELHI AT NEW DELHI**

% Judgment delivered on: 19.05.2022

\+ **O.M.P. (COMM) 121/2020**

**MR. RAJESH GUPTA** ..... Petitioner

versus

**SH. RAM AVTAR** .... Respondent

**Advocates who appeared in this case:**

For the Petitioner : Mr Sidhant Nath, Advocate.
For the Respondent : Mr Sushil Kumar Pandey and Mr Rahul Mourya, Advocates.

**CORAM**
**HON'BLE MR JUSTICE VIBHU BAKHRU**

**JUDGMENT**

**VIBHU BAKHRU, J**

1. The petitioner has filed the present petition under Section 34 of the Arbitration and Conciliation Act, 1996 (hereinafter the **'A&C Act'**) impugning an arbitral award (hereinafter the **'impugned award'**) dated 19.04.2012 delivered by the Arbitral Tribunal consisting of Justice (Retd.) J.P. Singh as the Sole Arbitrator (hereinafter the '**Arbitral Tribunal'**).

2. The impugned award was rendered in the context of disputes that have arisen between the parties in connection with the agreement dated

05.12.2008 captioned "Agreement to Sell and Purchase Cum Receipt' dated 05.12.2008 (hereinafter '**the Agreement'**).

3. In terms of the Agreement, the petitioner agreed to purchase the manufacturing unit including the built up factory, rights in the leasehold property No. C-37, Sector B-2, Tronica City, Loni Ghaziabad (UP) and all movable assets (hereafter '**the Property**') for a sale consideration of ₹1,60,00,000/-.

4. The petitioner paid a sum of ₹60,00,000/- to the respondent. The receipt of the said amount was expressly acknowledged in the Agreement as receipt of 'earnest money'.

5. After the parties had entered into the Agreement, the petitioner claimed that the respondent had committed fraud by representing that the entire constructed/covered area of the factory premises was 10,000 sq.ft. whereas, upon taking measurements, the actual constructed area was found to be only 6,500 sq.ft.

6. The petitioner claims that on discovering that the covered/constructed area of the factory premises was less by 3,500 sq.ft, the petitioner called upon the respondent to either reduce the consideration price; or to refund the earnest money/part sale consideration.

7. On 02.05.2009, the petitioner sent a legal notice calling upon the respondent to either refund the amount paid (₹60,00,000/- ), or in the alternative, execute the sale deed in respect of the factory premises

based on actual measurements. However, the respondent did not respond to the said legal notice.

8. Thereafter, the petitioner filed a suit before this Court captioned C.S. (OS) No. 1971/2009 for recovery of the earnest money along with damages.

9. The respondent filed an application under Section 8 of the A&C Act, which was allowed and by an order dated 19.01.2010, the parties were referred to arbitration under the aegis of the Delhi International Arbitration Centre (DIAC).

***Arbitral proceedings***

10. Before the Arbitral Tribunal, the petitioner filed his Statement of Claims and claimed an amount of ₹1,20,00,000/- being twice the earnest money as liquidated damages due to the failure on the part of the respondent in fulfilling his obligations under the Agreement. Additionally, besides costs, the petitioner also claimed *pendente lite* interest as well as future interest at the rate of 18% per annum and 5% per annum respectively to be compounded quarterly.

11. The petitioner claims that he was willing to consummate the transaction *albeit* on a proportionately reduce consideration. It thus, appears that the respondent was also willing to reduce the consideration marginally but the parties could not arrive at mutually acceptable solution. The Arbitral Tribunal had also encouraged the parties to resolve the disputes amicably, however, the same did not fructify.

12. The petitioner claims that he was entitled to refund of the money of ₹60,00,000/- which was paid as an advance in terms of the Agreement along with penalty of an equivalent amount as the respondent was not in a position to conclude the transaction. The petitioner further claims that respondent had induced the petitioner to enter into a transaction on a fraudulent representation that the constructed / covered area of the premises was approximately 10,000 sq.ft.

