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Critical Analysis of Law of Damages **under the Indian Contract Act, 1872**

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ABSTRACT

There are chances that a contract will be broken when it is signed or when parties enter into one. The parties who have been the victims of the unlawful conduct or violation shall be provided such remedies in this case, in order to defend the preferences or goals of the contractual parties or parties entering the contract and to provide them with justice. Damages are one of the remedies offered for contract infringement or breach. In its most basic sense, it refers to any type of monetary loss or compensation awarded once in the form of a lump sum of money. This article aims to clarify the definition, nature, and purpose of damages as a remedy for contract violation. In order to determine damages, it is necessary to consider the plaintiff's position in the event that the contract had been properly carried out. In this article, we will cover some of the different types of monetary damages.

Keywords- *Damages, Remedies, Breach, Compensation, Violation, Contract.*

INTRODUCTION:

The agreement is the result of two parties coming to a mutual understanding and reaching a consensus. Contracts are agreements that are legally binding and enforceable. A proposal from one party must be accepted by the other in order for there to be a contract. A legally enforceable agreement between two or more parties is known as a contract. A contract is essentially a commitment made by one party to another to perform an act or refrain from performing one in exchange for payment from the other party.

In exchange for consideration, parties enter into a contract and promise to do or refrain from doing

certain things. This promise made by the parties, which is the subject of the contract, is legally binding on both parties, and they are obligated to fulfill their respective parts of the promises. A breach occurs when either party fails to do something they promised to do or does something that is prohibited by the contract.

The Law of Damages in India is codified under Section- 73 of the Indian Contract Act, of 1872. The term "Damages" is not defined under the Indian Contract Act of 1872. So, what does it mean to sustain damages? The value of any injury or loss caused by the person in breach of contract is referred to as damages.

In order to be eligible for compensation, the plaintiff must first demonstrate that the harm they experienced was a direct result of the violation. In every case of breach of contract, the affected individual does not have to provide evidence of actual damage or harm sustained before requesting a ruling, and the court is able to award reasonable compensation for the breach of contract even without proof of any actual harm. In reality, the breach of any contract will always provide grounds for a claim for damages without proof of any damage. The sum of damages that can be recovered will depend on the amount of loss caused by the defendant's act.

WHAT IS A CONTRACT?

The term “contract” generally refers to a legally binding enforceable agreement signed between two parties that should include terms that courts have the authority and obligation to enforce.

According to Indian Contract Act, 1872 Section 2(h), A contract is an agreement enforceable by law.

An agreement becomes a “contract” only when it is intended to meet its legal obligation.

BREACH OF CONTRACT:

Any party who refuses or fails to carry out their obligation under a contract constitutes a breach of that agreement. A legal claim for breach of contract arises when one or more parties fail to uphold the terms of a contract by making it difficult for them to fulfill their obligations. Section 37 of the Indian Contract Act, 1872 provides that the parties to the contract are under obligation to perform or offer to perform, their respective promises under the contract, unless such performance

is dispensed with or excused under the provisions of the Indian Contract Act or of any other law¹.

According to *Section 39*, where the party has refused to perform or disabled himself from performing, his promise in its entirety, the other party may put an end to the contract, unless that other party has expressly or impliedly signified its consent for the continuance of the contract. If the other party chooses to put an end to the contract, the contract is said to be broken and amounts to a breach of contract by the party not performing or refusing to perform its promise under the contract. This is called Repudiation. Repudiation can happen when either party makes it hard for the other to fulfill their obligations under the contract or refuses to carry out their respective obligations in a way that indicates a desire to breach such obligations.

DAMAGES:

If a contract is broken, the affected party has the right to sue for damages. If there is a breach of contract by any one of the parties of the contract then the party can be sued for damages. The plaintiff is entitled to compensation for any losses that occur, and the offending party is responsible for providing the funds to the injured party. A 'remedy' is a right that the aggrieved party acquires when the other party violates the terms of the contract². The Indian Contract Act of 1872 also offers a variety of remedies to the party whose rights have been violated. 'Damages' is one such cure and is also the one that is most frequently used. Damages refer to monetary restitution to the amount of the victim's loss or damage.

Illustration: A contracts to repair B's house in a certain manner, and receive payment in advance. A fixes the house, although not in accordance with the agreement. B is qualified to receive compensation from A for the price of doing the agreed-upon repairs.

