



Jus Corpus Law Journal

Open Access Law Journal – Copyright © 2022 – ISSN 2582-7820
Editor-in-Chief – Prof. (Dr.) Rhishikesh Dave; Publisher – Ayush Pandey

This is an Open Access article distributed under the terms of the Creative Commons Attribution-Non-Commercial-Share Alike 4.0 International (CC-BY-NC-SA 4.0) License, which permits unrestricted non-commercial use, distribution, and reproduction in any medium, provided the original work is properly cited.

Critical Analysis of the Theory of Fundamental Breach of Contract

Aakanksha N^a

^aTamil Nadu National Law University, Tiruchirappalli, India

Received 28 May 2022; Accepted 15 June 2022; Published 22 June 2022

If necessity is the mother of invention, then conflict is its father, if the need is the motive behind the formation of a contract between people, then it's the self-same contract that pretexts the dispute between them. Breach of contract is the common term, which is used for claiming the damages, so in this paper, we shall look through what constitutes one of the most important kinds of the breach, i.e., Fundamental Breach. Exclusion clauses are an integral part of the contract, so any breach or damages to be awarded can't be discussed without, paying due diligence to this concept. This research is an attempt to examine the impact of sections 28 and 124 of the Indian Contract Act in the event of a FUNDAMENTAL BREACH of a contract.

Keywords: *contract, breach, damages, due diligence, contract.*

INTRODUCTION

The ever-expanding global economy has engulfed the hawks and formed a single outlet known as the global market, this has not only, given a way out for the customers but also, instigated the local industries to expand their production and compete with the world at large. Abridging the same, we could say that, a nation, in the present times, can't survive without interacting with other countries. Even the most developed country like America depends on

less developed middle-east countries for crude oil and China for the supply of electronic parts. What better proof than Russia-Ukraine War, to prove global market agglomeration, the warmth of which could be felt in the domestic markets of the countries. So, just like, manufacturing and selling, contracts have also become an important limb of business transactions. There are various agreements signed, explicitly or impliedly every moment even without us noticing them. Therefore, two or more people every second of the clock, enter an agreement, and people, having different interests come together, and negotiate their difference to achieve their goals in the best possible way. In our country, it is the Indian Contract Act of 1872, which is the chief legislature that governs the contract proceedings. Section 2¹ and Section 73² of the Indian contract Act, basically speaks about the primary and secondary obligations of the parties to the contract. The primary obligation would be to fulfill the contractual agreement in good faith and the latter would be the remedial step the party has to take, in the case of the non-performance of the first. Non-performance of the primary obligation would be cited as a BREACH of the contract, by section 39³ of the Contract Act. The nature of the contract and its obligation determines the nature of the breach. If a particular breach or breach has disrupted the root of the contract, making the other party repudiate the entire contract, then, this breach is referred to as a fundamental breach of contract. We as humans are used to speaking squarely, so we use 'fundamental breach' and 'breach of fundamental' synonymously former involved paying attention to "the character of the breach" and determining "whether, in consequence of it, the performance of the contract becomes something different from that which the contract contemplates." The latter was something underlying the whole contract so that, if it is not complied with, the performance becomes something different from that which the contract contemplated

For instance, if a man contracts to buy peas but gets beans instead, there is no warranty to sell peas, instead, the contract is to sell peas and if he sends him anything else in their stead it is a non-performance of it. These were the famous words of Lord Arbinger from the Chanter v

¹ Indian Contract Act, 1872, s 2

² Indian Contract Act, 1872, s 73

³ Indian Contract Act, 1872, s 39

Hopkins case.⁴ Extrapolating the judgment, we realize that, if there is a fundamental difference between what has been agreed upon and what has been done purportedly under that agreement and this difference forms the basis for the fundamental breach of the contract This gets us to the breach of the contract, tailing through the same we can understand the main postulate of the paper, i.e., how to strike a negotiation between section 28⁵ and section 39 of the Indian Contract Act.

