1930

Present : **Maartensz A.J. and Jayewardene A.J.**

ABDUL MAJEED *v.* SILVA.

162—*D. C. Colombo*, 26,795.

Liquidated damages—Breach of contract—Sum recoverable as a fine—Pre-estimate of possible damage.

Where the plaintiff entered into a contract with the defendant to make and supply certain roofing sheets by a certain date and in default to pay a fine of Rs. 500, which the defendant was authorized to deduct from the balance sum due to the plaintiff who had received an advance,—

Held, that the sum provided for was liquidated damages and was recoverable as being a genuine pre-estimate of the damage which the defendant might sustain from a breach of the contract.

THE plaintiff sued the defendant to recover a sum of Rs. 610.65, balance due to him for supplying certain goods and roofing sheets. The defendant, while admitting his liability in a sum of Rs. 110,63, claimed to set off a sum of Rs. 500 as damages in terms of an agreement (D1) dated July 20, 1927. By the agreement the plaintiff agreed to supply the roofing sheets by August 20, 1927, and in default to pay a fine of Rs 500, which the defendant was authorized to deduct from the balance due to the plaintiff, who had received an advance. The roofing sheets were supplied in consignments, the last of which was delivered on September 3, 1927. The learned District Judge held that the sum provided for was a penalty and, as the defendant had not proved damages, entered judgment for the plaintiff.

De Zoysa, K.C.(with him *Rajapakse*),for defendant, appellant.—The amount specified may be deemed " liquidated damages " despite the use of the words " fine " and " penalty " in the agreement, if such intention can be gathered from a perusal of the whole instrument. (*Wallis v. Smith* [1] ; *Elphinstone v. Markland Iron and Coal Co.*[2])

[1] (1882) 21 *Ch. D.* 243. [2] (1886) 11 *A. C.* 332.

If the agreement contains several covenants of varying importance and a large sum is made payable upon the breach of any of them irrespective of its importance, or where the sum named is out of proportion to the contract, it is a penalty *in terrorem*. (*Subbramaniam v. Abeywardene* [1]; *Wickremasuriya v. Appuhamy* [2]; *Wijewardene v. Noorbhai.* [3])

It is " liquidated damages " if the sum specified is a genuine pre-estimate by the parties of the loss they contemplated; or where a particular specified act had to be performed and, as the extent of the damage is difficult to estimate exactly, the parties fix upon a certain sum. (*Law v. Local Board of Redditch* [4]; *Elphinstone v. Markland Co.* (*supra*); *Clydebank Engineering Co. v. Castaneda* [5]; *Pless Poll v. Soysa.*[6])

Tisseverasinghe, for plaintiff, respondent.—The words used are " penalty " and " fine ". Defendant himself in his letter refers to it as " the punishment ". The onus, therefore, lies on him to show it is not a " penalty ". He has not disproved the presumption. (10 *Halsbury*, *p.* 329, *section* 605, *rule* (1).)

The Roman-Dutch law does not allow the enforcement of agreements where the sum stipulated is *ingens* or *immanis*. If there is an adequate means of ascertaining the precise damage, only the actual damage suffered (of which here there is no proof) is awarded. (10 *Halsbury*, *p.* 331, *section* 605, *proviso to rule* (6).)

The defendant elected to prove the actual damages sustained by him, and the finding of the Court below is that he had failed. The question whether the amount is a penalty or liquidated damages therefore does not arise.

A comparison of the two contracts, one for damages at Rs. 10 a day and the other for a lump sum of Rs. 800, irrespective of the period of delay, shows that the latter is a penalty.

[1] 21 *N.L.R.* 161.
[2] 6 *C. W. R.* 57.
[3] 28 *N. L. R.* 430.
[4] (1892) 1 *Q.B.* 127.
[5] (1905) *A. C.* 6.
[6] 15 *N. L. R.* 57.

Rajapakse, in reply.—The Roman-Dutch law is in our favour; in any case the English law is applicable in Ceylon [1]. If the sum is held to be " liquidated damages " the Court will not interfere with the actual amount, as it is pactional damage. (*Public Works v. Hill.*[2])

The point of time at which the question of whether there is adequate means of ascertaining the damage is when the agreement is made, not after the breach. The rules are summarized in *Dunlop Tyre Co. v. New Garage, Ltd.*[3]

October 17, 1930. MAARTENSZ A.J.—

The plaintiff brought this action to recover a sum of Rs. 610·63, being the balance amount due to him from the defendant for supplying certain goods and for making and supplying an all-iron roof with roofing sheets.

