


Advanced Contracts, Tendering and Public Procurement
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Breach of Contracts – Part 2

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Section 73

Compensation for Loss or Damage caused by breach of Contract – 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, then 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 reason of the breach.

Explanation – In estimating the loss or damage arising from a breach of contract, the means which existed of remedying the inconvenience caused by the non-performance of the contract must be taken into account.



If one looks at Section 73 of the Indian Contract Act, it clearly states that in compensation for loss or damage caused by the breach of contract, the party who has broken the contract is entitled to give that compensation to the party who suffers such loss or damage due to the broken contract.

However, Section 73 very clearly underlines the rule that the loss or damage that naturally arises in the usual course of things is the only kind of damages that are available. This brings you to the distinction between direct loss and indirect loss or what we call as direct damages or consequential damages.

Now, in India, in ordinary contracts, only direct damages are awarded. However, in cases regarding infringement of intellectual property rights, the courts may grant you some consequential loss. So, depending upon the kind of breach of the contract there could be some kind of variation.

But the ordinary rule which looks at the implementation of Section 73 of the Indian Contract Act 1872 clearly states that the loss should have naturally arisen from the breach and it is something that should occur in the usual course of things and that is all that is what entitles

you to get damages. So interestingly, if I can give a simple illustration of what can be such damages is let us assume that I have promised to sell something to you.

Say it could be a laptop, and the price of the laptop is around 60,000 rupees and I do not after making a contract supply this laptop to you. Now, what should be the damages in case I failed to supply this laptop to you? Now, it cannot be 60,000. Why? Because you must pay me 60,000 if I deliver that laptop to you.

So, I have saved that 60,000 for you. You have not incurred any kind of loss even though I have breached the promise and I have not delivered the laptop to you. Here, you cannot give proof of damages and that is not something you can be entitled to, though it can be considered as something that has naturally arisen but the loss is not naturally arisen.

What is the loss in the usual course of such a breach of contract if I do not supply the laptop? Let us assume that you need this laptop. Obviously, I agreed to 60,000 for the same laptop, but because of my breach, now you must go to the market and buy this laptop at 70,000 rupees.

Please note, this difference between the 60,000 that I promised and the actual price at which you bought is 10,000 rupees, the difference is 10,000 rupees and this difference has naturally arisen in the usual course of this contract and is a consequence of the breach that I committed. Had I performed, you would have just spent 60,000.

Now that I did not perform, you must buy it at 70,000, and the difference of 10,000 between what was agreed to, and how much you buy it for is the kind of loss or damage that is caused to you, and that is all you will be entitled to as the direct consequences of my breach of not selling that laptop.

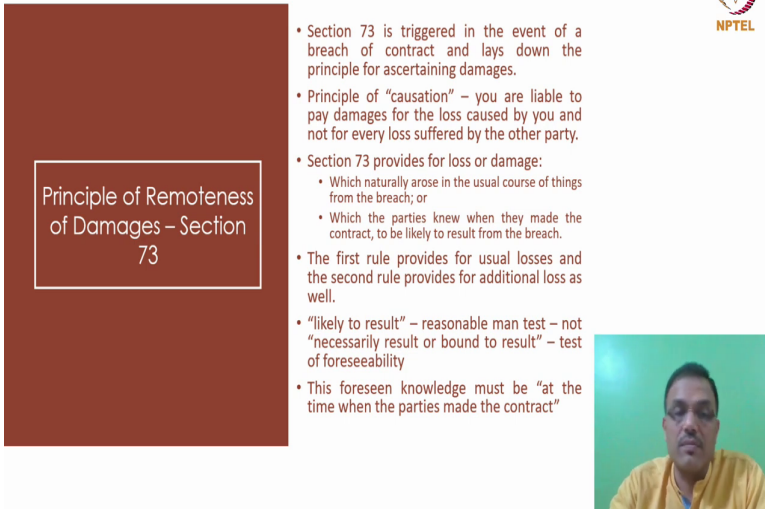

So now, if you look at the laptop example, we could argue that there are other kinds of losses that have occurred and why cannot we claim damages for that? For this, we must discuss the other kind of losses that you may have suffered. Now, let us say that the contract was supposed to be performed on the 1st of May and I did not perform and it took some time for you to understand that there is a breach, and by the 30th of May, you went and bought this laptop, though, at a difference of 10,000 rupees.

Now, these 30 days that unfortunately occurred because of a delay due to my breach, you lost, say, an opportunity to make a presentation and if you would have done that presentation using this new laptop, you would have gotten a new contract, and if you got that contract, you would have made profits. Now, can I, who had agreed to supply this laptop to you, be made responsible for all these events?

For the kind of losses that might be anticipated sometimes, you may say sometimes not known, something that was not foreseeable but something that you want to substantiate and say, “Look. these are the kind of losses that I could have incurred or that have already occurred to me.”


