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Contract of Indemnity in India: Consideration for Premature Damages A Study on, Gajanan Moreshwar Parelkar v. Moreshwar Madan Mantri: (1942) 44 Bom LR 703

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Abstract

Legal provisions related to indemnity and discharge of liability by indemnifier are yet not exhaustive, though several cases have been adjudicated but a redefinition of the said sections of the Act seems necessary. Most of the landmark decisions in this context happen to be with due consideration to the prevalent legal practices worldwide. The English law and the amendments made therein through equitable principles stand as landmarks while discussing the Act in equitable terms.

Section 124 of The Indian Contract Act, 1872 defines the Contract of Indemnity where the Indemnifier promises the Indemnified to safeguard him against any indemnified losses caused to him by the conduct of Indemnifier himself or any other person. While Section 125 states the rights of the indemnified (promisee) to recover from the indemnifier (promisor) all the damages, the costs borne therein and the sums paid against the indemnified contract which he may be compelled to pay in any suit in respect of any matter to which the promise to indemnify applies.

Both the above sections all or any of the facts not intimately relating to those, where, the actual loss is not yet borne by the indemnity holder or is not yet imposed legally over him, the claim of indemnity holder is unfit or premature. The circumstances under which, the promise of indemnity is made, the nature of the suit, whether claims are made to undertake the responsibility owed to others or to release the indemnified after discharge of possession, sale deed, transfer through local self government etc cannot be exhaustively covered under this part of the Act.

This article with a case comment examines the relevant considerations leading to trends of judgements over a period of time and yet points the inadequacies yet to be addressed.

Keywords: Indemnity, Damages, Premature, Law of Contract, Court of Equity.

Introduction

The judgement given by the Bombay High Court on April 1, 1942 in the case of Gajanan Moreshwar Parelkar vs Moreshwar Madan Mantri[1] is a considered judgement where the provision of the Section 124[2] and 125[3] of the Indian Contract Act, 1872 falls short of the requirements of the case and that the defense lawyer had quoted two judgements of which one was of Shankar Nimbaji v. Laxman Supdu[4] adjudged depending on the facts and findings therein; thus applying Section 124 though not as it is. In the other case of Chand Bibi v Santosh Kumar Pal[5] again the provision of Section 124 and 125 along with Section 68(2)[6] Transfer of Property Act, 1882, taken together needed the consideration of common English law and its ammendment through equitable principles with regard to time. The consideration of the case of Osman Jamal & Sons. Ltd. V. Gopal Purshottam[7] was used by Justice Chagla to justify the extensive purview of the indemnification, which was not possible to be included solely in section 124 and 125 of the Indian Contract Act, 1872.

Objective

To do the factual and legal analysis of the case, in the view of legal provisions and relevant decisions, taken into consideration and to make necessary comments on the case decision.

Aims

1. To study the provisions of contractual law on indemnity. (Sec. 124 and 125)
2. To do the legal analysis of the case and look into the facts of the case.
3. To assess the sufficiency/insufficiency of the legal provisions in this case.
4. To read and understand the relevant decisions taken into consideration.
5. To understand the provisions of Common English Law on Indemnity.
6. To understand the views of Court of Equity in present context.

Facts and Arguments

In this case the plaintiff had procured and taken possession of a plot from Bombay Municipal Corporation on lease of 999 years in 1934 but, since he did not make use of it, defendant entered into play and on defendant's request the possession was handed over to him. He erected building over the land thus rendering the plaintiff to mortgage the land twice for rupees 5 thousand each time to the building material supplier. Finally on the request of defendant and agreeing of plaintiff the lease of the plot was also transferred in his name. The defendant never paid to material supplier except some of the interest over principle amount and a few lease installments to the municipal corporations. After passage of more than one and half year ahead of the deadline the plaintiff was embarrassed and demanded the release deed against the mortgage from building material supplier or /else deposit of mortgage amount with the court to ensure the repayment.

Regarding the provision of Section 124, it has been stated that, it defines the contract of indemnity as the contract by which one party promises to safeguard the other from loss caused to him by the conduct of the promisor himself or by the conduct of any other person.[8]

The argument given by the defense lawyer was that the promisor promises to save the promisee from the loss caused to him and not the loss which may be caused to him.