In the case of, *Birch v Thomas*⁶, the plaintiff, Clive Roosevelt birch, the plaintiff brought an action claiming damages for injuries that he had endured, when he was traveling as a passenger, in a car driven by the defendant. Thomas, the defendant, had placed a sticker on the window of his car, which, said, "Passengers ride at their own risk and on the condition that no claims shall be made against the driver or owner. Additionally, the defendant was a minor, so, he didn't cover insurance, which indemnified the passenger injury cost. So, he had informed the plaintiff about both, clauses, before the ride. The question before the court was whether this amounted to a fundamental breach. The court while, pronouncing the decree said that "*To come within the doctrine of fundamental breach, the conduct would have to be something quite outside the contemplation of the parties, such as the instance of a man who drove off the road across a field, or who drove up the wrong carriageway*"⁷ which became one of the primary definitions of the fundamental breach of contract. This case will act as a nutcracker for us to study fundamental breaches, in cognate to the exclusion clause and indemnity clause.

EXCLUSION CLAUSES

No condition or warranty that the vehicle is roadworthy, or as to its age, condition or fitness for any purpose is given by the owner or implied herein."⁸Imagine, after economizing your spending for a year, you go to purchase an important asset, after stacking up the money you required and there is a clause like this in the agreement. You plod around looking for the

⁴ *Chanter v Hopkin* [1838] 4 M & W 399

⁵ Indian Contract Act, 1872, s 28

⁶ *Birch v Thomas* [1911]

⁷ Stephen J. Leacock, 'Fundamental Breach of Contract and Exemption Clauses in the Commonwealth Caribbean' (1975) 4 (2) *Anglo-American Law Review*, 181

⁸ *Karsales (Harrow) v Wallis* [1956] 1 WLR 936

article in the other shops, but you are despoised to find the same clause everywhere. Now, after the expedition you are left with just two alternatives, either to accept the contract with the clause or to reject it, in either case, the clause which steeples the freedom of the contract is denying the consumer his freedom of choice.

These kinds of clauses could be found, in all aspects of the working society, from your Maggie packets to the government contract, they are present everywhere. For instance, many standard form contracts relied upon and floated by public sector enterprises contain clauses that specifically provide that in the event of delay in completion of work, the contractor shall not be entitled to compensation.⁹ Could, there be a blanket ban on the exclusion clause to protect the right of the customers? Will this not impede the functioning of the business? So, it's very important to understand what this clause means, in the real sense.

INCEPTION & OBJECTIVE OF THE CLAUSE

An exclusion clause in the contract is like the provision of *Volenti non-fit injuria* in torts, it limits or excludes the liability of the party in the legal phenomenon. The main purpose of this clause is to place substantive limitations upon the rights to which they apply, and, accordingly, to help delimit and define those rights.¹⁰ The intention of these, clauses isn't to lump the claim for damages, but rather to, prevent those problems, from arising in the first place. People, at the time of entering the contract, wouldn't have contemplated, that their exclusion clause deprives a party, of all contractual forces, if a person, has deceitfully framed the clause, to deceive the other party, then it won't be called a contract, but rather a declaration. Parties in contract, are free to determine for themselves, what primary obligations they will accept, in lieu, that, it is legally acceptable. And, these clauses are, generally accepted all over the world, hence, it even acceptable under the Indian Contract Law.

⁹ Michael Bridge, 'Avoidance for Fundamental Breach of Contract under the UN Convention on the International Sale of Goods' (2010) 59(4) *The International and Comparative Law Quarterly*, 911

¹⁰ G.H.L. Fridman, 'The Effect of Exclusion Clauses' (1969) 7 (2) *Alberta Law Review*, 281

