REPORTABLE

IN THE SUPREME COURT OF INDIA

CIVIL APPELLATE JURISDICTION

CIVIL APPEAL NO. 3343 OF 2005

Phulchand Exports Ltd. …. Appellant

Versus

OOO Patriot ….Respondent

JUDGMENT

R.M. Lodha, J.

This appeal, by special leave, occupied judicial time of almost whole day, and the basic question raised is this : whether enforcement of the award dated October 18, 1999 given by the International Court of Commercial Arbitration at the Chamber of Commerce and Industry of Russian Federation, Moscow in favour of the respondent is contrary to public policy of India under Section 48(2)(b) of the Arbitration and Conciliation Act, 1996.

2. By contract dated November 18, 1997, between — Phulchand Exports Limited, Mumbai, India ('the sellers') and OOO Patriot, Moscow, Russia ('the buyers'), a transaction relating to sale of 1000 Metric Tons of Indian long grain 1.5 time polished rice PR—106 of 9 per cent broken maximum (for short, 'the goods') for a price fixed at INR 12,450 (Indian Rupees twelve thousand four hundred fifty only) per one metric ton net on CIF (liner out) Novorossiysk, Russia basis was concluded. The price was fixed according to Incoterms-90 and included value of the goods, packing and marking, loading into hold, stowing of the cargo, fulfilling the customs formalities in the sellers' country, insurance, freight charges, berthing charges and unloading charges of the goods at the port of Novorossiysk. The total value of the contract was firm and fixed at INR 12,450,000,00 (Indian Rupees twelve million four hundred fifty thousand only). It is upon this contract, and on what was done under it, that the above question in this appeal turns. Some of the relevant terms, and, omitting clauses which do not appear important, are as follows :

> "1. SUBJECT OF CONTRACT :
>
> ……the Goods on CIF Novorossiysk port, Russia basis,…….

2. PRICE OF THE CONTRACT

.....The price is fixed on the terms of CIF (liner out) Novorossiysk, Russia according to Incoterms—90……

3. TERMS OF PAYMENT

Payment for the Goods, delivered under the present contract is to be effected by irrevocable documentary Letter of Credit opened in favour of the sellers for the total value of the contract for the period of 45 days…....

The L/C is governed by "ICC Uniform customs and practice for documentary L/C"……..

The L/C should be opened within 10 working days from the date of signing of the contract.

The L/C is executed by the beneficiary's bank against presentation by the sellers of the following documents:

x x x x x x x x

3. Insurance Policy for 11% of the value of the Goods, Covering all risks stipulated in the Institute Cargo Clauses (A), Institute War Clauses, Institute Strike Clauses till the completion of the unloading of the Goods at the port of Novorossiysk, issued in the name of the Buyers Bank – Joint Stock Commercial Bank AVTOBANK, Moscow, Russia.

x x x x x x x

4. TERMS OF DELIVERY

Shipment should be done on the basis of CIF (liner out) Novorossiysk, Russia in accordance with Incoterms – 90.

The Goods sold under the present contract should be shipped within 40 days from the date of opening the L/C.

The date of shipment is the date of loading of the Goods to the board of vessel……..

Shipment should be done by a vessel that is on the way to Novorossiysk as the first port of discharge. The Sellers shall take all possible measures that transit time of the Goods to Novorossiysk, Russia will not exceed 25 days.

x x x x x x x x x

The sellers shall take all possible measures for placing the Goods in such a way that it will be free for examination and will not be blocked up by any other cargo while unloading at the port of Novorossiysk…….

Insurance Policy for 110% of the value of the Goods, covering all risks, stipulated in the Institute Cargo Clauses (A), Institute War Clauses, Institute Strike Clauses till the completion of the unloading of the Goods at the port of Novorossiysk, issued in the name of the Buyers Bank – Joint Stock Commercial Bank AVTOBANK…….

x x x x x x x x

In case the Goods do not arrive to the customs area of Russian Federation within 180 days from the date of payment the transferred amount is to be reimbursed to the Buyers' account.