Regarding Section 125 it has been stated that all that the promisee is entitled to recover from the promisor or the damages which he may be compelled to pay in any suit in respect of any matter to which to promise to indemnify applies.[9]

The defence lawyer has contended that until a mortgagee files the suit against plaintiff and obtains a judgement which the plaintiff is compelled to satisfy, the plaintiff is not entitled to sue the defendant.

The issues raised in the case were:

1. Whether the plaint discloses any cause of action? (since plaintiff has neither paid off the dues nor has been compelled to do so by some legal movement, suit or decision).
2. Whether the suit was premature?

Hon'ble Justice Chagla, on the basis of cases cited by defense lawyer disagreed to the prematurity of the suit with the following comments:

He also opined the inadequateness of Sections 124 and 125 of the Indian Contract Act, 1872 in such cases. Indian Contract Act is both amending and consolidating Act and is not exhaustive of the law of contracts to be applied in the courts of India.

> *"If the whole law of indemnity was embodied in Sections 124 and 125 of the Indian Contract Act, there would be considerable force in the contention of Mr. Tendolkar ; but that is obviously not so. The Indian Contract Act is both an amending and a consolidating Act, and it is not exhaustive of the law of contract to be applied by the Courts in India. Section 124 deals only with one particular kind of indemnity which arises from a promise made by the indemnifier to save the indemnified from the loss caused to him by the conduct of the indemnifier himself or by the conduct of any other person, but does not deal with those classes of cases where the indemnity arises from. loss caused by events or accidents which do not or may not depend upon the conduct of the indemnifier or any other person, or by reason of liability incurred by something done by the indemnified at the request of the indemnifier.*[10]
>
> *In the present suit the indemnity arises because the plaintiff has become liable owing to something which he has done at the request of the defendant and therefore, in my opinion, Section 124 does not apply at all to the facts of this case. Further, Section 125, as the marginal note indicates, only deals with the rights of the indemnity-holder in the event of his being sued. Section 125 is by no means exhaustive of the rights of the indemnity-holder as I shall presently point out. The indemnity-holder has other rights besides those mentioned in Section 125."*[11]

Regarding this case Shankar Nimbaji v. Laxman Supdu[12] the facts of that case were that one Supdu used to deposit monies with defendant No. 2. After the death of Supdu, defendant No. 2 withdrew Rs. 5,000 from Supdu's khata and lent them to defendant No. 1 on a mortgage bond in his own favour. The plaintiffs, who were the sons of Supdu, protested against this and after some correspondence, defendant No. 2 passed a promissory note for Rs. 5,000 in favour of the plaintiffs. The plaintiffs then filed a suit to recover Rs. 5,000 and interest from defendant No. 1 by sale of the mortgaged property and in case of deficit prayed for a decree against the estate of defendant No. 2 which was in the hands of his sons, defendant No. 2 having died during the pendency of the suit. These facts therein led to the

judgement that the plaintiffs could not sue the defendants in anticipation that the proceeds realized by the sale of the mortgaged property would be insufficient and there would be some deficit left. The court construed the promissory note as an indemnity. The court also provided the plaintiffs to opt for repudiation of the mortgage wholly and recover the whole amount from defendant no. 2 but the plaintiffs opted for the recovery from the mortgaged property. Thus there being no actual clue to the apprehension that the recovery from the sale o mortgaged property shall be insufficient the said decree could not be awarded.

Comments of the learned Judge in the given judgement were very clear

> *"if one examines the facts of that case, the decision there did not require the enunciation of the law in these very extensive terms, and I am not prepared to extend the principle of that case beyond the facts proved there and for the decision of which it was necessary".*[13]
>
> *"I am not prepared to read this judgment to mean that in no case can an indemnity-holder maintain an action against an indemnifier unless he has suffered actual loss".*[14]

The second case cited by the defense lawyer was that of Chand Bibi v. Santoshkumar[15] the plaintiffs sold an already mortgaged property along with some other property and the amount required to be paid for release of mortgage was Rs. 2,700. However in the deed the plaintiffs were indemnified by the purchaser (Defendant's father) who had covenanted to pay off the mortgage amount and release the purchased property and the other property mortgaged along with and the liability of the plaintiffs by the mortgage deed.