So, everyone who supplies laptops must know that time is important to the buyer, they will use it, it is of business value and it can result in profits and anyone who fails to supply their laptop must also be responsible for the same, is something that people can argue and bring that discussion forward as well.

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Principle of Remoteness of Damages – Section 73

- Section 73 is triggered in the event of a breach of contract and lays down the principle for ascertaining damages.
- Principle of “causation” – you are liable to pay damages for the loss caused by you and not for every loss suffered by the other party.
- Section 73 provides for loss or damage:
 - Which naturally arose in the usual course of things from the breach; or
 - Which the parties knew when they made the contract, to be likely to result from the breach.
- The first rule provides for usual losses and the second rule provides for additional loss as well.
- “likely to result” – reasonable man test – not “necessarily result or bound to result” – test of foreseeability
- This foreseen knowledge must be “at the time when the parties made the contract”



So, the principle of remoteness of damage clearly states that “Look, you are liable to pay damage for the loss caused by you not for every loss that the other parties suffer. So, when he was supposed to make a presentation, he was supposed to get a contract, and he was supposed to make a profit, I am not sure whether I have contributed to that kind of a loss.

How can I be sure that one laptop will result either in profits or losses? Is it something that I have contributed, is it due to a natural cause of my fault? This is something that people will

have to answer before they claim damages. So, one is what is the natural course of things in the usual contractual business? That is the pre-checker, and what is the realistic direct loss that is caused to the other party?

Second, it is important that sometimes you will notice that the parties if they knew that the consequence of the breach can be a, b, and c, and hence, I have already informed you that this could be the loss that I incur.

Then there is a possibility and a chance that look that is not remote because the party knew it, the party was told about it, and he was informed about it, very well in advance that this is required for the presentation. The presentation of this value, the contract is due, and hence if you do not give it this is the loss. So, if that is already known and the breach occurs then because of that kind of knowledge it is not remote to the contract breaker.

And he may be responsible to compensate for those kinds of losses that were brought to his knowledge that was brought to his information as well. So, though they may be consequential, they were something that was already informed to the other party. The second rule is that when you talk about additional losses, again when it comes to consequential or additional losses that are known, you must notice that there must be a direct cause and effect theory.


So, you cannot, even if I say something to you beyond what is the cause and effect, cause of the contract to the effect of the breach, then the courts are not going to give it to you just because you mentioned it. So, there must be a causation, there must be a link to the direct loss and it must be a result of the breach. It should be a kind of a chain of events that has occurred due to the breach and not beyond it most importantly the courts will apply the reasonable man test and they will probably give damages that are just necessary enough to compensate you that can in a reasonable man's expectation be something that can be awarded.

But again, the reason simply is that the principal rule of unjust enrichment applies to the law of damages in India. So, while you talk about equity, you talk about contracts in various stages, even in the stage of remedies the courts will apply unjust enrichment and say, "Look, you cannot avoid damages that will make him rich unjustly, you must give damages that should be adequate to compensate him but not make him rich otherwise.

So, reasonability and unjust enrichment will tie the hands of the judge and make him do equity and not unnecessarily create some kind of profit or profitability for the one who seeks the same. And what is important is that this kind of foreseeability of the kind of losses that can be anticipated for the other party must be such that is made at the time of the contract, not at the time when the breach occurs.

So, when I made the contract, can I foresee that this is the loss that can happen to the other party, if, yes, or if it is not foreseeable and it is communicated, then I shall be liable for it, not otherwise.

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Hadley v. Baxendale, (1854) EWHC J70

FACTS:
H, owner of a mill, contracted B, a common carrier, to deliver a crankshaft to engineers for repair by a certain date at a cost of £2.4 without delay. B failed to deliver on the date in question, causing H to lose business. H sued for profits he lost due to B's late delivery.

Issue:
Whether B could be held liable for damages that he was not aware would be incurred from a breach of contract?

Held:
"Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonably be considered either arising naturally, i.e., according to the usual course of things, from such breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it." **Held that B is liable only for losses that were generally foreseeable, or if H had mentioned his special circumstance in advance.**

Illustration (j) of Section 73,




Now, a couple of cases that one would want to look at is the Hadley versus Baxendale rule. In this case, it was very clearly held and please note this was before the 1872 law. Illustration 1 of Section 73 says exactly what this case is about and this case very clearly says that "Look, if a common carrier delays in the delivery of a crankshaft to an engineer. Did the common carrier know that the delay will cause, losses apart from just being the delay of delivery?" So, I think the court here very clearly said that you can be liable for those kinds of losses that can be generally foreseeable by a reasonable man. So, if I am a carrier and I am delivering something to you and if there is a delay, for that delay, whatever is the kind of pro rata loss, I may be responsible.

But suppose you do not get this crankshaft into your engine and because of that, you lost customers, profitability, and business, how will a common carrier or a delivery person ever

knows what is this used for, how valuable it is, how many customers or profit you are making, this is not something that people will know, especially if you are a common carrier.