The concept of the exclusion clause was first dealt with in the case of *Wallis v Prat*¹¹ which induced numerous questions in people's minds. Could the purchaser under the conditional sale agreement repudiate and rescind this contract? Or were they bound by the exclusion clause therein?¹² In this case, the House of Lords held that, though there was a breach of condition, the plaintiff can only claim damages, as he re-sold the product which he received, this brings us to the next question. Is there any provision that could prevent the negative effect of the clause on the traders, i.e., should there be any control over the exclusion clauses in the business contracts? For which we shall firstly proceed with, the provision of the exclusion clause according to section 28 of the Indian Contract Act.¹³ Exemption clauses are terms inserted into the contract, whereby the party seeking to rely upon them tries, to escape liability for the consequences of his breach, which arises in the course of performing the contract.¹⁴ Liability arises as a breach of the primary obligation by the contracting party, and the presence of the exclusion will immune the party from the liability. The provision of the exclusion clause is a double edge barrel, it not only promotes the freedom of the promoters of the contract but could also be used as a tool of exploitation, by the deceitful party against another, after all the clauses are grammatically played out sentences. So, people, who are against the exclusion clause opine that the exclusion clauses would evade the secondary obligation of the party, by this the whole essence of the contract is lost.¹⁵ And it's the secondary obligation that makes the primary objective effective, that is the reason in parallel, Article 32¹⁶ of the Indian constitution is referred to as the heart and soul of the constitution.

Most, fundamental breaches, cases, claiming damages, usually have to deal with, the definition and implication of this clause. For instance, in the case of *R.S Deboo v Ms. Hindlekar*,¹⁷ the liability clause was printed on the back of the receipts. To restrict his liability for the quantum of loss to twenty times the laundering charges or half of the value of unreturned articles

¹¹*Wallis Son and Wells v Pratt and Haynes* [1911] AC 394

¹² G.H.L. Fridman (n 10)

¹³ Indian Contract Act, 1872, s 28

¹⁴ Stephen J. Leacock (n 7)

¹⁵ Indian Contract Act, 1872, s 28

¹⁶ Constitution of India, 1950, art.32

¹⁷*R.S. Deboo, (Since Deceased By v Dr. M.V. Hindlekar And Another* (1994) 96 BOMLR 60

whichever was less whatever the cause for non-return of the article entrusted by the customer to the laundry for purpose of laundering. Still, the Bombay HC opposed the clause and didn't provide the exclusion stating that the liability clause was against the constitutional values and the fundamental principles of the contract law. A clause, which was written behind the receipt, won't form the base of the contract, without the signature of the other party and directed the defendant to justify his actions. The court also held that the party in the contract can't unjustly, enrich himself, by implying a deceitful clause in the contract. Similarly, in the case of *Maharashtra State Electricity Distribution Co. Ltd v DSL* and *HPA International v Bhagwandas* and *LIC v Consumer Education*, the court upheld the fundamental breach against the exclusion clause. But, the case of the MP high court in the case of *P.C. Rajput v State of M.P.*¹⁸, rejected the application for the fundamental breach, upholding the exclusion clause, asserting to the parties of the contract that, the exclusion clause was not an independent rule of law, imposed arbitrarily by the court, rather, it was the state of affair, which the party of contract has entered on own. Ergo, this would surge our confusion and make us skeptical. What are the parameters which are used by the court of law, to determine whether to exclusion clause would be implied in the particular breach case or not? Is there any definitive legislation that lays down the procedure to determine the exclusion clause cases? Firstly, answering the former question, there isn't any substantive law, which explicitly says, the exclusion clause is not applicable in the cases of the fundamental breach. So, as propounded by Lord Reid in the judgment of *Suisse Atlantique*¹⁹, on the establishment of a fundamental breach, the applicability of exclusion clauses is a matter of construction. Further illustrating the same, in the case of *Photo Production Ltd. v Securicor Transport Ltd.* which is extensively referred by the courts, while determining the pertinence of the limitation clause, in adjudicating fundamental breach cases²⁰. In this, case, the parties, were at odd, due to the mischief caused by the defendant's employee, according to the clause of the contract, under no circumstances shall the Company be responsible for any injurious act or default by any employee of the company unless such act or default could have been foreseen and avoided by

¹⁸ *P.C. Rajput v the State of M.P.* AIR 1993, MP 107

¹⁹ Stephen J. Leacock (n 7)

²⁰ *Photo Production Ltd. v Securicor Transport Ltd.*, [1980] AC 827

the exercise of due diligence on the part of the company as his employee. Be that as it may, the employee, of the defendant company, lit a fire, which, burnt down the factory of the plaintiff. The case, before the court, was to determine, whether there was a fundamental breach of contract or if the case could be dispersed on the grounds of the presence of the clause?