8. PENALTY

The Sellers are obliged within 5 working days from the date of receipt of the Buyers advice of the L/C to open in favour of the Buyers the Performance Bond issued by the Sellers Bank for 2% of the total value of the Contract in favour of the Buyers valid for 60 days from the date of opening of the L/C. The original of the said document should be dispatched to the Buyer's by courier mail. The

copy of the AWB should be faxed to the Buyers immediately.

x x x x x x x x

When failing to deliver the goods in time stipulated in clause 4 of the present Contract, the Sellers are to pay penalty to the Buyers at the rate of 0.3% of the value of non-delivered Goods per each day of delay from the 5th day after expiry of the delivery date to the 15th day inclusive. Total amount of penalty should be paid to the Buyers within 10 days from the date of bill in the currency of the Contract.

9. TERMS OF CANCELLATION OF THE CONTRACT

The Buyers have the right to cancel the Contract under the following circumstances:

The quality of the delivered Goods does not correspond to the Appendices No. 1 and No. 2 to the present Contract
(according to the report of the State Board Inspection of Russian Federation for the testing of the Goods at the port of shipment Kandla (India).

The date of shipment of the Goods is postponed by the Sellers beyond the period of more than 15 days.

The Sellers have the right to cancel the Contract if the date of the opening of the L/C is postponed for the period of more than 15 days from the agreed date.

x x x x x x x x."

3. The buyers opened irrevocable letter of credit ('L/C') for the total value of the contract on December 3, 1997 with the last

date of shipment – January 12, 1998. On presentation of documents by the sellers, the bank honoured L/C and paid the amount to the sellers. The sellers shipped goods on January 29, 1998 – 16 days later of the stipulated time and the vessel freighted by the sellers left the port of loading viz., Kandla (India) on February 20, 1998 — 38 days later than the time of departure stipulated in the contract. The goods never reached the port of destination (port of Novorossiysk). It so happened that the vessel carrying the goods suffered an engine failure as a result of which it was declared 'General Average' by the Master of the vessel. In salvage operation, the vessel was rescued and taken to the Turkish sea port of Eregli. The owner of the rescue vessel claimed to the Admiralty Court of Eregli to arrest the vessel with the cargo in an action for enforcement of the lien against the vessel. The concerned court took judgment to arrest vessel towards the cost of rescue and the entire cargo was sold out to compensate the cost of rescue of the vessel.

4. The buyers lodged their claim with the United India Insurance Company Limited (insurers) on August 24, 1998 due to non-delivery of the goods to Novorossiysk. However, insurers denied their liability under the insurance policy for the loss of goods

on the ground that risk of detention was not covered. Their stand was that the insured voyage having been frustrated due to detention of the cargo, there was no liability under the policy. The sellers also took up the matter with the insurers and they were informed by the insurers vide letters dated September 16, 1998 and December 29, 1998 that the liability of the insurers was not established and the parties (the sellers and the buyers) must act as the goods were uninsured.

5. On November 27, 1998 the buyers lodged claim against the sellers for recovery of amount of USD 285,569.53 in the International Court of Commercial Arbitration at the Chamber of Commerce and Industry of the Russian Federation (for short 'Arbitral Tribunal"). The buyers' claim was admitted for consideration by the Arbitral Tribunal on December 7, 1998. The sellers did not acknowledge the buyers' claim and set up the defences that they have honoured all commitments under the contract; the risk in the goods and the property in the goods passed to the buyers upon shipment of the goods i.e. the date on which the goods were loaded on board the vessel being January 29, 1998 and in any event the property in the goods passed over to the buyers when their shipping documents were handed over through the banking channels upon

negotiations of the letter of credit, namely on February 19, 1998. According to the sellers, if for some reasons the goods were not received by the buyers then they had remedies under the policy of insurance against insurers or against the ship owners but in so far the sellers were concerned, they were not liable. The sellers also set up the defence that the delayed shipment was acquiesced to and accepted by the buyers as they were informed of the delay of shipment; the buyers had right to repudiate the contract on the ground of delay in shipment which they never did. The sellers thus submitted before the Arbitral Tribunal that the claim was misconceived and liable to be dismissed.

