AN ANALYSIS OF THE CONTRACT OF INDEMNITY

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ABSTRACT

This research concerns with the Contract of indemnity including the rights of the indemnity holder. The author's aim in writing this research is to analyse the Contract of indemnity with reference to some important case laws and outlines the non-exhaustive nature of Section 124 and Section 125.

Objectives of study are: -

1. Meaning of Indemnity.
2. Nature and scope of Indemnity.
3. Analysis of various case laws.
4. Analysis of Section 124 and Section 125.
5. Distinction between Express and Implied Indemnity.

Introduction:

Indemnity is an obligation by a person (**indemnitor/indemnifier**) to provide compensation for a particular loss suffered by another person (**indemnitee/indemnity holder**).

Many insurance contracts are based on indemnities; A car owner, for example, may obtain various types of insurance as an indemnity for various types of loss arising from the operation of the car, such as car damage itself or medical bills incurred as a result of an accident.

A principal may be required to indemnify their agent in the context of an agency relationship for liabilities incurred while carrying out the relationship's responsibilities. While the events that trigger an indemnity may be predetermined by contract, the steps that must be taken to compensate the harmed party are frequently unexpected, and the maximum compensation is frequently expressly limited.

In early English law, Indemnity was characterized as "a promise to save an individual from the results of an act. Such a promise can be express or implied from the circumstances of the case".

The case of **Adamson vs Jarvis (1872)**[1] exemplified this point of view. The plaintiff, an auctioneer, sold some things on a person's instructions in this case. The commodities turned out not to belong to the person, and the rightful owner held the auctioneer responsible in exchange for the products. The defendant, in turn, was sued by the auctioneer for indemnification for the damage he sustained as a result of the defendant's actions. It was determined that since the auctioneer preceded the defendant's instructions, he was allowed to believe that if something went wrong, the defendant would compensate him.

This gave the term "indemnification" an extremely broad definition, including the guarantee of indemnity for loss caused by any cause. So, with the exception of life insurance, all insurance was a contract of indemnity. The Indian Contract Act of 1872, on the other hand, limits the scope of an indemnity contract by defining it as follows:

Section 124 - 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 a "contract of Indemnity".[2]

First and foremost, we must define the terms "contract" and "indemnity." In one sense, Section 124's definition of a contract is incomplete: a contract is complex in nature, but the meaning only accounts for one party's obligations, and even then, just for one type of duty. In English, the term "contract of indemnification" is frequently used in a more specific sense to describe a contract in which one party's sole, or only significant, executory obligation is to indemnify the other.

The main issue is that an indemnity commitment in a contract, not an indemnity contract, is the correct subject of analysis. In the precise sense previously indicated, a contract of indemnity can then be regarded similarly to a promise of indemnity that is merely among several clauses in a larger contract. As a result, it appears that the technical distinction between a contract of indemnification and a promise of indemnity has not perplexed Indian courts. The terms 'promise' and 'promise to indemnify' appear in Sections 124 and 125, respectively, and Section

[1] Adamson vs Jarvis (1872)
[2] Section 124, Indian Contract Act, 1872

125(1) pertains to the 'promise to indemnify.' The same mixed usage may be found in other jurisdictions.

The term "indemnity" refers to a broad concept that can be applied to any arrangement in which one party is guaranteed not to lose money. There are two kinds of 'indemnity' arrangements: those in which the undertaking's primary concern is to accurately protect the promise against loss, and those in which the undertaking's primary concern is not of that nature, but the promise is incidentally or appropriately indemnified against loss. The prior arrangements are the subject of this article, as well as Sections 124 and 125. In the strictest sense, these are assurances of indemnity. Despite this, the use of the term "indemnity" in the last sense is extremely common. It could be contended that A's payment of damages for breach of contract with B in an agreed amount to B's loss or obligation to another 'indemnifies' B, or whether A's guarantee to B offers an 'indemnity' to B against default by a third party, C, or of A's promise to B to pay C, B's creditor, impacts an 'indemnity' against B's liability to C.

For example, A indemnifies B against the repercussions of any legal action taken by C against B in correlation with the payment of Rs. 200. This is an indemnity contract.

The following fundamental aspects are included in this definition:

1. There has to be an actual loss that has been caused to the indemnity holder.

2. Either the promisor or another individual must be responsible for the loss (in Indian law Only a human agency is capable of causing loss.)

3. The indemnifier is exclusively responsible only for the loss.

According to the facts, this contract is conditional, and it is only legally binding if and when the loss occurs.

Promise to indemnify or right to be indemnified can either arise from an express or an implied contract.