The court, while pronouncing the decree, said that the defendant company was vicariously liable for the acts of the employee, though, the act, was committed, beyond the scope of employment.²¹ Thus, the clause of unforgeability can't be used, it also acknowledged, that, the case wasn't about the breach of fundamentals, unlike Pearson L.J. as chalk for cheese. In, this case, the court, rather, looked upon the objective of the exclusion clause. The purpose of the clause, was, ascertained, to prevent harmful damage, caused by accidental fire and also, to prevent, the defendants from, encumbering the loss, for the accident. Since, the incident was the result of deliberate action, the clause can't be used as protection by the defendant. It could be inferred that there is no definite rule which suggests that, in every case of the fundamental breach the exclusion clause, wouldn't be implied, as in the case the judge had, said, the resources of the English law, aren't so narrow and limited that it is impossible to devise an exclusion clause which will apply to at least some cases of fundamental breach.²² Therefore, in determining these types of cases, it is important to have a two-step construction, first to determine the fundamental breach and later to establish whether the clauses apply to the breach.²³ While determining the fundamental breach, the court is going to consider whether the exclusion clause, is a part of a contractual obligation or not, if the clause, qualifies this parameter, then the breach would be declared no breach at all. For instance, in the case of *Angles* where the relevant clause stated inter alia that the charterer was not to be liable for failure to supply cargo "due to unavoidable hindrances"²⁴

²¹ Stephen J. Leacock (n 7)

²² Tony Dugdale & N.V. Lowe, 'The Construction of Exclusion Clauses Upon Affirmation of a Fundamental Breach,' (1979) 17 (3) *Alberta Law Review*, 423

²³ Stephen J. Leacock (n 7)

²⁴ Tony Dugdale & N.V. Lowe (n 22)

INSURANCE CONTRACTS

Here, it is very important, that we understand, what is indemnity clause, before, discerning the fundamental breach aspect. INDEMNITY CLAUSE, the contracting party, may attempt to avoid the consequences of liability by making the person with whom he contracts, bears the loss resulting from this, own breach of duty. The insurer employs a variety of devices in the form of terms and conditions to protect himself against alteration of the risk insured during the period it is covered. These terms and conditions include temporal exclusions and continuing or promissory warranties. Here, we need to discuss the scope of the indemnity clause, and how the principle of the construction of the contract, impacts insurance contracts? Is negligence included or not in the indemnity clause? Section 124 to 147²⁵ of the Indian contract act speaks about INDEMNITY AND GUARANTEE. Section 124 of the Indian contract act defines the contract of indemnity²⁶, in the definition the term promise is ambiguous used, it doesn't specify whether it is expressed or implied promise, which would be indemnified²⁷ since it just uses the term promise, we could also assume that as in the case of *Eastern Shipping Co. Ltd. v QuahBengKee*. The right to indemnity need not arise by contract; it may (to give other instances) arise by statute²⁸ Since there are various types of insurance contracts, health insurance, property insurance, travel insurance, etc. And different insurance has been framed to serve different purposes. For instance, in the case of *McIntosh v Dalwood*, it was held that the court must ascertain the contractual obligation, if the contract is just about repaying the money he has paid (damages), then no other relief is required. Alternatively, if the insurer must relieve the debtor, then the party need not pay first to get indemnified.

The indemnity clause of the insurance specifically states that the Ohio case states the express referential rule. The better rule for interpretation of indemnity clauses appears to be the one that excludes coverage for the indemnitee's negligence in the absence of express provision for its inclusion. The law in this area lacks certainty and uniformity, as exemplified by the Ohio

²⁵ Indian Contract Act, 1872, ss 124-147

²⁶ Indian Contract Act, 1872, s 124

²⁷ Wayne Courtney, 'Indemnities and the Indian Contract Act 1872' (2015) 27 (1) National Law School of India Review, 66

²⁸ Indian Contract Act, 1872, s 124

decisions, and gives rise to much unnecessary litigation and unfairness which could be eliminated should the "express reference" rule be adopted in all jurisdictions. In the case of Ohio, it was held that the rule of express reference would be used, in determining whether the indemnity clause would cover the negligence of the indemnitee.