6. The Arbitral Tribunal held its sessions on various dates; heard the parties through their representatives and delivered its judgment (verdict) on October 18, 1999. The Arbitral Tribunal did not find any merit in the defences set up by the sellers. It held that the sellers broke the terms of the Contract (Article 4) and shipped goods on January 29, 1998 – 16 days later of the stipulated time and the vessel freighted by the sellers left the port of Kandla (India) on February 20, 1998 – 38 days later than the time of departure stipulated in the contract. The sellers gave a line bill of lading giving a carrier right to determine the line of unloading and the consecutive

order of destination of sea ports and, thus, at the moment of loading on board the vessel was no longer to reach the port of Novorossiysk as the first port of discharge in accordance with the terms of contract. The vessel with cargo had not arrived at the port of Novorossiysk on the date of lodging the claim (as a matter of fact the vessel never reached the port of destination). The Arbitral Tribunal held that there was clear term about the commitment of the sellers to reimburse the paid amount towards goods in case of non- arrival. The Arbitral Tribunal referred to the sellers' conduct in sending its representatives to Eregli (Turkey) to find out the situation of goods and observed that it was evident therefrom that the sellers did not consider themselves exempted from the commitment for fate and safety of the goods. It was held by the Arbitral Tribunal that the sellers did not prove the fact of force majeure which could discharge them from their liability. The Arbitral Tribunal, however, found that there was delay on the part of the buyers in acting in accord with clause 4 of the Contract; they (buyers) did not pass the insurance certificate and cargo documents to the sellers and the buyers did not demand from the sellers reimbursement of the transferred amount immediately after expiration of 180 days (i.e. 26-27/11/1998). The Arbitral Tribunal,

therefore, split the amount of losses between the parties – buyers and sellers – in equal parts and ordered that the sellers shall pay the amount of USD 138,402.03 to the buyers. The Arbitral Tribunal awarded interest in the some of USD 2,562.71 payable by sellers to the buyers and also directed the sellers to pay the amount of USD 4,869.00 to recover claimant's expenses to pay registry and arbitrage fees.

7. The buyers filed Arbitration Petition on December 22, 2000 before the High Court of Judicature at Bombay under Sections 47 and 48 of the Arbitration and Conciliation Act 1996 (hereinafter referred to as 'the 1996 Act') for enforcement of the above award.

8. The sellers contested the petition on the ground that subject award was contrary to the principles of public policy and, therefore, the award was unenforceable.

9. The Single Judge of the Bombay High Court in his order dated July 16, 2001 did not find any merit in the objections raised by sellers; overruled the objections and held that the award dated October 18, 1999 could be enforced as a decree of the Court.

10. Against the order of the Single Judge, the sellers preferred appeal before the Division Bench. The Division Bench relying upon the decision of this Court in *Renusagar Power Co. Ltd*

vs. General Electric Co.[1] held that award was purely based on findings of facts and no public policy was involved and the Single Judge rightly dismissed the petition. Consequently, the Division Bench by its order dated May 3, 2002 dismissed the appeal.

11. Mr. Krishnan Venugopal, learned Senior counsel for the appellant at the outset submitted that test concerning public policy applied by the Division Bench based on the decision of this Court in *Renusagar Power Co. Ltd*[1]. is flawed. He referred to a subsequent decision of this Court in *Oil and Natural Gas Corporation Ltd. vs. Saw Pipes Ltd.*[2] and submitted that this Court has given wider meaning to the expression "public policy of India" used in Section 34 of the 1996 Act in that case. He submitted that the wider meaning given to the expression "public policy of India" used in Section 34 by this Court has also been applied to the same expression occurring in Section 48 (2)(b) of the 1996 Act. He, thus, submitted that the matter needs to be sent back to the High Court for reconsideration on this ground alone.

12. It is true that in *Renusagar*[1], relied upon by the Division Bench, a narrower meaning has been given to the expression 'public policy of India' while this Court in a subsequent decision in

[1] AIR 1994 SC 860
[2] (2003) 5 SCC 705

the case of *Saw Pipes Ltd.*[2] has given wider meaning to that expression. This Court in the case of *Saw Pipes Ltd.*[2] (para 31, page *727)* stated as under:

> "31. Therefore, in our view, the phrase "public policy of India" used in Section 34 in context is required to be given a wider meaning. It can be stated that the concept of public policy connotes some matter which concerns public good and the public interest. What is for public good or in public interest or what would be injurious or harmful to the public good or public interest has varied from time to time. However, the award which is, on the face of it, patently in violation of statutory provisions cannot be said to be in public interest. Such award/judgment/decision is likely to adversely affect the administration of justice. Hence, in our view in addition to narrower meaning given to the term "public policy" in *Renusagar case* it is required to be held that the award could be set aside if it is patently illegal. The result would be — award could be set aside if it is contrary to:
>
> (*a*) fundamental policy of Indian law; or
> (*b*) the interest of India; or
> (*c*) justice or morality, or
> (*d*) in addition, if it is patently illegal.
>
> Illegality must go to the root of the matter and if the illegality is of trivial nature it cannot be held that award is against the public policy. Award could also be set aside if it is so unfair and unreasonable that it shocks the conscience of the court. Such award is opposed to public policy and is required to be adjudged void."

13. There is merit in the submission of learned senior counsel that in view of the decision of this Court in *Saw Pipes Ltd.*[2], the expression 'public policy of India' used in Section 48 (2)(b) has to be

given wider meaning and the award could be set aside, 'if it is patently illegal'. At the first blush we thought of remanding the matter to the High Court, but on a deeper thought, we decided to hear the objections relating to patent illegality in the award ourselves as the award by the Arbitral Tribunal was given as far back as on October 18, 1999 and about 12 years have elapsed since then. We thought that the issue relating to enforceability of the subject award must be brought to an end finally one way or the other.

14. Mr. Krishnan Venugopal, learned Senior counsel strenuously urged that the contract entered into between the sellers and the buyers was a CIF contract and the risk in the goods and the property passed over to the buyers upon the shipment of the goods on January 29, 1998 and in any case the property in the goods passed over to the buyers when the shipping documents were handed over to them through the Banking channels on negotiations of letter of credit on February 19, 1998. He would submit that from this day the sellers' liabilities ceased to exist. In this connection he relied upon a decision of this Court in *Maula Bux vs. Union of India*[3]. He also referred to Section 26 of the Sale of Goods Act, 1930 (for short '1930 Act').

[3] 1969 (2) SCC 554

15. Learned Senior counsel also submitted that the stipulation in clause 4, "in case the goods don't arrive the customs area of Russian Federation within 180 days from the date of payment the transferred amount is to be reimbursed to the Buyers' account" amounts to penalty within the meaning of Section 74 of the Contract Act, 1872 (for short, `1872 Act') and being unconscionable bargain is void under Section 23 of the 1872 Act and, therefore, enforcement of the subject award by the Indian Courts is contrary to 'public policy of India'. He relied upon two decisions of House of Lords; (i) *Lord Elphinstone vs. The Monkland Iron and Coal Company Limited, and Liquidators*[4]*; and* (ii) *Dunlop Pneumatic Tyre Company Limited vs. New Garage and Motor Company Limited*[5].

16. C.I.F. (Cost, Insurance, Freight) contract is well-understood by the people in commerce and in law. In Kennedy's C.I.F. Contracts (Third Edition) revised by Dennis C. Thompson, a C.I.F. contract is explained (at page 1) thus :

> "……It is a contract which contemplates the carriage of goods by sea, and is the most common form of shipping contract in use today. It is known as a c.i.f. contract, for the price which the buyer has to pay is the cost of the goods, together with the insurance of the goods during transit and the freight to the port of destination.

[4] 1886 House of Lords VOL. XI page 332
[5] (1915) AC 79

> Under this form of contract the seller performs his obligations by shipping, at the time specified in the contract or, in default of express provision in the contract, within a reasonable time, goods of the contractual description in a ship bound for the destination named in the contract, or by purchasing documents in respect of such goods already afloat, and by tendering to the buyer, as soon as possible after the goods have been destined to him, the shipping documents, i.e., a bill of lading for carriage of goods, a policy of insurance covering the reasonable value of the goods, together with an invoice showing the amount due from the buyer."

17. In C.I.F. and F.O.B. Contracts (Fourth Edition) by David M. Sassoon dealing with essence of C.I.F. contracts, it is stated that essential feature of a C.I.F. contract is that delivery is satisfied by delivery of documents and not by actual physical delivery of the goods. Shipping documents required under a C.I.F. contract are bill of lading, policy of insurance and an invoice.