So, yes, a delay is to be made actionable and accountable, but you cannot expect them to foresee your business, and your loss and expect them to cover those kinds of losses as well.

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Victoria Laundry Ltd. v. Newman Industries Ltd.,
(1949) 1 All ER 997

FACTS:
Victoria Laundry Ltd (VLL) ordered a new large boiler from Newman Industries Ltd. (NIL) in order to extend their business and in contemplation of some lucrative dyeing contracts from Ministry of Supply. As per the contract, the boiler was to be delivered and installed by June 5. However, it was delivered on 8 November. There was a delay of 5 months. NIL were aware of the nature of plaintiff's business, and by letter had been informed by VLL that they intended to put the boiler to use in the shortest possible space of time. In the damages claimed by VLL for breach of contract they wanted to claim the loss of business profits suffered by them.

Issue:
Whether VLL could also claim from NIL the profits it would have made if they had been able to take advantage of the lucrative Ministry of Supply contracts?

Held:
NIL had to compensate for the ordinary, not the extraordinary loss of profits. Losses from "particularly lucrative dyeing contract" are different type of loss which would only be recoverable if the defendant had sufficient knowledge of them to make it reasonable to attribute to him acceptance of liability for such losses. In the present case, NIL were not aware of the "lucrative contracts" that VLL intended to benefit from but were only aware of the general business of VLL. They are only liable to pay "general/ordinary loss of profits" and not extraordinary loss of profits from lucrative Ministry of supply contracts.




The second case is the Victoria Laundry case, this is also a very interesting case that mentions profits. Because what this case clearly says is that you can be made liable for loss of profit, but in profit, it is the general and ordinary profits that are lost that can be covered, and not extraordinary loss of profits.

So, when damages are awarded to you, you are not going to be lucratively rewarded for the breach that is committed by the other party. If you decide that yes, profits must also be granted or what we call interest must be granted, for example, under Section 74 we say interest on damages can also be awarded as a penalty.

And the courts have consistently held that penalty in Indian Contract Law can also be given over and above damages, but in the form of a penalty if it so required in that context. So, profits, that too ordinary profits are an expected loss due to the kind of lucrative business that you are running and because of the breach, or that lucrative business is no longer lucrative.

So, to that extent, what is the benefit that has been lost in the business can be covered, but it is not extraordinary loss of profit that will be covered in the contract.

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Heron II, Koufos v. C Czarnikow Ltd., (1969) 1 AC 350


FACTS:
Koufos, a firm of sugar merchants, chartered a ship (the Heron II) from Czarnikow to carry 3000 tons of sugar from Costanza to Basra. The ship deviated on the voyage and the cargo was delayed by 9 days. In the meantime, sugar market fell at Basra and Koufos obtained £3,800 less than the price obtainable when it should have been delivered. Koufos claimed this loss of profit as damages. Czarnikow argued that they knew there was a sugar market, but not that Koufos intended to sell it straight away.

Issue:
Whether the loss of profit was too remote?

Held:
It was held that the loss of profit was not too remote.
The test for remoteness in contract is narrower than it is in tort.

In determining whether a particular type of loss or damage, such as consequential loss of profit, is recoverable as damages for breach of a contract of carriage of goods, the crucial question is whether, on the information available to the defendant carrier when the contract was made, the loss or damage was sufficiently likely to result from the contract to make it proper to hold that the loss of damage flowed naturally from the breach or that loss or damage of that kind should have been within his contemplation.

It was held that loss of profit was recoverable as damages for breach of the contract of carriage by deviation involving delay because on the knowledge available to the shipowner when the contract was made, the sale of the sugar in Basra market on ship's arrival was something of which there was such probability that it should be regarded by the court as arising in the usual course of things and as being, within the contemplation of the parties at the time of the contract.



This is also a similar case of whether the loss of profit was too remote. Again, it was a case of cargo that was delayed by 9 days. It was sugar that had to be delivered between two destinations. Interestingly because of the delay of 9 days the sugar market fell at Basra and they had to sell the sugar at a loss.

If it had arrived on time, they would have made a lot of profit. So, for this, they asked the carrier to compensate them. So, can a carrier that deliberately deviates on its voyage, knowing that a delay may cost loss be held responsible or liable was the question in this case.

Now, interestingly, the ship owner, in this case, knew what he was carrying and he was aware that it was an essential commodity, that it was meant to be sold at Basra on a particular date and there was a high probability that had the ship arrived on that day it would have been sold for some profit and the captain of the ship, and it was a chartered ship in any sense.

Charter ships cannot have deviation. This is one important rule and the entire ship had to only serve one customer. So, deviations cannot be justified in any manner and if suppose the delay was of 9 days due to some other events that were not within the control of parties, probably the court would have taken a lenient view, but not otherwise.

So, in this case, I think because of the rule of probability, I think profits were also granted in this case because that was something that can be easily anticipated and should have been granted to the parties.