Since the defendant's father did not pay for the mortgage amount, the suit was filed. The Learned Judge Lort William adjudged the case to be premature since the plaintiffs had not paid or were compelled to pay by a legal procedure, the indemnified amount.

In the view of Justice Chagla, this was not at all a Considered Case and no authorities being cited therein, the learned Judge Lort Williams had also overlooked his own judgement in Osman Jamal & Sons, Ltd. v. Gopal Purshattam[16]. In this case the plaintiff company were agents of the defendants who, on the indemnification by plaintiff company made a purchase which the defendant did not materialize. Thus the third party had to sale the said Hessian at a loss. The loss was actually incurred by the third party and the plaintiff party was under compulsion to pay the damages. Justice Lord Williams had negative the contention of not maintaining the suit since the plaintiffs had not actually had to pay and passed a decree in favour of plaintiff company. It was established that the right of indemnity did not arise from contract but from a trust

Thus Justice Chagla[17] stated that all English Authorities were considered in Osman Jamal Case[18]. He realized that :

> *"an indemnity might be worth very little indeed if the indemnified could not enforce his indemnity till he had actually paid the loss."*

One actually has to wait till a judgment gets pronounced, and it was only after satisfying the judgment, that one could sue on his indemnity. Under certain circumstances, this might throw an intolerable burden upon the indemnity-holder. He might not be in a position to satisfy the judgment and yet he could not avail himself of his indemnity till he had done so.[19]
Court of equity has mitigated the rigour of the common law holding that, if his liability had become absolute then he was entitled either to get the indemnifier to pay off the claim or to pay into Court sufficient money which would constitute a fund for paying off the claim whenever it was made.[20]

The Provisions in Present Context

In Indian context, Sections 124 and 125 of the Indian Contract Act not being exhaustive of the law of indemnity and that the Courts here would apply the same equitable principles that the Courts in England do.[21] Therefore*, if the indemnified has incurred a liability and that liability is absolute, he is entitled to call upon the indemnifier to save him from that liability and to pay it off.*[22]

Further Justice Chagla[23] has elaborated

> *"I have already held that Sections 124 and 125 of the Indian Contract Act are not exhaustive of the law of indemnity and that the Courts here would apply the same equitable principles that the Courts in England do. Therefore, if the indemnified has incurred a liability and that liability is absolute, he is entitled to call upon the indemnifier to save him from that liability and to pay it off."*[24]
>
> *And that under both the mortgage and the further charge there is a personal covenant by the plaintiff to pay the amount due, and it would be open to the mortgagee to sue the plaintiff on the personal covenant reserving his rights under the security. Therefore, the liability of the plaintiff under the personal covenant is absolute and unconditional, and he would have no answer to a suit filed by the mortgagee under that covenant also that If the plaintiff is sufficiently substantial--and I am told he is--the mortgagee may content himself with obtaining a personal decree against him and give up his security, I, therefore, hold that the plaintiff is entitled to be indemnified by the defendant against all liability under the mortgage and the deed of further charge.*[25]

Hence the case was settled in favour of plaintiff with an order to defendant to procure a release deed for the plaintiff rendering him relieved of mortgage and all the related liability.

Decisions in Various Circumstances

The fact that, as per previously prevailing English Common Law, the recovery of money(s) actually paid and incurred by the indemnified, from the indemnifier has been averred later by the Court of Equity and equitable principles stating that "if it be held that payment is a condition precedent to recovery, the contract may be of little value to the person to be indemnified, who may be unable to meet the claim in the first instance."[26]

That if, an absolute liability has been incurred by the promise and that the contract of indemnity covers such liability the indemnity holder (promisee) could sue the indemnifier (promisor) for specific performance of contract of indemnity even before the damage has been incurred by him. This has been held in Khetrapal v. Madhukar Pictures[27]

It was similarly held in the case of Kumar Nath Bhuttachargee v Nobo Kumar[28] when a person contracts to indemnify another in respect of any liability which the latter may have undertaken on his behalf such other person may compel the contracting party, before actual damage is done, to place him in a position to meet the liability that may hereafter be cast upon him.