18. In *Johnson* v. *Taylor Bros.*[6], Lord Atkinson in the House of Lords explained the meaning of C.I.F. contract as under :

> "……. when a vendor and purchaser of goods situated as they were in this case (Seller in Sweden and buyers in England) enter into a c.i.f. contract, such as that entered into in the present case, (Ordinary c.i.f. terms), the vendor in the absence of any special provision to the contrary is bound by his contract to do six things. First, to make out an invoice of the goods sold. Second, to ship at the port of shipment goods of the description contained in the contract. Third, to procure (There might be added the words "on shipment, see ante, § 7") a contract of affreightment under which the goods will be delivered at

[6] [1920] A.C. 144 at p. 155

the destination contemplated by the contract. Fourth, to arrange for an insurance upon the terms current in the trade which will be available for the benefit of the buyer. Fifthly, with all reasonable despatch to send forward and tender to the buyer these shipping documents, namely, the invoice, bill of lading and policy of assurance, delivery of which to the buyer is symbolical of delivery of the goods purchased, placing the same at the buyer's risk and entitling the seller to payment of their price……..".

19. Section 26 of the 1930 Act upon which reliance was placed by the learned senior counsel for the sellers reads as follows :

> **"**S. 26. Risk *prima facie* passes with property.— Unless otherwise agreed, the goods remain at the seller's risk until the property therein is transferred to the buyer, but when the property therein is transferred to the buyer, the goods are at the buyer's risk whether delivery has been made or not:
>
> Provided that, where delivery has been delayed through the fault of either buyer or seller, the goods are at the risk of the party in fault as regards any loss which might not have occurred but for such fault:
>
> Provided also that nothing in this section shall affect the duties or liabilities of either seller or buyer as bailee of the goods of the other party."

20. The title of Section 26 shows that the rule provided there-under is the prima facie rule subject to the agreement otherwise between the parties. This is clearly indicated by the expression "unless otherwise agreed" with which the section begins. The parties

to the contract are, thus, free to by-pass the prima facie rule provided in Section 26 by making agreement otherwise. The prima facie rule in Section 26 is that the goods remain at the seller's risk until the property in the goods is transferred to the buyer. But when the property in the goods is transferred to the buyer the goods are at the buyer's risk whether delivery has been made or not. The above rule has some exceptions. The first proviso provides that where delivery of goods has been delayed due to the fault of either buyer or seller, the goods are at the risk of the party in fault as regards any loss which might not have occurred but for such fault. The second proviso is further subject to the first proviso and provides that nothing in the section shall affect the duties or liabilities of either seller or buyer as bailee of the goods of the other party.

21. The obligations upon a seller under a C.I.F. contract are well known, some of which are in relation to goods and some of which are in relation to documents. In relation to goods, the seller must ship goods of contract description on board a ship bound to the contract destination. If there is a late shipment or the seller has put goods on board a ship not bound to the contract destination as stipulated, in our view, the logical inference that must necessarily

follow is that the seller has not put on board goods conforming to a contract destination.

22. In the present case, as we see it, there is late shipment of goods by 16 days. Besides delay in shipping the goods and the delayed departure of the vessel from the port of loading, the goods were shipped in a vessel having no firm commitment to reach the port of Novorossiysk as the first port of discharge. As a matter of fact the sellers gave a line bill of lading giving a carrier right to determine the line of unloading and the consecutive order of destination of sea ports and as a result of that the goods were loaded on board the vessel that was no longer to reach the port of Novorossiysk as first port of discharge. The contract clearly provides in clause 4 that shipment should be done by a vessel that is on way to Novorossiysk as the first port of discharge. This term in the contract is not inconsequential or immaterial but seems to be fundamental having regard to the subject matter of the goods. The sellers breached the terms of the contract at the very threshold by late shipment of goods and by loading on board the vessel which was no longer to reach the port of Novorossiysk as the first port of discharge. The sellers having breached the terms of the C.I.F. contract at the threshold, it is very difficult to hold that property in the goods got transferred out and out to the buyers on

shipment of the goods or when the shipping documents were handed over to the bank for negotiations of L/C. In a case such as this one, the sellers' failure to discharge the primary obligation under the contract regarding the shipment of goods can be held to have resulted in postponement of transfer of title in goods to the buyers. In any case the prima facie rule contemplated in Section 26 of the 1930 Act stands rebutted in the facts of the present case.

