Page 1419 - 1430 **DOI:** *https://doij.org/10.10000/IJLSI.112059*

INTERNATIONAL JOURNAL OF LEGAL SCIENCE AND INNOVATION

[ISSN 2581-9453]

Volume 6 | Issue 3

2024

Restraint in Legal Proceedings

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ABSTRACT

Indian Contract Act, section 28, talks about agreements made in restriction of legal proceedings being null. Basically it says that any such agreement that prohibits the parties from bringing a lawsuit to protect their rights is null and void to the extent it restricts them from bringing a lawsuit. In this section, however, there are two exceptions to the rule."

Only the first exception is discussed here. A contract between two or more parties whereby they agree that any dispute that may arise between them in respect of any subject or class of subjects shall be referred to arbitration, and that only the amount awarded in such arbitration shall be recoverable for the dispute so referred, is exempt from the provisions of the first exception. It can also be noted that arbitration is one of the possibilities supplied by the ICA to the parties. A double benefit is achieved. One being the hassle of going to courts and litigation can be avoided and secondly, this also reduces the burden on the courts."

When we look into the scope of this exception, it can be said that when the agreement between the parties provided that whatever award the arbitrators give shall be acceptable to them in every way without objection, it was held that the agreement could not be relied upon to shut objection even on the ground of misconduct to the arbitrators. However, this section does not apply to cases where there is no absolute restraint against enforcing the rights. Through this paper the author will be analysing the nature and objective of Section 28 of the Indian Contract Act, and the restrictive clauses included herein. This section of the ICA purposes to enforcement of the agreements in view of those clauses which restrict one party from having their rights enforced in the court of law and also to analyse agreements restricting law of limitations.

I. INTRODUCTION

Indian Contract Act, section 28, talks about agreements made in restriction of legal proceedings being null. Basically it says that any such agreement that prohibits the parties from bringing a lawsuit to protect their rights is null and void to the extent it restricts them from bringing a lawsuit. In this section, however, there are two exceptions to the rule.

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 [ISSN 2581-9453]

they agree that any dispute that may arise between them in respect of any subject or class of subjects shall be referred to arbitration, and that only the amount awarded in such arbitration shall be recoverable for the dispute so referred, is exempt from the provisions of the first exception. It can also be noted that arbitration is one of the possibilities supplied by the ICA to the parties. A double benefit is achieved. One being the hassle of going to courts and litigation can be avoided and secondly, this also reduces the burden on the courts.

When we look into the scope of this exception, it can be said that when the agreement between the parties provided that whatever award the arbitrators give shall be acceptable to them in every way without objection, it was held that the agreement could not be relied upon to shut objection even on the ground of misconduct to the arbitrators.[2] However, this section does not apply to cases where there is no absolute restraint against enforcing the rights.

II. SECTION 28 OF INDIAN CONTRACT ACT

Section 28 of the Indian Contract Act reads :

"Every agreement,—

(a) by which any party thereto is restricted absolutely from enforcing his rights under or in respect of any contract, by the usual legal proceedings in the ordinary tribunals, or which limits the time within which he may thus enforce his rights; or

(b) which extinguishes the rights of any party thereto, or discharges any party thereto, from any liability, under or in respect of any contract on the expiry of a specified period so as to restrict any party from enforcing his rights, is void to that extent."

This section of the ICA purposes to enforcement of the agreements in view of those clauses which restrict one party from having their rights enforced in the court of law. The English Law has a very famous saying to its account, "an agreement purporting to oust the jurisdiction of the courts is illegal and void on grounds of public policy" which explains this section. However, this section does not affect those agreements or contracts which have the option of referring to arbitration or out of the court settlements, but is applied to those which contain partially or wholly prohibit the parties from having a recourse from the court of law. A party cannot contract himself out of a clause to approach the courts in case of disputes or alter the period for arbitration in the Limitation Act. But a line of distinction has to be drawn between the absence of right and loss of remedy. Section 28 of the ICA shows that the cases in which the loss of remedy will destroy the right. On the other hand, the loss of a right indicates the

[2] "Abdul Majid v. Ch. Bahawal Baksh, AIR 1950 Lah 174."

disappearance of a remedy. The section aims at the prohibition of the agreements which would solely operate as long as the rights associated are in existence.

An agreement which embodies doubts arising out of a previous contracts between parties is in contradiction of this section because thereby the parties agree to abandon their rights under the original contract which necessarily include the right to resort to a civil court in regard of any conflict.