Section 124 talks somewhat narrow and it does not include loss incurred from accidents, unforeseen events, inevitable incidents, etc.

Implied indemnity is not included under Section 124.

In 13th report of the law commission of India 1958 it suggested: -

- To include the concept of implied indemnity in Section 124.
- It is also suggested that where the loss is not caused by the promisor or any third party, it should be included. E.g.- Accidents, Unforeseen events, etc.

Before a loss occurs, the indemnity is enforced.

It is worth noting that the Act says nothing about the promise's ability to enforce the indemnity. The Act went into effect long before England's legal and equitable systems were merged. The action taken by an indemnified party to enforce the indemnity under English law at the time was based in part on the nature of the loss." In most cases, the commitment to indemnify was interpreted as a promise to hold the indemnified party harmless from the specified loss. At common law, imposing a contract was typically accomplished through a claim for breach of contract damages. The contract would be breached only if the indemnified party suffered a loss; at that point, the indemnifier had ended in failure by definition to hold the indemnified party harmless against loss. The amount of real loss was equal to the number of damages awarded. As a result, the remedies available in common law courts were ineffective in protecting the indemnified party before the loss is incurred. If the loss was only anticipated, the indemnified party had to seek redress in a court of equity. The ability of a court of equity to demand specific performance of an indemnification contract was thought to underpin intervention in equity. Equity, on the other hand, worked by explicitly enforcing a specific term of a contract - the promise to indemnify - instead of by enforcing the entire contract."

Rights of Indemnifier:

After attempting to pay the indemnity holder, the indemnifier is bound to pursue all other avenues through which the loss could have been prevented.

Rights of the indemnity holder:

Section 125, defines the rights of an indemnity holder. These are as follows - The promisee (Indemnity holder) in a contract of indemnity, acting within the scope of his authority, is

entitled to recover from the promisor (Indemnifier).[3] These are:

1. Right of recovering Damages - any and all damages that he is obligated to pay in a suit in connection with any matter to which the promise of indemnity applies.

2. Right of recovering Costs - all costs incurred in any such suit if, in bringing or protecting it, he did not violate the promisor's orders and acted as it would have been reasonable for him to act in the utter lack of the contract of indemnity, or if the promisor endorsed him in bringing or defending the suit.

3. Right of recovering Sums - all takes into account he may have reimbursed under the terms of a negotiated settlement in any such suit, if the compromise was not contrary to the promisor's orders and was one that the promisee would have made cautiously in the lack of the contract of indemnity, or if the promisor authorised him to negotiate the suit.

Some of the restrictions that he should observe here are that the indemnity holder's rights are neither absolute or unrestricted under this provision. He must act within the scope of the promisor's power and not go against the promisor's commands.

He must also exercise the same degree of intellect, prudence, and treatment as if there was no indemnity written contract.

As a matter of fact, if he has met all of the contract's requirements, he is also eligible for the rewards.

Calcutta High Court declared in **Mohit Kumar Saha vs New India Assurance Co AIR 1997**[4] that perhaps the indemnifier should pay the entire value of the stolen car as ascertained by the surveyor. Any agreement at a lower amount is imprecise and biased, and thus violates Article 14 of the Constitution.

When does the beginning of liability occur?

Generally, it appears that the indemnity holder may not sue the indemnifier accountable unless he has actually suffered a loss, as defined in section 124. In circumstances where a loss is

[3] Section 125- Rights of Indemnity holder
[4] Mohit Kumar Saha vs New India Assurance Co AIR 1997

imminent and the indemnity bearer is unable to endure the loss, this is a significant disadvantage.

In the well-known case of **Gajanan Moreshwar vs Moreshwar Madan, AIR 1942.**[5] In this case, the plaintiff transfers a property plot to BMC, and BMC agrees to lease the plot to the plaintiff for 999 years. The defendant now desired to construct a structure on the property, which the owner agreed to. Despite the fact that the plaintiff was the owner, the defendant now had control of the plot. The building materials were provided by a Keshavdas. At one point, there was a due of Rs. 5000, but the defendant had been unable to pay.

As a result, the defendant asked the plaintiff to mortgage. As a result, the property was mortgaged to Keshavdas, and he now owed Rs 5000 plus 10% interest. Keshavdas sought Rs. 5000 on supplies once more.

Defendant demanded that Keshavdas be charged with the same property. Plaintiff was now the owner of the property, but the title deed remained with Keshavdas, who refused to hand it over. The landowner is now suing for indemnity because he wishes to exchange title deeds for the land.

The defendant asserted that the promisor commits to protect the promisor from whatever losses he may suffer until the mortgagee brings a complaint against him. Except for life and personal accident insurance, almost all insurance is a contract of indemnification.