23. Even if the property in the goods is deemed to have transferred to the buyers, since there was no delivery of the goods due to the fault of the sellers in shipment of the goods, firstly belatedly and then by a vessel that was not on way to Novorossiysk as the first port of discharge, the goods continued to be at the risk of the sellers as they were in fault. In that situation, first proviso to Section 26 of the 1930 Act is clearly attracted.

24. We do not find any merit in the case set up by the sellers that their liability ceased to exist on shipment of the goods on January 29, 1998 or in any case when the shipping documents were handed over through the banking channels on negotiations of Letter of Credit. As in the present case, the sellers were in breach at the threshold, it is immaterial whether or not the buyers had a right of action against the insurers or carrier.

25. The buyers' claim was founded on the breach of contract by the sellers and particularly with reference to the last paragraph of clause 4 of the contract that provided, "in case the goods do not arrive to the customs area of Russian Federation within 180 days from the date of payment the transferred amount is to be reimbursed to the buyers' account". The goods not only did not arrive to the customs area of Russian Federation within 180 days from the date of payment but they never arrived at all in the customs area of Russian Federation/the port of Novorossiysk (port of discharge). The Arbitral Tribunal held that there were breaches by the sellers and that the above clause for reimbursement could be invoked by the buyers. The Arbitral Tribunal, however, did not award the full price paid by the buyers to the sellers but instead awarded half of that amount as there was delay by the buyers in invoking the clause of reimbursement and the buyers also did not pass the shipping documents and the insurance certificate to the sellers. The contention of the learned senior counsel for the sellers in contesting the enforcement of the award is that the clause of reimbursement amounts to 'penalty' within the meaning of Section 74 of the 1872 Act and also unconscionable bargain and, therefore, void under Section 23 of that Act. He would,

thus, submit that enforcement of such award would be contrary to public policy of India.

26. Section 73 of the 1872 Act provides for compensation for loss or damage caused by breach of contract and Section 74 makes a provision for compensation for breach of contract where penalty is stipulated for. These two Sections – 73 and 74 – of the 1872 Act read as under:

> "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, 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 reason of the breach.
>
> Compensation for failure to discharge obligation resembling those created by contract.—When an obligation resembling those created by contract has been incurred and has not been discharged, any person injured by the failure to discharge it is entitled to receive the same compensation from the party in default, as if such person had contracted to discharge it and had broken his contract.
>
> *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.

> S. 74. Compensation for breach of contract where penalty stipulated for.—When 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 damage or loss is proved to have been caused thereby, to receive from the party who has broken the contract reasonable compensation not exceeding the amount so named or, as the case may be, the penalty stipulated for.
>
> *Explanation.*— A stipulation for increased interest from the date of default may be a stipulation by way of penalty.
>
> *Exception.*— When any person enters into any bail-bond, recognizance or other instrument of the same nature, or under the provisions of any law, or under the orders of the Central Government or of any State Government, gives any bond for the performance of any public duty or act in which the public are interested, he shall be liable, upon breach of the condition of any such instrument, to pay the whole sum mentioned therein.
>
> *Explanation.*— A person who enters into a contract with Government does not necessarily thereby undertake any public duty, or promise to do an act in which the public are interested."

27. Both these Sections provide for reasonable compensation in a case of breach of contract. None of these two Sections makes the award of liquidated damages illegal. Section 74, as observed by this Court, in the case of *Fateh Chand* v. *Balkishan Dass*[7] is, "an attempt to eliminate the somewhat elaborate refinements made under the English common law in distinguishing between stipulations

[7] (1964) 1 SCR 515

providing for payment of liquidated damages and stipulations in the nature of penalty……The Indian Legislature has sought to cut across the web of rules and presumptions under the English common law, by enacting a uniform principle applicable to all stipulations naming amounts to be paid in case of breach, and stipulations by way of penalty."