In the case Rutnessur Biswas v.Hurrish Chunder[29] it was held that Plaintiff was entitled to recover the sum due to his superior landlord as damages for breach of the contract and that the amount of such damages ought not to be taken as nominal, but should be assessed on the footing of the sum for which A might become liable to the landlord. These cases, therefore, show that in a certain class of cases, even before an injury is done or damage takes place, the plaintiff may bring an action in order for the person making the covenant and may place him in a position to meet the liability he has undertaken on the latter's behalf.[30]

While in the case of Ramalingathudayar v. Unnamalai Achi[31] The question was whether the suit was premature. Since at the date of suit the defendant had committed a breach of his contract and the plaintiff had suffered damage by having her property attached. There was therefore sufficient to give her a cause of action.

In case of an imminent injury Profulla Kumar Basu v. Gopee[32] it was held even though the Official Liquidator had actually not paid the sum to the vendor, he can recover amount from the defendant.

Buckley L.J.[33] has stated "Indemnity require that the party to be indemnified shall never be called upon to pay" considering the verge of Court of Equity given in 1911, in Re Richardson Ex parte the Governors of St. Thomas's Hospital reconsidered the English Common Law and thus, through modification, indemnity before payment by the indemnity holder was made the norm.[34]

In 1914, in the case of In re Law Gurantee Trust and Accidental Society, Limited. Liverpool Mortgage Insurance Company's Case[35] case, it was stated that, 'to indemnify does not mean merely to reimburse with respect to the money paid but to save from loss with respect to liability for which indemnity has been given'

In certain cases, however, looking to the facts and findings, the decisions of Lahore, Nagpur and Bombay respectively Sham Sundar v. Chandu Lal and Ors.[36], Ranganath v. Pachusao[37], Shankar Nimbaji Shintre and Ors. V. Laxman Supdu[38] went in favour of the indemnifier party as it was held that the suit remains premature till the losses are actually incurred by the plaintiff(s).

In Sham Sundar's[39] case on July 15, 1935 - The Judge, Din Mohammed was pleased to say that, "The whole case hinges on the interpretation to be placed on the words "may be compelled to pay" as used in Section 125, Contract Act. If the words mean "may have paid" or "may have been made to pay" under compulsion, this petition must succeed; but if those words merely mean "may be liable to pay" the petition must fail."

Thus deciding "A man cannot be said to have been damnified so long as he is not deprived of anything. A mere remote chance of being deprived will not entitle him to realise damages from his promisor or indemnifier. This being so, the plaintiff's previous suit was rightly dismissed as premature."

In Shankar Nimbaji Shintre's[40] case – The Judges N J Wadia and N S Lokur, since it was an appeal made by the defendants of the original case, first of all revisited the sections 126, 128 of Indian Contract Act 1872 and Article 83 Contract of indemnity, and concluded with the facts of the case that defendant no.2 was not the guarantor or Surety. Thus, it was considered Indemnity, that too under section 124 of Indian Contract Act 1872. Thus the decision went in favour of the provision in section 124 rendering the suit to be premature.

Deliberation

All the above views expressed by Learned Judges in variety of circumstances leads us to the understanding that u/s 124 and 125 of Indian Contract act 1972 the case of the one who is indemnified becomes a futile exercise even if the liability incurred by the promisee becomes absolute, or the person, though fully liable to incur the damages is not yet compelled through some legal movement to repay.

The results could still worsen if the indemnified is not financially capable for repayment or the attachment happens to his personal property.

In a few cases however and may be earlier as a practice the these sections must have been being applied in strict and absolute sense since they also favour the the version of English Common Law.[41]

The English Common Law hence fell deficient to intervene in and provide justice in all other cases where the situations were different.[42]

The intervention of Court of Equity has provided a great relief in all such places where the prematurity of the plaint happened to be quoted on the basis of prevailing law and legal provision in section 124 and125 of Indian Contract Act 1872.