13. The respondent filed his Statement of Defence, however, did not raise any counter-claims.

14. Considering the rival contentions of the parties, the Arbitral Tribunal framed the following issues for determination:

> "1. Whether the measurement of the property in question was 10,000 sqft or 6,500 sqft? OPP
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> 2. Whether there was a fraudulent representation by the respondent to the claimant before execution of the agreement to sell and purchase cum receipt dated 5th December 2008. If so, its effect? OPC
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> 3. Whether the claim was barred under exception as per clause 19 of the Indian Contract Act 1872? OPR
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> 4. Whether the claimant is entitled to recover the claimed amount? OPC
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> 5. Whether the earnest money paid by the claimant is liable to be forfeited as per clause 12 of the above said agreement?
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> 6. Whether the claimant is entitled to double the amount of

the earnest money in terms of the clause 12 of the above said Agreement.
7. Relief, costs including interest etc.

15. In regards to issue no.1, the Arbitral Tribunal accepted the report of the architect and found that the constructed area was neither 10,000 sq.ft nor 6,500 sq.ft but was actually, 7,506 sq.ft.

16. Notwithstanding the decision that the total covered area / constructed area of the factory premises was substantially less than 10,000 sq. ft., the Arbitral Tribunal decided the second issue in favour of the respondent. The Arbitral Tribunal held that the Agreement was not regarding the purchase of constructed area but of the complete running unit including the plot of land measuring 450 sq.mtr. along with the building constructed thereon as well as plant and machinery and other movable and immovable assets. The Arbitral Tribunal held that the petitioner was not bound to accept the representation that the constructed area / covered area of the factory premises was 10,000 sq.ft. and was required to in his own interest inspect the property and take the necessary measurements. The Arbitral Tribunal held that the maxim *"caveat emptor"* squarely applied to the facts of the case.

17. The Arbitral Tribunal referred to the decision of the Supreme Court in ***Commissioner of Customs (Preventive) v. M/s Aafloat Textiles (I) Pvt. Ltd. and Ors.: (2009) 11 SCC 18*** and on the strength of the said decision held that it was the duty of the petitioner as a purchaser to make the necessary enquiries and ascertain all facts relating to the property prior to committing to purchase the same. The

petitioner was also required to discharge the onus of establishing that he had made all necessary enquiries and had taken the necessary precautions and if had failed to do so, necessary consequences have to follow. The Arbitral Tribunal did not accept that the petitioner had entered into the Agreement without inspecting the property and observed that the petitioner ought to have examined the sanctioned site plan. In view of the above, the Arbitral Tribunal rejected the petitioner's allegation regarding the fraudulent representation as being without any basis.

18. The Arbitral Tribunal also rejected the petitioner's contention that the sum of ₹60,00,000/- paid by the petitioner was part payment of the consideration and not earnest money. Consequently, the respondent was entitled to forfeit the same in terms of the Agreement.

***Reasons & Conclusion***

19. Mr. Nath, learned counsel appearing for the petitioner has assailed the impugned award on two fronts. First, he submits that the conclusion of the Arbitral Tribunal that there was no misrepresentation by the respondent is manifestly erroneous. He contended that since the Arbitral Tribunal had concluded that the covered / constructed area was 7,506 sq.ft., the petitioner's claim that respondent had misrepresented the covered area / constructed area of the factory premises to be approximately 10,000 sq.ft. was established.

20. Second, he submitted that the decision of the Arbitral Tribunal to deny the petitioner's claim for refund of ₹60,00,000/- is manifestly

erroneous. The respondent had not produced any evidence or material to establish the loss suffered by it. Thus, there was no question of permitting the respondent to forfeit the amount of ₹60,00,000/- paid by the petitioner as part consideration. He also contended that even though the Agreement referred to the payment of ₹60,00,000/- as earnest money, it was, *ex facie*, clear that the same was part consideration for purchasing the property in question. The said amount constituted substantial portion of the total agreed sale consideration and could not be treated as a nominal amount.