THE RULE IN “*Hadley v Baxendale*”

In the well-known case of *Hadley vs. Baxendale*³, a noble attempt was made as early as 1854 to

¹ A Brief Overview on Breach of Contract, available at: <https://blog.iplayers.in/a-brief-overview-on-breach-of-contract> (Last Modified January 16, 2020)

² Damages under the Indian Contract Act 1872, available at: <https://vidhinama.com/damages-under-the-indian-contract-act-1872/#DAMAGES> (Last Modified December 19, 2022)

³ [EWHC J70, (1854) 156 ER 145, 9 ExCh 341, (1854) 23 LJ Ex 179, 18 Jur 358, All ER Rep 461]

solve the problem by establishing certain rules.

The plaintiffs ran a large miller business. Their mill was shut down due to a crankshaft breakage. The defendants, a carrier firm, were hired to transport the shaft to the manufacturers as a pattern for a new one. The plaintiff's servant informed the defendants that the mill had been shut down and that the shaft needed to be delivered immediately. However, the defendants delayed delivery due to negligence, and as a result, the plaintiffs did not receive the new shaft for several days longer than they would have otherwise. The suit was brought for the loss of profits that would have been made during the period of delay.

ALDERSON B laid down the following rule⁴:

“Now we think the proper rule in such a case as the present is this: 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.”

CONSEQUENCES OF BREACH OF CONTRACT:

For compensation to be payable, two factors must be considered⁵:

- (a) the loss or damage must have occurred as a natural result of the breach, or
- (b) it must have been something the parties could have reasonably expected to occur as a result of a breach of the contract.

(A) THE LOSS OR DAMAGE MUST HAVE OCCURRED AS A NATURAL RESULT OF THE BREACH-

⁴ Avtar Singh, Avtar Singh's Law of Contract & Specific Relief 466 (Eastern Book Company, Lucknow, 13th edn., 2022)

⁵ A Brief Overview on Breach of Contract, available at: <https://blog.iplayers.in/a-brief-overview-on-breach-of-contract> (Last Modified January 16, 2020)

The Indian Contract Act, of 1872 uses the words *loss or damage* under section 73:

(i) COMPENSATION FOR LOSS OR DAMAGE CAUSED BY BREACH OF CONTRACT:

When a contract is violated, the party who was harmed by the breach is entitled to compensation from the party that committed the breach for any loss or damage caused to him, which naturally arose in the natural 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.

There will be no compensation for any remote or indirect loss or damage caused by the breach.

(ii) COMPENSATION IN REGARD TO FAILURE TO DISCHARGE OBLIGATION WHICH RESEMBLES THOSE CREATED BY THE CONTRACT

When a contract is broken, the party that suffered loss or damage has a right to reimbursement from the party who broke the agreement.

(iii) COMPENSATION FOR LOSS OR DAMAGE WHICH NATURALLY AROSE IN THE USUAL COURSE OF THINGS FROM SUCH BREACH

Compensations to be recovered for loss or damage which the parties knew or which would have naturally arisen in the usual course, to be likely to result from the breach of it.

CASE- Pannalal Jankidas v Mohanlal⁶, the Supreme Court observed "that the party in breach must make compensation in respect of the direct consequences flowing from the breach and not in respect of loss or damage indirectly or remotely caused"

(B) IT MUST HAVE BEEN SOMETHING THE PARTIES COULD HAVE REASONABLY EXPECTED TO OCCUR AS A RESULT OF A BREACH OF THE CONTRACT

The Non-Defaulting Party bears the burden of proof under this section. However, remote and indirect losses suffered by the Non-Defaulting Party as a result of the Defaulting Party's breach of the terms of the contract have been excluded from the scope of this section. As a result, the loss must be a genuine loss or actual damage, rather than merely probable or possible.

⁶ [1951 AIR 144 1950 SCR 979]

(iv) DEALS WITH REMOTE AND INDIRECT LOSS OR DAMAGE

It states that no compensation is payable for remote and indirect loss or damage arising on account of a breach of contract. The indirect loss cannot be said to arise in the usual course of things. Only when it is expressly stated to the other party or foreseen by the contract that breach of the terms of the agreement will cause some indirect loss or loss of profit to the party, can the aggrieved party make a claim for compensation for indirect loss or loss of profit. The legal standard used to determine whether kind of harm brought on by a breach of contract may be compensated by the award of damages is known as the remoteness of damage.

(v) DEALS WITH BREACH OF RESEMBLING CONTRACT

Even if there may not be a contract to pay compensation, it grants a party a statutory right to receive compensation from a person that has incurred a statutory obligation to do so in the event of default. The party in default is under obligation to pay compensation to the injured party as if there was a contract and has broken such a contract.