Agreements restricting Law of Limitation

The phraselogy of this section is explicit and strikes at the very root by declaring that any agreement curtailing the normal statutory period of Limitation would be void. The rationale is to ensure the protection against unfair dealing between unequal bargaining parties. The intention and objective being clear the Court's primary responsibility is to be construe and interpret it in a manner so as to advance the objective and protect the interest of the party who might be frustrated by too technical approach in the matters. Conditions which clearly and distinctly restrict the time period are the conditions under which suits brought are void. But, there is also a marked distinction between the condition which so limits the time within which a suit may be brought to enforce rights and one which provides that there shall be no longer any rights to enforce. Such a condition is not illegal in itself. A man may contract so far happening of a certain event he shall lose all his rights, such a condition is not an infringement of any of the provision of the Limitation Act. What this section prohibits is not to extinguish rights or liabilities of a party to a contract on the happening of a specified event but the limiting of the time within which a party may enforce his rights. A party will have no right to enforce, if the rights have already been extinguished under the contract. In such a case, there can be no question of the time for enforcement of the rights being limited.

One of the landmark cases of this aspect is the case of FCI v. New India Insurance Co. Ltd.[3], where a few rice millers had, one, entered into a contract with the FCI and, two, had obtained an infidelity insurance from an Insurance Company which had promised to keep the FCI indemnified in case of any breach of contract by the rice millers. Now this clause put the FCI in a position to claim directly against the concerned insurance company to recover the amount of loss. However, the liability of the insurance company to discharge the guarantee was subject to the restriction within 6 months from the termination of the contract. The court here, in this case, held that in construing the restriction adverted to in the clauses of the bond that the restriction only puts embargo on the right of the FCI to make its claim known not later than six

[3] "Food Corporation of India vs. New India Insurance Co. Ltd. , AIR 1994 SC 1889"

months from the date of termination of performance of the contract. But, if the clause of agreement is construed otherwise, it would hit section 28 of the ICA for imposing restriction to file a suit within 6 months from the day the performance of the contract is breached, thus the suit filed by the FCI for the enforcement of Fidelity Insurance was not restricted under the restriction in contracts. The amended provisions of sec 28 of the Contract Act are prospective in nature but contract entered into prior to the amendment and the conditions to the insurance policy are held to be liable.

However, in the case of Ailsa Craig Fishing[4], the court held that in construing an exemption that clauses of limitation are not regarded in the courts with the same hostility as clauses of exclusion; this is only because they must be related to other contractual terms.

Jurisdiction of Proper Courts

Where an agreement provides for ousting the jurisdiction of a court,, it is void but but does not have the effect of making the whole contract void but only that portion which relates to ouster the jurisdiction of a court. The section has no application when a party agrees to restrict a party to a contract from enforcing his rights under the contract in ordinary tribunal.[5] Where the parties enter into a contract restricting their rights to institute a suit except in particular courts, it must be strictly proved that the restriction pertains to proceedings in question. In deciding whther such restriction prevents either of the parties from filing a suit in another court regard must be had to the actual wording used in the contract.

In cases where the parties to the contract hail from two different locations, an agreement that only one of the two competent courts shall try the dispute is not contrary to public policy or does not go against the provisions of section 28. But where the parties agreed between themselves that for the purpose of litigation the contract should have been deemed to be entered in a place where neither of the parties belong the contract having been actually made elsewhere the contract was void and that the jurisdiction of the said court was invalid[6]. In a few cases, it has been held that the condition restricting the jurisdiction to a particular court alone does not in any way create a bar to the filing of a suit in the lower court.

A dealer of Tamil Nadu delivered to a carrier having its principle offices at Bombay and branch offices at various other places as subordinate offices. The dealer entrusted an assignment of goods to the carrier for delivery at Delhi. But the goods were kept at a godown at Delhi and the

[4] "Ailsa Craig Fishing Co. Ltd. V. Malvern Fishing Co. Ltd. [1983] 1 WLR 964."
[5] "Balwant Singh v. M. H. Siad Khan, AIR 1947 Pesh 48
[6] Bhagwandas Govardhan Das v. M/s Girdharilal Parshottamdas 1966 AIR 543"

same was destroyed and samaged by a fire as a result of which the assignee of the goods refused to take delivery. The dealer instituted a suit at a court within whose territorial jurisdiction the subordinate office of the carrier was situated wherefrom the goods were entrusted for transport for damages alleging that the fire was due to negligence and carelessness on the part of the staff of the carrier. It was held that the court having territorial jurisdiction over the subordinate office and shall alone have jurisdiction in respect of any cause of action and not at the principal place of business carrier.[7]

An agreement which seeks to curtail the period of limitation and prescribes a shorter period than that prescribed by law would be void as offending section 28 of the Contract Act. But there may be agreements which do not seek to curtail the time for enforcement of the right but which provide for the forfeiture of rights itself if no action is commenced within the period stipulated by the agreement. Hence, extinction of the right itself, unless exercised within a specified time is permissible and can be enforced.

However, where an ouster cause takes place, it is pertinent to see whether there is an ouster of a jurisdiction of other courts, where the clause is clear, unambiguous and specific accepted notions of contract which binds the parties unless an absence of ad idem can be shown.