21. He referred to the decision of a Coordinate Bench of this Court in ***Vandana Jain v. Rita Mathur & Ors.*** [RFA No.38/2018 decided on 20.04.2018] in support of his contention that forfeiture of a substantial amount was impermissible without any evidence of loss.

22. Before proceeding further, it is relevant to refer to the terms of the Agreement, which are reproduced below:

> "**AGREEMENT TO SELL & PURCHASE CUM RECEIPT**
>
> This Agreement is made and executed at New Delhi on 05th December, 2008 by and between Mr. Ram Avtar S/o Shri Om Prakash Verma R/o C-5/9, Model Town, New Delhi (hereinafter called the **FIRST PARTY / SELLER).**
>
> **AND**
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> Sh. Rajesh Kumar Gupta S/O Shri Hari Ram Gupta permanent R/o 286/73, Niwaz Khera, Aish Bagh, Moti Nagar, Lucknow U.P. for the time being residing at F-244-245, New Rajinder Nagar, New Delhi 110 060

(Hereinafter called the **SECOND PARTY *I* PURCHASER**)

The expressions of both the parties shall mean including their respective legal heirs, successors, executors, representatives and legal assigns.

WHEREAS the first party is the owner in possession of Lease hold entire property measuring 450 sq. meters on which he has constructed from his own resources factory premises admeasuring approx 10,000 sq. feet of covered space spread into Ground, First and Second floor after obtaining sanction from competent authorities at property bearing No.C-37, Sector B-2,Tronica City, Industrial Loni, Described in the scheme annexed hereto (hereinafter called as "the factory premises") from where he is carrying on the business as a sole proprietor of manufacturing of C.T.C. Juices, Ketchin Juice and Cakes etc. under the name and style of M/s Shyam Food & Bakery after obtaining Industrial license from the Directorate of Industries U.P.

WHEREAS both the parties have entered into agreement to sell & purchase for the sale of Lease hold entire built up Industrial property bearing No.C-37, Sector B-2,Tronica City, Industrial Loni, Ghaziabad, having constructed area 10,000 sq. feet (approx) in Ground Floor, First Floor & Second Floor with roof rights on a total plot area measuring 450 sq meters (Approx) with running manufacturing of CTC Juices, Ketchin Juice and Cakes etc. under the name and style of M/s Shyam Food & Bakery after obtaining Industrial License from the Directorate of Industries UP along with complete plant and machinery and all the movable/non movable assets more particularly described in the schedule annexed hereto,

AND WHEREAS the First party has created an equitable mortgage of the said Factory Premises in favour of Syndicate Bank, Tronica City, Ghaziabad

U.P. branch from which the First Party has borrowed a sum the current outstanding of which is approx. Rs.16,00,000/- (Rupees Sixteen lacs only) by depositing the original sale deed of the said Factory Premises with the said bank. That it shall be the sole responsibility of the First Party to clear its dues with its banker and get the property free from mortgage.

WHEREAS the First Party has indemnify and assure the second party, about its legal ownership and its full right to enter into this Agreement to sell for the above property. The first party has agreed to sell the said property to the second party The second party has also agreed to purchase the same and both the parties agreed on the following terms and conditions of this Agreement to sell & purchase:

**NOW THIS WITNESSETH AS UNDER:**

1. That the total sale consideration have been fixed by both the parties at a sum of Rs,l,60,00,000/- (Rupees one crore sixty lacs only) which will be paid by the second party (Mr.Rajesh Kumar Gupta) to the first party.

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9. Whereas the first party has received a sum of Rs.60,00,000/- (Rs. Sixty Lacs Only) as EARNEST MONEY as per detail given below:-

I. Rs.1,00,000/- only (Rs. One Lacs only) By Cheque No.299903, dated 05th December, 2008, Drawn on Bank – HDFC, Hazrat Ganj, Lucknow, U.P. in favour of "Mr. Ram Avtar".