The defendant filed answer admitting his liability in a sum of Rs. 110·63 and claiming the right to set off a sum of Rs. 500 as damages in terms of the agreement (D1) dated July 20, 1927.

The plaintiff and defendant entered into two agreements regarding the roofing sheets.

By the first agreement dated July 11, 1927, the plaintiff agreed to make and supply the roofing sheets for the sum of Rs. 3,225 within one and a half month and also agreed " to pay a penalty of Rs. 10 for each day that the work delays ".

By the second agreement dated July 20, 1927, which superseded the first, the plaintiff agreed to supply the roofing sheets by August 20, 1927, and in default to pay a " fine " of Rs. 500, which the defendant was authorized to deduct from the balance sum due to the plaintiff, who had received an advance.

These agreements were not drawn by a legal draftsman, and it is impossible to say whether the parties knew the meaning of the word " penalty " or the meaning of the words " fine " used in the agreements.

[1] 28 *N. L. R.* 430.
[2] (1906) *A. C.* 368, 375.
[3] (1915) *A. C.* 79.

The roofing sheets were admittedly supplied to the plaintiff in several consignments, the last of which was delivered on September 3, 1927. The plaintiff therefore made default in performance of the agreement.

As regards the defendants' claim for damages, the learned District Judge held that the sum provided for was a penalty on two grounds : (*a*) As the agreements do not refer to it as liquidated damages ; (*b*) As " the stipulation to pay a fixed sum where the delay was one day or one month seems hardly reasonable or conscionable ". He further held that the defendant had not proved damages and entered judgment for plaintiff as prayed for with costs. The defendant appeals from this judgment.

The question we have to decide is whether the sum of Rs. 500 was provided for in default of performance of the contract as a penalty or as liquidated damages.

The same question arose for decision in the case of *The Dunlop Pneumatic Tyre Co., Ltd. v. The New Garage & Motor Co., Ltd.*[1] I need not state the facts of that case which are not relevant to this appeal. Lord Dunedin stated in his judgment the various propositions deduceable from the decisions, thus :—

(1) Though the parties to a contract who use the words " penalty and liquidated damages " may *prima facie* be supposed to mean what they say, yet the expression used is not conclusive. The Court must find out whether the payment stipulated is in truth a penalty or liquidated damages.

(2) The essence of a penalty is a payment of money stipulated as *in terrorem* on the offending party. The essence of liquidated damages is a genuine covenanted pre-estimate of damages.

(3) The question whether a sum stipulated is penalty or liquidated damages is a question of construction to be decided upon the terms and inherent circumstances of each particular contract, judged of as at the time of the making of the contract, not as at the time of the breach.

(4) To assist this task of construction various tests have been suggested, such as (*a*) It will be held to be penalty if the sum stipulated for is extravagant and unconscionable an amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach ; (*b*) It will be held to be a penalty if the breach consists only of not paying a sum of money and the sum stipulated is a sum greater than the sum which ought to have been paid ; (*c*) There is a presumption (but no more) that it is a penalty when a single lump sum is made payable by way of compensation on the occurrence of one or more or all of several events some of which may occasion serious and others but trifling damage ; (*d*) It is no obstacle to the sum stipulated being a genuine pre-estimate of damage, that the consequences of the breach are such so as to make precise pre-estimation almost an impossibility. On the contrary that is just the situation when it is probable that the pre-estimated damage was the true bargain between the parties.

Applying these tests to the present case, the sum of Rs. 500 stipulated for cannot be said to be extravagant and unconscionable an amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach. The plaintiff was about fourteen days in default, but he may have been in default for weeks and months and it is quite possible that the damage sustained by the defendant would have amounted to Rs. 500.

Test (*b*) does not apply for the breach, does not consist in the non-payment of a sum of money, nor does test (*c*), for the sum of Rs. 500 is not payable on the occurrence of one or more or all of several events, but on the occurrence of one event.

[1] (1915) *A. C.* 79.

Applying test (*d*), it appears to me that the consequences of the breach of the agreement are such as to make precise pre-estimation almost an impossibility.

Plaintiff's claim therefore that the sum of Rs. 500 was stipulated for breach of the agreement stands the tests formulated by Lord Dunedin.

Respondent's counsel contended however that the appellant had not discharged the burden which lay upon him, by reason of the use of the expressions " penalty " and " fine " used in the two agreements. I am unable to agree with this contention.