(vi) DEALS WITH: MITIGATION OF LOSSES

It explains that the means which existed of remedying the inconvenience caused by the non-performance of the contract must be considered while calculating the damage or loss for breach of the contract⁷.

CASE-Brahmdeo Narain Singh v Members of the Notified Area Committee⁸, it was held that “When it is not possible to calculate accurately or in a reasonable manner the actual amount of loss incurred or when the plaintiff has not been able to proof loss suffered, he will be, all the same, entitled to recover nominal damages for a breach of contract”.

The first rule is "objective," as it bases liability on a reasonable man's foresight of the loss that will inevitably result from the breach of the contract. The second rule is "subjective," as it states that the extent of liability is determined by the parties' knowledge of the likely outcome of the

⁷ A Brief Overview on Breach of Contract, available at: <https://blog.iplayers.in/a-brief-overview-on-breach-of-contract> (Last Modified January 16, 2020)

⁸ AIR 1965 Patna 179

DAMAGE CAN BE RECOVERED BY:

Only those parties who have performed or are willing to perform their part of the contract's obligations may seek damages for breach of contract. Sections 73 and 74 are intended to benefit the party willing to perform the contract, not the defaulting party. Loss caused by a party's failure to perform his duties is not recoverable from the other party. A party to a contract cannot be in a better position because of his own default than if he had fulfilled his obligations. Damages cannot be claimed by anyone who is not a party to the contract.

CAN THIRD-PARTY DAMAGE OR LOSS BE RECOVERED?

The party claiming the damage does not have to suffer any loss as a result of the breach of contract. When the contract allows for it. When it is contemplated by the contract that a breach by any of the contracting parties is likely to cause loss to an identified or identifiable stranger to the contract, rather than to the contracting party, a party not in default can claim damages for the loss caused to an identified or identifiable stranger to the contract. Thus, the party may recover substantial damages even if it does not personally bear the cost of correcting the defects or suffers the decline in value; provided, however, that this was intended or was within the parties' contemplation; and if such intention or contemplation

CASE- In the case of *Alfred McAlpine Construction (AMC) Ltd v Panatown Ltd [2001]*⁹, the appeal by AMC was allowed. In light of the fact that the employer was not a party to the original contract, it was determined that they lacked standing to sue for delays and faults, particularly in cases where the terms of the duty of care deed have already been put to use. The employer could only seek the nominal damages set forth in the duty of care deed since it had not experienced any financial loss.

CONDITIONS TO CLAIM DAMAGES:

Every claim for damages raises two issues. The first is the remoteness of the damage problem,

⁹ [2001] 1 AC 518; [2000] 3 WLR 946; [2000] 4 All ER 97; [2000] CLC 1604; [2000] BLR 331; [2000] EG 102 (CS); (2000) 150 NLJ 1299

and the second is the measurement of damages.

i. The remoteness of Damages:

In the case of a contract, a much higher degree of foreseeability is required, i.e., a serious possibility or real damages that the loss will occur. Damages are hence more strictly limited in contracts than in torts as a result.

The test for determining whether the claimed damages are too remote is whether the damage is such that the parties must have considered it as a possible result of the breach. If it is, it cannot be considered too far away. The damage will be calculated based on the natural and probable consequences of the breach. Actual knowledge must be demonstrated. Knowledge is more than just prudence and carelessness.

The defendant is only liable for reasonably foreseeable losses—those that a normally prudent person would have reason to foresee as likely consequences of a future breach if he were contracting in his place with his information.

There must be a limit to liability and beyond that limit, the damage is said to be too remote and, therefore, irrecoverable.

When two parties enter into a contract and one party breaches the contract, the other party is entitled to compensation for the loss or damage caused by the breach in the terms of the contract. Only in such cases, where the loss is the result of a breach of contract, is the person who breached the contract obligated to pay compensation. If the loss is even remotely related to the breach, the party who breached the contract is not obligated to compensate the injured party. This is known as the remoteness of damages. This rule was laid in the case of *Hadley v Baxendale* as we discussed above¹⁰.

ii. The measure of Damages:

Once it is determined that the loss is a direct result of the breach of contract and is not too remote, the amount of compensation to be paid or the assessment of compensation must be determined.