II. Rs.59,00,000/- only (Rs. Fifty Nine Lacs Only) by CASH.

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**Total** = Rs.60,00,000/- only (Rs. Sixty Lacs Only).

> 10. The Second party will complete the Balance payment Rs.1,00,00,000/- (Rs. One Crore only) within three month from the date of this agreement on or before the 03rd March 2009 at the time of getting the physical possession of the entire property, if any of the require documents or NOC / Permission left pending the final date will automatically be extended.
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> 11. The second party will have the right to transfer the said property to any one it likes and the first party will have no objection at the time of documentation. When the deal is finalized, the first party will peacefully handover the physical possession of the property to the purchaser or his nominee(s).
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> 12. That in case the First party fails to complete the transaction within the stipulated period as specified above then there will be sole discretion of the Second party either to recover double the amount of the Earnest money paid or to finalize the transaction through the Court of law with the suit for "specific performance" of the contract, and on the other hand if the Second party fails to make the full and final payment within the period as specified above, the Earnest money / amount shall be forfeited and the transaction shall be deemed to be cancelled."

23. The first question to be examined is whether the decision of the Arbitral Tribunal to reject the petitioner's claim of fraudulent misrepresentation is manifestly erroneous. As is apparent from the above, the Agreement expressly indicates that the respondent had constructed an area of 10,000 sq.ft. approximately. It was also established during the arbitral proceedings that the constructed / covered area was 7,506 sq.ft. Thus, undisputedly the representation regarding the covered area as reflected in the Agreement was incorrect. However, the Arbitral Tribunal found the petitioner's allegation of

misrepresentation was without any basis. This conclusion is based on the finding that the petitioner had not only the means but was expected to satisfy himself as to the measurements of the factory premises. More importantly, the Arbitral Tribunal held that the petitioner had agreed to purchase and the respondent had agreed to sell the entire factory premises as a running unit, which included the rights in the leasehold land measuring 450 sq.mtr, the entire built up factory along with plant and machinery, and other movable assets. The Agreement also contemplated transfer of licenses for running the said unit. Although, not stated in so many words, it is also discernable from the impugned award that the Arbitral Tribunal was of the view that the reduced area was not material.

24. It was the respondent's case that the petitioner was aware of the factory premises as he had also visited the same. The respondent had further denied that he had made any fraudulent misrepresentation.

25. The Arbitral Tribunal had reasoned that copies of the building plan had been provided to the respondent, however, there is no material on record to indicate that the sanctioned plan reflected the covered / constructed area as was subsequently ascertained by the Architect.

26. Undeniably, the covered / constructed area of the factory was less and the Agreement was based on an erroneous representation. This Court also finds it difficult to accept that the reduced area of the factory to the extent of almost 25% could be considered as not material.

27. The decision in the case of ***Commissioner of Customs***

***(Preventive) v. M/s Aafloat Textiles (I) Pvt. Ltd. and Ors.*** (*supra*) which was referred to by the Arbitral Tribunal is not applicable. In that case, the Supreme Court had set aside the order passed by the Customs, Excise and Service Tax Appellate Tribunal (CESTAT), which in turn impugned an order of Commissioner of Customs confirming the duty demand in respect of nine consignments of gold and silver imported by the respondent (M/s Aafloat Textiles (I) Pvt. Ltd.). The goods were imported under a Special Import License (SIL), which was found to be forged. The forged SIL was purchased by the importers from certain brokers. In that case, the premises of certain concerns were searched by the officers of the Directorate of Revenue Intelligence and copies of the forged SIL was recovered. Inquiries established that the SIL in question was forged. The persons from whose premises the copy of the SIL was recovered, claimed that they had purchased the same from another person. He admitted that SIL was given to him by one Mr. Jain who in turn had obtained several bogus SILs from two other persons.