MOTOR VEHICLE INSURANCE

In Motor vehicle insurance, the contract is framed, so the contractor indemnifies the damage caused. Usually, the exclusion clause is used to evade the liability, arising due to non-deliberate, unforeseen actions, but, in this case, the indemnity clause, states that the contractor, will only indemnify for non-deliberate actions, if the exclusion clause, is used in these cases, which would destroy the purpose of the contract itself.²⁹ In the case, *Central Bank of India v Hartford Fire Insurance Co.*, the insurance was against loss of goods by fire, riot, or civil commotion, and then the insurance could be terminated at the discretion of the party. This provision applies to both the parties, Supreme Court while, adjudicating this case, referred to *Sun Fire Office v Hart*.³⁰

BAILMENT CONTRACT

In the case of *Sze Hai Tong Bank Limited v Rambler Cycle Co. Ltd.*,³¹ the bill of lading included a clause, which stated that the responsibility of the carrier will commence when the goods are loaded and concludes once they are discharged. According to the bill of the lading, the shipowner is not authorized to deliver to the consignee without the production of the bill of lading. Hence in this case the defendant was held liable under section 8 of the carrier act, which speaks about the liability of the carrier irrespective of the present exclusion clause. This is because, the primary duty of the carrier is to deliver goods only on production of the bill of lading, so this duty can't be disregarded on taking of indemnity.³²

²⁹ Michael Bridge (n 9)

³⁰ John Hartshorne, Nicholas Smith & Rosemarie Everton, 'Caparo under Fire: a Study into the Effects upon the Fire Service of Liability in Negligence' (2000) 63 (4) *The Modern Law Review*, 502

³¹ *Sze Hai Tong Bank Limited v Rambler Cycle Co. Ltd.* (1969) 25 M.L.J. 200

³² *Ibid*

Section 153 of the Indian contract states that the bailee is under the obligation to act in accordance, with the contract³³. In the instance of, wrongful use or the disposal of the goods, the bailer has the right, to terminate the contract and recover the possession. And the subsequent sections till section 170, speak about various rights of the bailee and the bailor³⁴. Hence, to determine the liability of the party in the case of a fundamental breach, the core of the contract has to be evaluated, whether it was a contract of carriage or safekeeping. So, the presence of the exclusion clause, without the specified ambit, would immune the bailee against negligence. As in the case of on in *Turner v Civil Service Supply Association*,³⁵ the exclusion clause provided immunity to the carrier against the damage caused by the fire during the transit. In reality, the driver of the transit consciously lit the gasoline during the journey, the court granted relief to the defendant just based on this clause.

For example, in the case of, *Rutter v Palmer*, it was held that in interpreting an exemption clause some rules may be applied

- First, the defendant is not exempted from liability for the negligence of his servants unless adequate words are used;
- Secondly, the liability of the defendant apart from the exempting words must be ascertained; If the immunity he is seeking is that, of negligence, then the court without any objection will provide him with the same.³⁶

CONCLUSION

From these precedents, we can theorize that exclusion, or the liability clause, can't be arbitrarily implied or disposed of, as this is the axis, with demarcates the freedom of contract and the contracting parties. At the same, time the court has the right to interfere, if the exclusion clause is discriminatory and is tyrannizing the other party, i.e., one party has more bargaining power than the other. Never the more minor, it should be noted that the terms of

³³ Indian Contract Act, 1872, s 153

³⁴ Indian Contract Act, 1872, s 170

³⁵ *Turner v Civil Service Supply Association* [1926]

³⁶ *Rutter v Palmer* [1922] All ER Rep 367

the clause, should be lucid and to be conveyed in the positive terms, and shouldn't be phrased in a way, which could deceive the other party. Since, there, is no magic bullet that could be used to determine the scope of exclusion clauses, it would rather be more convincing that, we look through the construction of the contract in conjunction with the objective of the clause, used in the construction, to establish the realm of the clause in the contract. The purpose of this paper was not to prove a point for or against fundamental breach, rather was a progressive step, toward emphasizing the construction of the contracts.