In the case under study Gajanand Moreshwar v Moreshwar Madan Mantri[43] settled by Justice Chagla J dates the occurrences, back to 1934. Here, the defense lawyer preliminarily quoted the sections 124 and125 and two cases one settled in the same court previously.

The Learned Judge stated the case to be out of the scope of sections 124 and 125 and found one of the referred cases being decided solely over the findings since the findings could suffice the requirements therein as per the prevalent legal provisions and denoted the other case being not considered in all aspects. Justice Chagla quoted the case of Osman Jamal & Sons. Ltd. V. Gopal Purushottam[44] decided by the same court over several considerations, previously. Thus he took the consideration of English Common Law and the intervention of Court of Equity thus, as in the cases quoted in analysis Re Richardson Ex parte the Governors of St. Thomas's Hospital and In re Law Gurantee Trust and Accidental Society, Limited. Liverpool Mortgage Insurance Company's Case[45] the new understanding of Indemnity applicable in present context has been taken for the considered decision.

In certain other conditions or facts, terms like 'exact' and 'compensated loss' have been used to denote the losses incurred or damages paid and to ascertain the indemnified amounts. that are not reasonably foreseeable.[46]

While in other cases, the promisee or the one indemnified received the benefits of Losses.

'Mitigation' or the 'interest over the payables' or the 'losses to be incurred, which happens to increase per annum' have also been considered in the relief as against the exact amount of payable, once decided.[47] Thus the concept of 'Enforcement of indemnity before losses' laid down in the given case context, has opened the doors of justice for the indemnified.[48]

Looking to the Insurance sector, generally, a contract of insurance is not treated as a contract of indemnity in India. The cases of life insurance are not considered to be those pertaining to indemnification but it is only a sum of money to be paid by insurance company to the beneficiary.[49]

In case of General Insurance, marine insurance, fire insurance or motor insurance are deemed to be contracts of indemnity. It may be either the payment of damages in full if there be a loss within the insured limits, or the payment of the assured amount if it happens to be a part and parcel of the payment due.[50] Hence the concept of indemnity insurance is justified, where to insurance company (indemnifier or promiser) has to pay the sum to the concerned party in place of the insured person (Indemnified or promisee) and free the indemnified (insured) from the liability thus incurred.[51] Thus comes the Professional Indemnity Insurance which is perfectly behind the statement in case of Re Richardson Ex parte the Governors of St. Thomas's Hospital[52] that "A Contract of indemnity would serve little purpose if the indemnity holder was made liable in the first instance. What if he is unable to meet the claim in the first instance?"[53]

The terms of indemnity contract define the rights of indemnity holder besides the only possibility of section 125 coming into play in specific situation when the liability over the promisee becomes absolute through a legal suit or order that is if the indemnified has paid or is forced to pay the damages thus the indemnity holder is entitled to recover the the damages that he may have been compelled to pay in any suit in respect of any matter to which the promise of the indemnifier applies.[54] This exemplifies as: if A contracts to indemnify B against the consequences of any proceedings which C may take against B in respect of a particular transaction. If C does institute legal proceeding against B in that matter and B pays damages to C, A will be liable to make good all the damages B had to pay in the case. This will include all the costs of suits that he may have had to pay to the third party provided he does not act in contravention of the directions of the promisor or the promisor had authorized him legally to contest such a suit.

Conclusion

Contract of Indemnity is the type of contract where one person promisor agrees to make good for all the losses and costs incurred or to be incurred by the promisee in broad terms through the execution of such contract. Though quite many clauses are made in the Indian Contract Act 1872 related to indemnity, sections 124 and 125 have their significance in legal suits when the indemnified turns to the indemnifier demanding the liability to be paid off.[55]

Since section 124 applies when the promisee has to bear the losses due to some act of promisor or a third person and section 125 considers the case mature for legal suit only when promisee has actually paid for the losses, both of them apply pretty elaborately in the case of indemnification. But they fall short and may even pronounce injustice in the cases where the promisee is made fully liable after the deadlines of payment have already been crossed but the liability cannot be fixed over the promisor till the dues/ damages are actually incurred. Similarly when the payment to the concerned party is not made in the time frame by the indemnifier, embarrassment of the indemnified is obvious but any legal suit moved against indemnifier appears to be premature without consideration that what will happen if the promisee is not solvent or capable to pay at that time ?