¹⁰ A Brief Overview on Breach of Contract, available at: <https://blog.iplayers.in/a-brief-overview-on-breach-of-contract> (Last Modified January 16, 2020)

So, determining the quantum of damages (i.e., how much damages must be paid to the injured party) is the measure of damages. It can be difficult to assess and determine damages at times, but this does not absolve the party who breached the contract of liability. In the case of a sale contract, the measure of damages is the difference between the contract amount and the market price on the date of the breach. Also, if the breach was on the part of the seller, the buyer can seek damages on the date of the breach but is not required to repurchase the item on that date. Similarly, if the breach was caused by the buyer, he can seek damages on the date of the breach but is not required to resell the goods on that date.

CASE- In *State of Kerala v. K. Bhaskaran*¹¹, the government breached the Works Contract, causing the contractor to lose 10% of his profit. He filed a lawsuit against the government, and it was determined that he was entitled to compensation and the 10% profit that the contractor lost, which is the element for contract estimation.

LIQUIDATED AND UNLIQUIDATED DAMAGES:

‘Liquidated damages’ are those agreed upon by the parties when they signed the contract. Liquidated damages are damages in which the compensation that must be paid to the aggrieved party when a breach occurs is pre-determined and agreed upon by the parties when they enter into an agreement. However, the fixed amount should be reasonably pre-estimated by taking into account the potential damages. It must be genuine¹²

Section 74 talks about Liquidated damages and Penalty¹³,

The parties to the contract may agree at the time of contracting that, in the event of a breach, the party in default must pay a specified sum of money to the other, or that, in the event of breach by one party, any amount paid by him shall be forfeited. If this sum is a genuine pre-estimate of the damage likely to result from the breach, it is referred to as 'liquidated damages'. It may be called a 'penalty' if it is not a genuine pre-estimate of the loss, but rather an amount intended to secure

¹¹ AIR 1985 Ker 49

¹² Damages under the Indian Contract Act 1872, available at: <https://vidhinama.com/damages-under-the-indian-contract-act-1872/#DAMAGES> (Last Modified December 19, 2022)

¹³ Damages under the Indian Contract Act 1872, available at: <https://vidhinama.com/damages-under-the-indian-contract-act-1872/#DAMAGES> (Last Modified December 19, 2022)

ESSENCE OF PENALTY AND LIQUIDATED DAMAGE:

A penalty is a monetary payment made to a non-defaulting party that puts the other party in fear and forces the other party to perform its contractual obligations. The penalty has a deterrent effect.

Liquidated damage is a genuine and reasonable damage estimate. Liquidated damages are defined as the sum that the parties have agreed to pay as damages under the contract, *regardless of the actual damage*¹⁴.

CASE- In Fateh Chand Vs Balkishan Das¹⁵, the Hon'ble Supreme Court held that :- "Section 74 of the Indian Contract Act 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.

'Unliquidated damages' are those that were not pre-determined by the parties when they signed the contract. The amount of compensation to be paid in the event of a breach is not fixed and must be decided or estimated after the breach occurs by assessing it. Section 73 discusses unliquidated damages, which are made available by courts in the event of a breach after assessing the damage or loss caused by the breach.

CASE- The Supreme Court held in the case of ONGC v. Saw Pipes Ltd¹⁶. that, in the case of damages, sections 73 and 74 must be read together and, where there are liquidated damages they must be granted. In cases where the exact amount of damage or loss suffered cannot be determined, a reasonable decision to provide reasonable compensation must be made.

In this case, it has been held with regards to damages and penalty as under:

¹⁴ Understanding 'Damages' and 'Compensation' under Contract Law, available at: <https://lawlex.org/lex-pedia/understanding-damages-and-compensation-under-contract-law/20619> (Last Modified May 24, 2020)

¹⁵ 1963 AIR 1405, 1964 SCR (1) 515

¹⁶ Appeal (civil) 7419 2001 of 518

1. The stipulation providing for damages is by way of penalty, it can grant reasonable Compensation upon proof of damages.
2. Damages must be justified in cases of penalties.
3. Damages are reasonable compensation whereas penalties are not.

Unliquidated Damages are of the following types:

A. **General or ordinary Damages**: These are limited to monetary compensation to place the injured party in the position he would have been in if the contract had been fulfilled. It is the estimated amount of loss suffered. As a result, it only applies to the immediate consequences of contract breach, and the remote consequences are generally ignored¹⁷. In a contract for the sale of goods, for example, the damages payable are the difference between the contract price and the price at which the goods are available on the date of the breach.