28. It was the case of the department that the buyer of the SIL could not have better title than the seller. The CESTAT had allowed the appeal on the ground that the department had not established that the importer had any knowledge of the forgery. In the aforesaid context, the Supreme Court held that if the importer had not taken the necessary precautions for finding out the genuineness of the SILs, the consequences would necessarily follow. In the aforesaid context, the Court also referred to the principle of *"caveat emptor"*. The judgment of the Supreme Court did not involve determination of contractual rights and obligations

between the parties to a contract. The decision was in respect of the question whether the importer could absolve himself of the liability in respect of imports under a forged license. Clearly, the said decision did not preclude the importer from proceeding against the persons who had sold the forged SIL. This is not an authority for the proposition that the importer did not have any recourse against the seller of the forged SIL.

29. The principle of '*caveat emptor'* does not apply where an express representation is made by the seller and is relied upon by the purchaser.

30. The Arbitral Tribunal has held that the claim was barred under the exception clause mentioned in Section 19 of the Indian Contract Act,1872 as the petitioner could discover the truth in regards to measurement of the premises with ordinary due diligence. The Arbitral Tribunal, also observed that the petitioner had taken a contradictory stand by stating in the Statement of Claims that the actual measurement of the premises came to his notice when the factory premises was measured, however, in his evidence as CW-1, had affirmed that the actual measurement came into his notice on visual examination.

31. It is clear from the above that the conclusion of the Arbitral Tribunal that the Agreement is not voidable on account of being induced by fraudulent representation is based on evaluation of evidence and material on record. The jurisdiction of this Court to interfere with an Arbitral Award under Section 34 of the A&C Act is limited. It is not permissible for this Court to supplant its opinion in place of that of the Arbitral Tribunal's. Unless the Court finds that the impugned award is

in conflict with the public policy of India or is vitiated by patent illegality, no interference under Section 34(2)(b)(ii) or 34(2A) of the A&C Act is permissible. The conclusion of the Arbitral Tribunal when tested on the aforesaid standards, does not warrant any interference in these proceedings.

32. The second question to be examined is whether the decision of the Arbitral Tribunal that the respondent was entitled to forfeit the amount of ₹60,00,000/- is manifestly, erroneous.

33. The Arbitral Tribunal held that the payment of ₹60,00,000/- was not as part payment of the sale price but was as earnest money. And, in terms of Clause 12 of the Agreement, the respondent was entitled to the entire earnest money due to failure on the part of the petitioner to fulfil his obligations under the Agreement.

34. The Arbitral Tribunal's decision that a sum of ₹60,00,000/- was paid as earnest money is based on the plain reading of Clause 12 of the Agreement. The Arbitral Tribunal also referred observations made by the Bombay High Court in ***Hasmukhlal M. Parikh v. Commissioner of Income Tax: AIR 1960 Bombay 224***. In that case, the Court had held that if a document drawn up by a lawyer, uses the expression "earnest money", the Court would require a much stronger evidence than was found in that case, to justify holding that the expressly "earnest money" was not intended to have the meaning which it normally has.

35. It is material to note that a sum of ₹60,00,000/- is a substantial part of the consideration for purchase of the Property. In ***Shree***

***Hanuman Cotton Mills v. Tata Air Craft Ltd.: (1969) 3 SCC 522***, the Court had held that earnest money "*represents a guarantee that the contract will be fulfilled or, in other words, "earnest" is given to bind the contract*." The question whether an amount of ₹60,00,000/- could be considered as a guarantee for entering into a binding contract was also required to be considered keeping in view the quantum of the said amount.