In this case, the insurer's guarantee to indemnify is **unconditional and absolute**.

The Bombay high court declared that an indemnity contract was worthless if the indemnity holder was unable to pursue his indemnity until the loss had been compensated. If he was sued, he had to put it on hold until the judgement was rendered and then sue the indemnifier. He may be unable to pay the judgement fees and thus will be unable to sue the indemnifier. As a result, it was decided that if his liability became absolute, he was entitled to payment from the indemnifier.

Section 124 and section 125 of ICA are non-exhaustive of the whole law of indemnity and

[5] Gajanan Moreshwar vs Moreshwar Madan, AIR 1942

equitable principles applicable in the courts of England will apply in this case.

Section 73[6] of the Act gives a right to the parties of a contract, to claim for damages in case of breach of contract. Section 73 of the Act is given below:

"When a contract has been broken, the party who suffers by such breach is entitled to receive, form the party who has broken the contract, compensation for any loss or damage caused to him thereby, which naturally arose in the usual course of things from such breach, or which the parties knew, when they made the contract, to be likely to result from the breach of it.

Such compensation is not to be given for any remote and indirect loss of damage sustained by reason of the breach.

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

Explanation: In estimating the loss or damage arising from a breach of contract, the means which existed of remedying the inconvenience caused by non-performance of the contract must be taken into account."

Difference:

- The main distinction between damages and indemnity is that indemnity can be sought for loss caused by a third party's activity, whereas damages can only be sought for loss caused by the contracting parties' actions in the event of a breach of contract

- Another distinction between damages and indemnity is that damages can only be claimed for violation of contract, whereas indemnity does not need a breach of contract. Indemnity may be sought for losses caused by a third party's actions, which are not always related to a violation of contract.

[6] Section 73

- The primary goal of indemnity is to return a person to the position he was in prior to the loss. As a result, when someone is indemnified, he never makes or loses money; instead, he will be returned to his former position. Damages may be awarded for more than the real loss (in the case of punitive damages) or for less than the actual loss (in the case of compensatory damages).

ADVANTAGES: -

- Indemnity can be sought for a third party's actions, whereas damages can only be sought for the contracting parties' actions.

- Damages can only be recovered for losses caused by a violation of contract, whereas indemnity covers losses even if the contract is not broken.

- Damages can only be sought for a loss that has already occurred due to a breach of contract, whereas indemnity can be claimed even before the actual loss has occurred. "To indemnify" does not just mean to return moneys paid, but also to protect against loss in respect of the liability for which indemnity has been granted. When one person agrees to indemnify another for any liability that the latter may have believed on his behalf, the other party may obligate the contractual party to put him in a position to meet any future liability that may be imposed on him before any real damage is done.

DEEP ANALYSIS OF A CASE LAW:

Abdul Hussain Shaikh Gulamali Jambawalla v. Messrs Bombay Metal Syndicate[7]

The following are the important facts: - Between October 11, 1957, and January 3, 1958, the plaintiff sold and delivered various goods to the defendants, as well as recovering the price. "In respect of the transaction under your invoice...dated September 25, 1957, we do hereby indemnify you against any amount of sales tax that may be levied by the authorities with or without any guarantee thereof, as the case may be, as and when charged," the defendants stated in a letter dated October 11, 1957. On January 3, 1958, the defendants signed a similar letter of indemnity.

[7] Abdul Hussain Shaikh Gulamali Jambawalla v. Messrs Bombay Metal Syndicate

There is no disagreement between the parties that a contract of indemnity in the terms indicated in the above letters existed in respect of the products sold and delivered by the plaintiff to the defendants during the above time.

Before the learned Judge below, the parties agreed that the claim in suit was regulated by the provisions of art. 113 of the Schedule to the Limitation Act of 1963, which are as follows:

113.[8] Any suit for which no period of limitation is provided elsewhere in this Schedule. Three years. When the right to sue accrues."

The right to suit had accrued in favour of the plaintiff when the order dated February 28, 1963, demanding and/or levying sales tax and penalty was issued, according to observations of the case of Gajanan Moreshwar v. Moreshwar Madam (1942) 44 Bom. L.R 703. He held that the claim was barred and dismissed because the three-year period prior to the date of the initiation of the suit had ended.