I think the two agreements considered together indicate that the sum of Rs. 500 was agreed on as liquidated damages.

By the first agreement the plaintiff agreed to pay Rs. 10 for each day he was in default. If the defendant had claimed damages for each day the plaintiff was in default on the footing of the first agreement it would have been impossible to argue that the sum stipulated for was not agreed upon as liquidated damages. It could not possibly have been said that it was stipulated for as *in terrorem* of the defending party nor that it was extravagant and unconscionable in amount in comparison with the greatest loss the defendant could have sustained by the breach. I should therefore have held that the payment provided for by the first agreement for breach of the contract was a genuine covenanted pre-estimate of the damage. What then was the object of substituting Rs. 500 for the payment of Rs. 10 a day ?

Prima facie it was a pre-estimate of the damage the defendant might sustain by a breach of the contract. At the time the contract was made it was impossible for the parties to say what damage might result from a breach of the contract.

Apart from what can be gathered from the two agreements as to intention of the parties, the law is that where a contract contains only a single stipulation on the breach of which a specified sum whether large or small is to be payable, such a sum is liquidated damages. Unless the single stipulation is only of very trivial importance or can only give rise to nominal damages and the sum payable is considerable, the disproportion between the two may be so great as to make it plain that the sum was fixed as a penalty. (*Law v. Redditch Local Board.*[1]) On the principle laid down in this case the sum of Rs. 500 which is referable to the breach of a single stipulation was agreed on as liquidated damages. The qualification does not apply, for the stipulation is not of very trivial importance nor when the agreement was made one which could only give rise to nominal damages. An illustration of this qualification is given by Lord Halsbury in the case of *Clydebank Engineering & Shipbuilding Co., Ltd. v. Don Jose Ramos Yzquierdo Y Castaneda.*[2] He says : " For instance if you agreed to build a house in a year, and agreed that if you did not build the house for £50 you were to pay a million of money as a penalty, the extravagance of that would be at once apparent. " The disproportion between the damages and the sum payable in the illustration is so great as to make it plain that the sum was fixed as a penalty.

The learned District Judge's observation that " the stipulation to pay a fixed sum whether the delay was one day or one month seems hardly reasonable or even conscionable " is not in accordance with the principle that the agreed sum is a penalty if it is extravagant or unconscionable in relation to any possible amount of damages that could have been within the contemplation of the parties at the time when the contract was made.

The sum of Rs. 500 when the agreement was made was not an impossible amount either because of the length of the delay after the day fixed in the performance of

[1] (1892) 1 *Q. B.* 6, 127. [2] (1905) *A. C.* 6.

the contract or by reason of other causes for damage which might have arisen owing to the delay.

For the reasons given by me I hold that the sum of Rs. 500 was agreed upon as liquidated damages for breach of the contract. That being so it was not open to the Court to interfere with it (*Public Service Commissioner v. Hills* [1]).

I set aside the judgment appealed from and enter judgment for plaintiff for Rs. 110·63 with interest at 9 per cent. from January 18 till payment in full, and Court of Requests costs.

The plaintiff will pay the defendant the excess costs incurred by the defendant by reason of the action being brought in the District Court.

The appellant will be entitled to the costs of the appeal.

JAYEWARDENE A.J.—

By agreement dated July 20, 1927, the plaintiff undertook to complete the iron works of the roofs and the work of the verandahs of certain buildings within one month's time, and if he failed to complete all the works and give over within that month, he promised to pay a fine of Rs. 500 to the defendant and further authorized the defendant to deduct this sum from the full sum due to the plaintiff after the work was completed. The plaintiff failed to complete the iron work as stipulated on August 20, and the defendant claims to be entitled to withhold the sum of Rs. 500. The learned District Judge has held that the sum of Rs. 500 was a penalty and not liquidated damages, and awarded the defendant nothing at all as damages. In *Fernando v. Fernando* [2] Bonsor C.J. observed that these stipulations for penalties originated in the difficulty of proving damages. Voet (45, 1, 13) states that where damages had to be determined by a Court there was considerable difficulty in the way of proof and in consequence the practice arose of the parties agreeing to a fixed penalty which would obviate the necessity of the Court entering into an inquiry as to the *quantum* of damages. Justinian recommends the parties to stipulate for a penalty—*Et in hujusmodi stipulationibus optimum erit peonam subjicere, ne quantitas stipulationis in incerto sit ac necesse sit actore probare quid ejus intersit. Itaque si quis, ut fiat aliquid, stipuletur ita adjici poena debet ;*