B. **Special Damages**: Special damages are those that result from a breach of contract in unusual circumstances that make special loss the likely result of the breach in the normal course of things. The party who violated will be held responsible for the special loss¹⁸.

Illustration: A delivered goods to the Railway Administration to be transported to a location where an exhibition was being held and informed the goods clerk that if the goods did not arrive at the destination on the specified date, he would suffer a special loss. The merchandise arrived late. He had the right to sue for special damages.

Relevant Case Laws:

- I. The Supreme Court held in *Bharathi Knitting Company v. DHI Worldwide Express, Courier Division of Airfreight Ltd*¹⁹. that when a person signs a document containing certain

¹⁷ Avtar Singh, Avtar Singh's Law of Contract & Specific Relief 466 (Eastern Book Company, Lucknow, 13th edn., 2022)

¹⁸ Damages under the Indian Contract Act 1872, available at: <https://vidhinama.com/damages-under-the-indian-contract-act-1872/#DAMAGES> (Last Modified December 19, 2022)

¹⁹ 1996 SCC (4) 704, JT 1996 (6) 254

contractual terms, the parties are normally bound by such contract.

II. The Court recently held in *MI's. Classic Motors Ltd. v. Maruti Udyog Ltd*²⁰. that the parties are bound by the terms of the Contract and that once a party has signed the document, it cannot be claimed that he was unaware of the terms and conditions contained therein.

III. It was determined in the case of *Reliance General Insurance v. Anish Sebastian*²¹ that special damages are superior to general damages. They are not the result of a party's actions, but of some wrongful act. They are primarily concerned with the price outside of the contract.

C. **Exemplary or punitive Damages**: These damages are awarded to punish the defendant and are not usually granted in cases of contract breach. However, in two cases, the court may award such damages²²:

(i) breach of marriage promise; and

(ii) wrongful dishonor of a customer's cheque by the banker.

The number of damages in a breach of promise to marry will be determined by the extent of the party's emotional injury. In the banker's case, the smaller the amount of the cheque dishonored, the greater the damages, because the customer's credit is harmed far more severely if a small amount of a cheque is wrongfully dishonored.

D. **Nominal Damages**: Nominal damages are those that the person who breaches the contract must pay, even if the injured party cannot prove any damage occurred. For example, if a person's legal right is violated, he has the right to seek compensation even if no loss or damage has occurred²³.

E. **Vindictive Damages**: When one party breaches a contract and the other party suffers mental harm, vindictive damages are awarded. It is intended to compensate the aggrieved party

²⁰ 1997 (i) AD (Delhi) 190

²¹ Revision Petition No. 4607 of 2013

²² Avtar Singh, Avtar Singh's Law of Contract & Specific Relief 466 (Eastern Book Company, Lucknow, 13th edn., 2022)

²³ Damages under the Indian Contract Act 1872, available at: <https://vidhinama.com/damages-under-the-indian-contract-act-1872/#DAMAGES> (Last Modified December 19, 2022)

for mental stress or injury suffered as a result of the other party's wrongdoing. When the defendant, in this case, has no intention of compensating the injured party, he is sentenced.

CASE- In *Diesen v. Samson*²⁴, it was decided that compensation for a mental injury can be awarded where the contract itself is for providing enjoyment or pleasure, such as taking photographs at a wedding ceremony.

F. **Substantial Damages**: When a person commits an offense and is found guilty, all authorities affected by the offense must be compensated as substantial damages because the offense is against society. If determining or estimating the societal damage is difficult, the court may order the defendant to pay compensation to the authorities affected by the offense.

CONCLUSION:

The Indian Contract Act 1872 is designed to safeguard the interests of those involved in a contract, from the moment the agreement is made up until the resolution of any issues that may have arisen from it. This act enforces the parties who have entered a contract to remain consistent with the terms they have agreed upon, while also establishing guidelines to provide remedies if an injustice has been done.

Thus, The Indian Contracts Act ensures to provide the fullest extent of remedies for the breach of the contract. This may vary depending on the situation and extent of a breach that has been committed, such as in certain cases particular damages can also be claimed. This is because they are meant to protect the injured party's legal rights and ensure that they are fully compensated for the breach of contract cases and to alleviate the damages suffered.

Despite difficulties in calculating the exact losses incurred by breaking the law, courts will endeavor to provide a respectable payment to the wronged party following an evaluation of the ensuing damage. The purpose of these stipulations and restitutions is to safeguard the person or persons affected from monetary losses, resulting from any violation.

²⁴ (1971) SLT (Sh Ct) 49