Mr. Malkani, for the plaintiff, has argued that the learned Judge's ruling is in conflict with the Supreme Court's decision in Shanti Swarup v. Munshi Singh [1967] A.I.R S.C 1315. According to Mr. Malkani, the effect of the Supreme Court's observations in that case is that the plaintiff's right to sue on the parties' behalf indemnity contracts should be held to have accrued only if the plaintiff was damnified and suffered loss of Rs. 3,479.25 by deposit and payment between April 27 and July 1, 1963. As a result, he argued that the lawsuit, which was filed before the three-year term ended on April 27, 1963, was brought inside the three-year period, and was not prohibited by the Statute of Limitations.

On a proper construction of the contracts of indemnity included in the two letters stated above, Mr. Jhaveri for the defendants has argued that the plaintiff became entitled to be reimbursed immediately upon the levy of the sales tax and penalty. By order dated February 28, 1963, the levy was imposed. In fact, the plaintiff had demanded that the defendants deposit the sum of the tax and penalty in accordance with the indemnity contracts. The right to sue arose in favour of the plaintiff immediately upon receipt of the order dated February 28, 1963, according to the actual construction of the indemnity contracts. In this regard, he alluded to Chagla J.'s observations in the aforementioned instance.

[8] Article. 113 of the Schedule to the Limitation Act of 1963

Now, in relation to the expression "right to sue accrues" in the third column of art. 113, one may turn to the provisions of ss. 22 and 23 of the Limitation Act, which deal with ongoing breaches and torts, as well as compensation actions for acts that are not actionable without exceptional injury. It is sufficient to mention, without repeating the text of these sections, that the Law of Limitation has recognised that responsibilities for damages and/or compensation may continue to accrue from day to day in respect of continuous violations of contracts and torts. A negative covenant agreed upon in deeds of conveyance between purchasers and sellers, as well as between lessors and lessees in deeds of leases is an example of a cause of action that may continue to exist under a contract from time to time and day to day. However, this is not a topic in which one should delve too deeply. It is necessary to state that an indemnity contract may give rise to two distinct types of claims, either of which may be enforced in a court of law. The plaintiff's typical common law cause of action on a contract of indemnification did not emerge until after the plaintiff's damnification and/or loss. To put it another way, the plaintiff's cause of action emerged only if and when he or she was damned and incurred losses. Now, it is true that the Chancery and/ The common law was amended by Chancery and Equity Court rulings holding that the promisee in an indemnity contract had a right to compel the promisor to fulfil his obligations through payments to creditors and third parties and/or deposits made in Court in anticipation of actions and proceedings which such creditors and third parties may take against the promise in the indemnity contract or Equity Courts viewed this view of the nature of indemnity contracts as harsh and insufficient to carry out the complete and true purpose of such contracts. The effect of the learned Judge's findings is that the above additional relief, which is afforded to a promise it was sufficient to determine that the law established by Chancery and Equity Court judgements in an indemnification contract was adequate to make a finding that the cause of action which would have accrued to such promise only upon being damned and suffering loss at common law, was not a separate cause of action. Despite the discussion in Gajanan Moreshwar v. Moreshwar Madam, it appears to me that there is no justification in holding against the plaintiff-indemnified promise that when he is in fact injured, he is without a new cause of action under the same indemnification contract damned and/or suffers loss under the same contract of indemnity. True, under the law of indemnity, as amended by Chancery and Equity Court rulings, a promise in an indemnity contract would give rise to a right of action for relief of directives that the promisor make payment to the third-party creditor, ensuring that the promise is never damned. True, the promise may seek relief from the deposit of the necessary amount in a court of law, allowing the promise to have the

deposited funds in hand for payment to the third-party creditor. The decisions of the Chancery Courts have led to a rising cause of action. The cause of action vested in the common law in a promise under an indemnity contract for enforcement of the indemnity contract's obligation by seeking a direct decree against the promisor has not been eliminated.

At common law, he was only entitled to such a decree if he was damned and suffered loss. Only when a person is damned and suffers a loss does this cause of action arise. The aforementioned views are in line with the Supreme Court's findings in the case of Shanti Swarup v. Munshi Singh.

ANALYSIS OF THE CASE OF SHANTI SWARUP v. MUNSHI SINGH[9]

Some of the plaintiff-respondents possessed land in Mahal Narain Singh Village, Khetalpur Sahruiya, as did other plaintiff-respondents' predecessor-in-interest. On May 9, 1914, they executed a simple mortgage on this property in favour of two individuals, Bansidhar and Khub Chand, for a value of Rs 12,000. Following that, on February 9, 1920, the owners (now represented by the plaintiff-respondents) executed a sale deed of half of the mortgaged property Shanti Saran, the first appellant, and three others, the other appellants, were successful. The amount owed on the mortgages for principal amount under the May 9, 1914 mortgage was Rs 16,000, of which Rs 13,500 was left with the purchasers for payment of the amount owed on the mortgages for principal and interest under the May 9, 1914 mortgage.