28. The plain reading of Section 74 would show that it deals with the measure of damages in two classes of cases (i) where the contract names a sum to be paid in case of breach and (ii) where the contract contains any other stipulation by way of penalty. In *Fateh Chand*[7], this Court held :

> "….The expression "if the contract contains any other stipulation by way of penalty" widens the operation of the section so as to make it applicable to all stipulations by way of penalty, whether the stipulation is to pay an amount of money, or is of another character, as, for example, providing for forfeiture of money already paid. There is nothing in the expression which implies that the stipulation must be one for rendering something after the contract is broken. There is no ground for holding that the expression "contract contains any other stipulation by way of penalty" is limited to cases of stipulation in the nature of an agreement to pay money or deliver property on breach and does not comprehend covenants under which amounts paid or property delivered under the contract, which by the terms of the contract expressly or by clear implication are liable to be forfeited."

29. In the case of *Maula Bux*[3] while dealing with Section 74 of the 1872 Act, this Court was concerned with the case of forfeiture of the amount of deposit. It was held, "forfeiture of 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". It was further held, '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'. We are afraid the decision of this Court in *Maula Bux*[3] does not support the contention of the learned senior counsel that the stipulation of reimbursement contained in last para of clause 4 of the contract to transfer the payment of goods already received by sellers in the event of non-delivery of the goods within 180 days in the customs area of Russian Federation amounts to penalty. The stipulation for reimbursement in the event stated in last para of clause 4 of the contract is not in the nature of penalty; the clause is not *in terrorem.* It is neither punitive nor vindictive. Moreover, what has been provided in the contract is the reimbursement of the price of the goods paid by the buyers to the sellers. The clause of reimbursement or repayment in the event of delayed delivery/arrival or non-delivery is not to be regarded as

damages. Even in the absence of such clause, where the seller has breached his obligations at threshold, the buyer is entitled to the return of the price paid and for damages. We can see no reason why the sellers should not be bound by it and the court should not enforce such term. No way the clause is in the nature of threat held over the sellers in terror.

30. Section 23 of the 1872 Act reads as under :

> "S. 23. What considerations and objects are lawful, and what not.— The consideration or object of an agreement is lawful, unless—
>
> it is forbidden by law; or
>
> is of such a nature that, if permitted, it would defeat the provisions of any law; or
>
> is fraudulent; or
>
> involves or implies injury to the person or property of another; or
>
> the Court regards it as immoral, or opposed to public policy.
>
> In each of these cases, the consideration or object of an agreement is said to be unlawful. Every agreement of which the object or consideration is unlawful is void."

31. The transactions covered by Section 23 are the transactions where the consideration or object of such transaction is forbidden by law or the transaction is of such a nature that if

permitted would defeat the provisions of any law or the transaction is fraudulent or the transaction involves or implies injury to the person or property of another or where the court regards it immoral or opposed to public policy. Whether particular transaction is contrary to a public policy would ordinarily depend upon the nature of transaction. Where experienced businessmen are involved in a commercial contract and the parties are not of unequal bargaining power, the agreed terms must ordinarily be respected as the parties may be taken to have had regard to the matters known to them. The sellers and the buyers in the present case are business persons having no unequal bargaining powers. They agreed on all terms of the contract being in conformity with the international trade and commerce. Having regard to the subject matter of the contract, the clause for reimbursement or repayment in the circumstances provided therein is neither unreasonable nor unjust; far from being extravagant or unconscionable. It is the precise sum which the sellers are required to reimburse to the buyers, which they had received for the goods, in case of the non-arrival of the goods within the prescribed time. More so, the fact of the matter is that goods never arrived at the port of discharge. The Arbitral Tribunal has only awarded reimbursement of half the price paid by the buyers to the sellers and, therefore, the

award cannot be held to be unjust, unreasonable or unconscionable or contrary to the public policy of India.

32. Mr. Krishnan Venugopal, learned senior counsel would submit that the goods were insured and the buyers were made beneficiaries in the insurance policy and, therefore, they have right to claim loss for goods from the insurance company and not the sellers. Moreover, the right to claim under insurance policy is not subrogated in favour of the buyers. The argument is noted to be rejected having no merit at all for the reasons already indicated above.

33. In view of the above there is no merit in the appeal and it is dismissed accordingly. Since the buyers (respondent) have not chosen to appear, there shall be no order as to costs.

……J.
(R.M. Lodha)

…….. J.
(Jagdish Singh Khehar)

NEW DELHI.
OCTOBER 12, 2011.