36. In ***Videocon Properties Ltd. v. Bhalchandra Laboratories: (2004) 3 SCC 711***, the Supreme Court had explained that the description of the words used in the Agreement would not necessarily be determinative of the nature of the amount. The relevant extract of the said decision is set out below:

> "14. … Further, it is not the description by words used in the agreement only that would be determinative of the character of the sum but really the intention of parties and surrounding circumstances as well, that have to be looked into and what may be called an advance may really be a deposit or earnest money and what is termed as 'a deposit or earnest money' may ultimately turn out to be really an advance or part of purchase price. Earnest money or deposit also, thus, serves two purposes of being part- payment of the purchase money and security for the performances of the contract by the party concerned, who paid it."

37. In view of the above, the fact that ₹60,00,000/- was referred to as earnest money in the Agreement would not necessarily be dispositive of the controversy, whether it was in fact earnest money or paid as part of the consideration. Notwithstanding the nomenclature, a sum of

₹60,00,000/- which represented substantial portion of the total consideration (37.5%) could not be forfeited without the respondent's establishing that he had suffered any loss.

38. Undisputedly, the respondent did not lead any evidence or place any material to establish the losses suffered by it.

39. In ***Kailash Nath Associates v. Delhi Development Authority and Another: (2015) 4 SCC 136*** the Supreme Court had further explained that all stipulations claiming amounts to be paid in case of breach would be covered under Section 74 of the Indian Contract Act, 1872. The relevant paragraphs of the said judgment are reproduced below:

> "40. From the above, it is clear that this Court held that **Maula Bux's** case was not, on facts, a case that related to earnest money. Consequently, the observation in Maula Bux that forfeiture of earnest money under a contract if reasonable does not fall within Section 74, and would fall within Section 74 only if earnest money is considered a penalty is not on a matter that directly arose for decision in that case. The law laid down by a Bench of 5 Judges in Fateh Chand's case is that all stipulations naming amounts to be paid in case of breach would be covered by Section 74. This is because Section 74 cuts across the rules of the English Common Law by enacting a uniform principle that would apply to all amounts to be paid in case of breach, whether they are in the nature of penalty or otherwise. It must not be forgotten that as has been stated above, forfeiture of earnest money on the facts in Fateh Chand's case was conceded. In the circumstances, it would therefore be correct to say that as earnest money is an amount to be paid in case of breach of contract and named in the

contract as such, it would necessarily be covered by Section 74.

41. It must, however, be pointed out that in cases where a public auction is held, forfeiture of earnest money may take place even before an agreement is reached, as DDA is to accept the bid only after the earnest money is paid. In the present case, under the terms and conditions of auction, the highest bid (along with which earnest money has to be paid) may well have been rejected. In such cases, Section 74 may not be attracted on its plain language because it applies only —"when a contract has been broken".

42. In the present case, forfeiture of earnest money took place long after an agreement had been reached. It is obvious that the amount sought to be forfeited on the facts of the present case is sought to be forfeited without any loss being shown. In fact it has been shown that far from suffering any loss, DDA has received a much higher amount on re-auction of the same plot of land.

43. On a conspectus of the above authorities, the law on compensation for breach of contract under Section 74 can be stated to be as follows:-

43.1. Where a sum is named in a contract as a liquidated amount payable by way of damages, the party complaining of a breach can receive as reasonable compensation such liquidated amount only if it is a genuine pre-estimate of damages fixed by both parties and found to be such by the Court. In other cases, where a sum is named in a contract as a liquidated amount payable by way of damages, only reasonable compensation can be awarded not exceeding the amount so stated. Similarly, in cases where the amount fixed is in the nature of penalty, only reasonable compensation can be awarded not exceeding the penalty so stated. In both cases, the liquidated amount or penalty is the upper

limit beyond which the Court cannot grant reasonable compensation.

43.2. Reasonable compensation will be fixed on well known principles that are applicable to the law of contract, which are to be found inter alia in Section 73 of the Contract Act

43.3. Since Section 74 awards reasonable compensation for damage or loss caused by a breach of contract, damage or loss caused is a sine qua non for the applicability of the Section.