The purchasers took possession of the land, but neither they nor the appellants paid the mortgagees, who eventually sued the respondents to recover the amount owed to them under the mortgage. A final mortgage decree in their favour was issued on February 4, 1937, for a little more than Rs 26,000 in cash. Following that, the respondents filed an application under the Uttar Pradesh, the Special Judge allotted duty for the mortgage debt to the respondents and purchasers as half-owners of the mortgaged property under the Encumbered Estates Act. in an order dated May 22, 1939. The defendants and the appellants were each found responsible for Rs 14,307/9/6 as a result of this apportionment.

This order further said that the respondents would be required to pay interest at a rate of 6% per year on the amount due from August 1, 1933 to September 28, 1936, and then at a rate of

[9] Shanti Swarup V. Munshi Singh

412 percent per year thereafter. The Collector then filed for debt liquidation, and On January 30, 1943, the Collector ordered the applicants to execute a self-liquidating mortgage for three-fourths of a half of the property they owned. On February 25, 1943, the mortgage for Rs 20,803/4/3 was executed, and the applicants were required to hand over ownership of this portion of the property to the mortgagees.

The respondents then brought the complaint on which this appeal is based, seeking to recover compensation for the loss they suffered the consequences of the appellant's or his predecessors-in-failure interest's failure to discharge the original mortgage of May 9, 1914, they were awarded Rs 18,500 plus interest. This lawsuit was filed on July 30, 1943. The plaintiff alleged that they had actually suffered loss and damage as a result of the defendant's breach of trust on February 25, 1943, when they were obligated to implement the self-liquidating mortgage and give ownership of the land in the liquidation proceedings ordered by the Special Judge under the U.P Encumbered Estates Act.

It was argued on support of the petitioner- accused that the suit is time-barred. The plaintiffs-respondents claimed that their claim was for damages for a contract breached through the use of a registered instrument, so the limitation period was 6 years from date of the breach.

According to the trial court in 1920, the defendant-appellant promised to pay the mortgagees money, but did not do so in a reasonable time period. On the defendants objection, the court ruled in the appellant's favour. In the first instance, the division bench in the supreme court heard the defendant's appeal. It referred the matter of limitation to a Full Bench of five judges, who found that such suit was regulated by Article 83 read with Article 116 of the Limitation Act, so this time began running on February 25, 1943, the date on which the defendants were forced to enter a self-liquidating loan to settle the borrowings.

The Division Bench of the High Court dismissed the appeal after receiving the Full Bench's judgement and upheld the trial court's decision.

The question in this appeal is whether the Top Court was correct in preserving that the litigation is governed by Article 83 read in conjunction with Article 116 of the Limitation Act in the nature of the case, and whether the time limit began on February 25, 1943, the date on which the respondents were compelled to perform a self-liquidating mortgage.

Mr. B.C Misra argued on behalf of the appellant that a provision in a transfer in which the buyer promises to pay off a hindrance does not establish a contract of indemnity, that the appropriate article of the Limitation Act was Article 116, not Article 83, and that period began to run from the date on which the covenant to compensate the obstruction was separated. This argument cannot be accepted as valid. If a purchaser agrees in a transfer to clear an encumbrance on the sold property, Failure to do so by the buyer may result in two distinct civil actions. To start with, the seller does have the right to sue to have himself put into a position to satisfy the obligation which the buyer having failing to fulfil within the time period specified expressly or by implication if the purchaser fails to discharge the obligation within the time period specified expressly or by implication. In this situation, limitation will begin to run as Article 116 of the Limitation Act defines the period upon which buyer should really have paid the mortgage (or Article 115 if the sale deed is unregistered). In the second instance, If the seller sustains a loss in the event of the purchaser's inability to discharge the encumbrance, the vendor has the right to litigate under the indemnification contract. In the interest of the appellant, it was argued there was no such thing as specific obligation of indemnification in the completed sale deed in his favour on Feb 9, 1920. However, because the purchaser agreed that the contract of indemnification is implicit in this case to settle off of the pre-existing encumbrance on the house sold. **A contract of indemnity, as defined by Section 124 of the Indian Contract Act, is a contract in which one party promises to safeguard the other from loss caused by the promisor's or any other person's action.** A complaint based on an indemnity contract must be filed within 3 years of the petitioner being actually compensated, according to Article 83 of the Limitation Act. There really is no specific indemnity contract in this situation. However, we believe that the principles of Article 83 also apply in cases where the indemnity contract is implied rather than express.