In all such cases consideration of similar cases in various courts becomes necessary to deliver justice to promisee who files the case as a plaintiff. The decisions in the country and those made abroad through application of Common English Law were of the same view till in 1914 Court of Equity was of the opinion that "A Contract of indemnity would serve little purpose if the indemnity holder was made liable in the first instance".

Further this proposition of applying equitable principles became universally applicable in the present context but not all decisions were going properly considered rather several judgments depended on the facts of the case, the circumstantial evidence and plainly the application of sections 124 and 125 of the act.

The judgement of Justice Chagla J in the case of Gajanan Moreshwar Parelkar v Moreshwar Madan Mantri[56] realized the problem, thus he, besides commenting on the defence lawyer's quoted cases opined that sections 124 and 125 do not cover all the cases and hence for deciding the cases out of the purview of these sections, consideration to the

Common English Law and The Equitable Principles is absolutely necessary.

This finally defied the general understanding of actually bearing of the losses by the promisee first.[57] The promisor can be sued and made liable to the payments when they become due. Here the opinion of Justice Beckley J., saying that the indemnifier should pay for the liabilities under indemnity contract and rather the indemnifier should not be called upon to pay.

This judgement has brought a great relief in such cases and an assurance to the indemnified, may the indemnifier be a person or party or it may be a general insurance or an indemnity insurance company.

The Judgement pertains to the details of the case as well as it being a properly considered one carries its own significance.

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Footnotes

1. *(1942) 44 Bom LR 703*
2. *Contract of Indemnity states that - A contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person, is called a "contract of indemnity.*
3. *Rights of indemnity-holder when sued.- The promisee in a contract of indemnity, acting within the scope of his authority, is entitled to recover from the promisor -*

(1) *all damages which he may be compelled to pay in any suit in respect of any matter to which the promise to indemnify applies;*

(2) *all costs which he may be compelled to pay in any such suit if, in bringing or defending it, he did not contravene the orders of the promisor, and acted as it would have been prudent for him to act in the absence of any contract of indemnity, or if the promisor authorized him to bring or defend the suit;*

(3) *all sums which he may have paid under the terms of any compromise of any such suit, if the compromise was not contrary to the orders of the promisor, and was one which it would have been prudent for the promisee to make in the absence of any contract of indemnity, or if the promisor authorized him to compromise the suit.*

4. *(1939) 42 Bom. L.R. 175*
5. *(1933) I.L.R. 60 Cal. 761*
6. *Where a suit is brought under clause (a) or clause (b) of sub-section (1), the Court may, at its discretion, stay the suit and all proceedings therein, notwithstanding any contract to the contrary, until the mortgagee has exhausted all his available remedies against the mortgaged property or what remains of it, unless the mortgagee abandons his security and, if necessary, re-transfers the mortgaged property.*
7. *AIR 1929 Cal 208.*
8. *Dutt on Contract, 11th Ed. 2013, H.K. Saharay, Eastern Law House.*
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23. *Supra Note 1*
24. *Supra Note 1*
25. *Supra Note 1*
26. *As observed by, Kennedy L.J. in Liverpool Company's case (1914), 2 ch. 617.*
27. *[1] 57 Bom LR 1122 (1126) : AIR 1956 Bom. 106.*
28. *[1] 26 Cal 241*
29. *(1885) ILR 11 Cal 221.*
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36. *AIR 1935 Lah. 974: 159 Ind. Cas. 853*
37. *AIR 1935 Nag. 147*
38. *AIR 1940 Bom. 161: 1940 (42) Bom. L.R. 175*
39. *Supra Note 36.*
40. *Supra Note. 4*
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43. *Supra Note 1.*
44. *Supra Note 7.*
45. *[1914] 2 Ch. 617*
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57. *Law of Contract II - S.K. Kapoor, Ninth Ed., 2002, Central Law Agency.*