43.4. The Section applies whether a person is a plaintiff or a defendant in a suit.

43.5. The sum spoken of may already be paid or be payable in future.

43.6. The expression —"whether or not actual damage or loss is proved to have been caused thereby" means that where it is possible to prove actual damage or loss, such proof is not dispensed with. It is only in cases 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.

43.7. Section 74 will apply to cases of forfeiture of earnest money under a contract. Where, however, forfeiture takes place under the terms and conditions of a public auction before agreement is reached, Section 74 would have no application.

44. The Division Bench has gone wrong in principle. As has been pointed out above, there has been no breach of contract by the appellant. Further, we cannot accept the view of the Division Bench that the fact that the DDA made a profit from re-auction is irrelevant, as that would fly in the face of the most basic principle on the award of damages – namely, that compensation can only

> be given for damage or loss suffered. If damage or loss is not suffered, the law does not provide for a windfall."
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> (emphasis added)

40. In ***Ashokan v. Assistant Excise Commissioner and Others: (2009) 14 SCC 85***, the Supreme Court had referred to the various decisions and had held as under:

> "70. Forfeiture of earnest money under a contract for sale of property whether movable or immovable, **if the amount is reasonable**, would not fall within Section 74. That has been opined in several cases. (See *Kunwar Chiranjit Singh* v. *Har Swarup*; *Roshan Lal* v. *Delhi Cloth and General Mills Co. Ltd.*; *Mohd. Habib-ullah* v. *Mohd. Shafi* ; *Bishan Chand* v. *Radha Kishan Das*.) These cases have explained that forfeiture of a reasonable amount paid as earnest money does not amount to imposing a penalty. But if forfeiture is of the nature of penalty, Section 74 applies.
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> 71. Where under the terms of the contract the party in breach has undertaken to pay a sum of money or to forfeit a sum of money which he has already paid to the party complaining of a breach of contract, the undertaking is of the nature of a penalty. (See *Maula Bux* and *Saurabh Prakash* v. *DLF Universal Ltd.*)"
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> (emphasis added)

41. A Coordinate Bench of this Court had also considered the aforesaid issue in ***M.C. Luthra v. Ashok Kumar Khanna*** [RFA No.780/2017 decided on 27.2.2018] and observed as under:

> "15. In sum and substance what is held by the Constitution Bench of the Supreme Court in the cases of ***Fateh Chand (supra)*** and the recent judgment in ***Kailash Nath Associates (supra)*** is that whenever there is a breach of contract then earnest money which is

forfeited because of the breach, whether by a plaintiff or a defendant in a contract, the forfeiture is of that amount which are in fact liquidated damages specified under a contract and that for claiming damages under a contract, whether liquidated under Section 74 of the Contract Act or unliquidated under Section 73 of the Contract Act, existence of loss is a *sine qua non*. In other words, if no loss is caused to a seller who has in his pocket monies of buyer, then the seller can only forfeit a nominal amount unless the seller has pleaded and proved that losses have been caused to him on account of the breach of contract by the buyer. Once there is no pleading of loss suffered by a seller under an agreement to sell, then large amounts cannot be forfeited though so entitled to a seller under a clause of an agreement to sell/contract entitling forfeiture of 'earnest money' because what is forfeited is towards loss caused, and that except a nominal amount being allowed to be forfeited as earnest money, any forfeiture of any amount, which is not a nominal amount, can only be towards loss if suffered by the seller. Thus if there is no loss which is suffered by a seller then there cannot be forfeiture of large amounts which is not a nominal amount, simply because a clause in a contract provides so. The following has been held in the judgment in the case of ***Kailash Nath Associates (supra)***:-

(i) As per the facts existing in the case of ***Kailash Nath Associates (supra)*** the Single Judge of the High Court had held that since no damages were suffered by DDA therefore DDA could not forfeit the earnest money. (Para 30 of ***Kailash Nath Associates's*** case ***(supra)***).

(ii) The Division Bench of the High Court however set aside the judgment of the Single Judge by holding that amount tendered as earnest money can be forfeited because and simply forfeiture of amount called as earnest money can be forfeited in terms of the contract.