Si ita facta non erit, tunc poenae nomine decem qureos dare spondes ? (*Institutes* 3, 16, *sec.* 7). Voet discusses the subject in the 12th and subsequent sections of Book 45, tit. 1, and states at the end of section 13—*Denique moribus hodiernis volunt, ingente poena conventione apposita, non totam poenam adjuciandum esse, sed magis arbitrio judicis eam ita oportere mitigari, ut ad id prope reducatur et restringatur, quanti probabiliter actoris interesse potest.* The Court would intervene and reduce the damages, only when the penalty is out of all proportion to the damages likely to be caused by the breach of the contract, or where the penalty is *ingens.* In referring to this passage in *Namasivayam v. Suppramanium and Thambyah* [1] Berwick D.J., the learned translator of Voet, remarks that penalty, *poena* in the technical language of the Civil law, is not the same as it is in the technical language of the English law. The latter speaks of three things : Damages (to be assessed by a Jury) ; liquidated damages fixed by the parties themselves; and " penalty " or a penal sum which Equity reduces to the real damage sustained. But in the language of the Civil law, we have only two things, viz., *id quod interest,* which corresponds broadly with the English word " damages " and " *poena,* a penalty ", which is exactly equivalent to the English term " liquidated damages " or rather it includes both that and the English idea of a penalty.

Pothier in his *Treatise on Obligations, sec.* 345, says that the penalty stipulated in case of a breach of the contract

[1] (1906) *A. C.* 368. [2] (1899) 4 *N. L. R.* 285.

[1] (1877) *Ram. Rep.* 362, *at p.* 371.

can be reduced and mitigated by the Judge, when it is excessive (*lorsqu' elle est excessive*).

Bonser C.J. held that there is no authority for the proposition that, wherever a penalty is fixed, it is the duty of the Court to enter into the question of the *quantum* of damages. It must be shown that the *poena* is, as Voet describes it, *ingens*, or as other writers call it, *immanis* or *immensis*.

Withers J. observed that there is nothing in the use of the word "penal" in contracts governed by the Roman-Dutch law to prevent the stipulation being enforced. (*Fernando v. Fernando* (*supra*)). This case was followed in *Pless Poll v. De Soysa*.[1]

It was held by the Privy Council in *Webster v. Bosanquet* [2] that, whatever be the expression used in describing the payment, the question must always be whether the construction contended for renders the agreement unconscionable and extravagant and one which no Court ought to allow to be enforced. The case of *The Clyde Bank Engineering Co. v. Don Jose Castenada* [3] was referred to, where it was held that it is to be considered whether the stipulation is extravagant, exorbitant, or unconscionable at the time the stipulation was made, that is to say, in regard to any possible damages which may be conceived to have been within the contemplation of the parties when they made the contract. In *Jayasinghe v. Silva* [4] Lascelles C.J. thought that the Roman-Dutch law governs this question and that the *quantum* of damages should not be considered where a penalty is fixed unless it is shown that the *poena* is *ingens* or *immanis*. It was held by Schneider J. in *Attorney-General v. Costa* [5] that the Roman-Dutch law does not recognize the English distinction between penalty and damages and that under our law even a penalty may be recovered if it be not *ingens* or *immanis*. In the case of *Wijewardene v. Noorbhai*,[1] however, Dalton J. was of opinion that the law as it exists to-day had taken over the English distinction between penalty and liquidated damages. The criterion seems to be very much the same—that is whether the sum stipulated for can or cannot be regarded as a genuine pre-estimate of the creditor's probable or possible interest in the due performance of the principal obligation. Enormous disparity will point to its being a penalty, while the fact of the payment being in terms proportionate to the loss will point the other way. But the circumstances must be taken as a whole, and must be viewed as at the time the bargain was made.

In my view the sum of Rs. 500 agreed upon was neither extravagant nor *ingens*, but could be regarded as a genuine pre-estimate of possible damages to the defendant by the breach of the contract. I agree to the order proposed in all respects.

Appeal allowed.

[1] (1909) 12 *N. L. R.* 45. [3] (1905) *L. R. A. C.* 6
[2] (1912) 15 *N. L. R.* 125. [4] (1911) 19 *N. L. R.* 170.
[5] (1922) 24 *N. L. R.* 281.