(Para 30 of ***Kailash Nath Associates's*** case ***(supra)*** reproducing Para 39 of the Division Bench judgment of the High Court).

(iii) Supreme Court in the case of ***Kailash Nath Associates (supra)*** as per Para 44 of its judgment holds that the Division Bench of the High Court had gone wrong in principle because compensation can be awarded (where there is breach of contract) only if loss or damage is suffered i.e. where there is no loss or damage suffered as a result of breach of contract no compensation can be awarded as law does not provide for a windfall i.e. large amounts though called contractually as earnest money cannot be forfeited unless loss is pleaded and proved to have been suffered. These observations have cross-reference to Para 34 of the judgment of ***Kailash Nath Associates's*** case ***(supra)*** where with reference to the para of ***Fateh Chand's*** case ***(supra)*** it is held that the language of Section 74 of the Contract Act that 'whether or not damage or loss is proved to have been caused by breach' is the language that such language only discharges proof of actual loss but that does not justify award of compensation where in consequence of breach no injury/loss has at all resulted.

(iv) Earnest money is an amount to be paid in case of breach of contract, and named in contract as such, and that forfeiture of earnest money is covered under the entitlement to liquidated damages under Section 74 of the Contract Act *vide* Para 40 in the case of ***Kailash Nath Associates (supra).***

(v) The language of Section 74 of the Contract Act that "whether or not actual loss or damage is proved to have been caused thereby" means only that where it is difficult or impossible to prove loss caused by the breach of contract then the liquidated damages/amount (being the amount of earnest money) can be awarded

> *vide* Para 43(6) of ***Kailash Nath Associates's*** case ***(supra)*** but where nature of contract is such that loss caused because of breach can be assessed and so proved then in such cases loss suffered must be proved to claim the liquidated damages of earnest money. This finding has cross reference to Para 37 of judgment in ***Kailash Nath Associates's*** case ***(supra)*** where the observations of Supreme Court in Para 67 of the case of ***ONGC Ltd. Vs. Saw Pipes Ltd. (2003) 5 SCC 705*** are quoted that liquidated damages are awarded where it is difficult to prove exact loss or damage caused as a result of breach of contract.
>
> (vi) Even where liquidated damages can be awarded under Section 74 of the Contract Act because loss or damages cannot be proved in a contractual breach yet if the liquidated damages (earnest money) are a penalty amount by its nature i.e. prescribed liquidated damages figure is unreasonable, then for the liquidated damages amount or earnest money amount forfeiture cannot be granted/allowed and that only reasonable amount is allowed as damages with the figure of liquidated damages being the upper limit *vide* Para 43(1) of ***Kailash Nath Associates's*** case ***(supra).***"

42. As noted above, in the present case, the respondent has neither pleaded nor established that it had suffered any loss. The respondent's case that it was entitled to forfeit the sum of ₹60,00,000/- paid by the petitioner rested solely on the ground that it was earnest money and therefore, it could be forfeited in terms of the Agreement. However, as noticed above, in ***Kailash Nath Associates*** (*supra*), the Supreme Court had in unambiguous terms held that Section 74 of the Indian Contract Act would apply in cases of forfeiture of earnest money under the contract. The Court had further held that where it is possible to prove

actual damages of loss, such proof is not dispensed with.

43. In the given circumstances, without the respondent establishing that it had suffered any loss whatsoever on account of the petitioner failing to close the transaction for purchase of the Property would be impermissible for the respondent to forfeit the amount of ₹60,00,000/-, which admittedly is not a nominal amount, and constitutes substantial portion of the consideration.

44. In view of the above, the impugned award to the extent that it accepts that the respondent was entitled to forfeit the amount of ₹60,00,000/- is set aside.

45. The petition is, accordingly, disposed of.

**VIBHU BAKHRU, J**

**MAY 19, 2022**
**RK**