III. EXCEPTIONS

Exception 1 and 2:

When the parties agree to submit their dispute to a domestic tribunal of their own choice, and when the arbitration is made a condition precedent to an action being brought it is prima facie the duty of the court to give effect to the agreement unless the condition precedent has been removed under the powers conferred on the Court by the Arbitration Act or unless the Curt comes to the conclusion that the right to arbitration has been waived[8]. However, a contract that stipulates that the decision of the arbitrator shall be final and conclusive and which thus bars the jurisdiction of the ordinary tribunals from the examining the validity of the award is void and, notwithstanding that clause, the courts would have jurisdiction to examine the validity of the award.[9]

As laid down in the case of ***Raj Emporium Handicrafts vs. Pan American World Airways***[10], an agreement by which a party is not absolutely restrained from enforcing all his rights under or in respect of the contract by the usual legal proceedings but is only restricted from enforcing

[7] "Patel Roadways Ltd., Bombay v. Prasad Trading Co., AIR 1992 SC 1514"
[8] "New Zealand Insurance Co. Ltd. vs Nagpal Hosiery Factory, AIR 1955 Punj (DB)
[9] Union Const. Co. (Pvt.) Ltd vs Chief Engineer, Eastern Command, AIR 1960 A11 72
[10] Raj Emporium Handicrafts vs. Pan American World Airways, AIR 1984 Del 396

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any such rights are not given to him by the arbitrator in the shape of money compensation is not forbidden by the said section. Garth CJ said, "If a contract were to contain a double stipulation that any dispute between the parties should be settled by arbitration, and that neither party should enforce his rights under it in a court of law, that would be a valid stipulation so far as regards its first branch, viz. that all disputes between the parties should be referred to arbitration because of itself would not have the effect of ousting the jurisdiction of the courts, but the latter branch of the stipulation would be void because by that the jurisdiction of the courts would be naturally excluded."[11]

In order to establish arbitration as a serious alternative, it has been laid down in several judicial precedents that when a case is undergoing the arbitration procedure, neither parties can approach the court for legal proceedings unless the arbitrators have heard and decided on the dispute. It has also been seen that, generally, that no agreement restricts the parties from absolutely approaching the court for legal proceedings, but the terms and clauses are framed in such a fashion that they render the need for legal proceedings unnecessary.[12]

For a clause providing for arbitration and declaring that the Arbitration Act would not apply was to be held to be void. The arbitration clause was held to be valid. The part which excluded the application of the Arbitration Act being severable from the rest of the agreement was alone struck down.[13]

Therefore, when correspondence has been exchanged between parties between the advocates that the disputes would be settled by the domestic tribunal selected by them then the court can direct the parties to get their disputes determined by the domestic tribunal selected by the advocate on the basis thereof. So there are sufficient grounds for the court to pass such an order because the exceptions to Sec 28 are attracted and such an order by the Court directing the parties to settle the disputes by the domestic tribunal selected by them is valid and proper.[14] However, where a contract reads that the decision of the arbitrator is final and conclusive, and that it further bars the power of the ordinary tribunal from examining the award granted in the due process is rendered void and, the Courts have the authority to examine the validity of the award.[15]

To decide as to whether this arbitration clause, which is the crux of the first exception of the section 28 of the Contract Act, has played any significant role in solving of disputes between

[11] Coringa Oil Co. vs. Koegler , (1879) 1 Cal 466, pp. 68"
[12] "Chapsey v. Gill, 7 Bom LR 805
[13] Rajasthan Housing Board vs. Engineering Projects (India) Ltd., AIR 2000 Raj 200.
[14] N.T.P.C Ltd. vs. Reshmi Construction, Builders and Contractors, AIR 2004 SC 1330.
[15] Supra note 3"

the parties amicably, it is required that the arbitration clause is binding on all parties in the first place. Because this is a provision accorded by a statue it is binding in all circumstances, regardless whether the process of arbitration was decided before drawing of the agreement or after the breach. In the general trend, there may be circumstances where the parties may claim that the contract has been breached and has no legal standing anymore, the arbitration stands rescinded. And this is sure to create hassles in a smooth problem solving process.

The answer to this supposition is that an arbitration clause remains binding on the parties even when the agreement has ended by a breach or whatever reason may be stated. Theoretically, there can be a possibility that a contract has come to an end but the arbitration clause has not come to an end, or there can be an instance where the entire contract is valid but just the arbitration clause is invalid. It has been held by the Supreme Court that expressions such as any dispute "arising out of" or "concerning" or "in connection with", or "in consequence of" or "relating to" the contract, are sufficiently wide enough to compel parties to refer even this matter to arbitration whether the contract is itself valid.[16]

International Arbitration can take place either within India or outside India in cases where there are ingredients of foreign origin relating to the parties or the subject matter of dispute. The law applicable to the conduct of arbitration and the merits of the dispute may be Indian law or foreign law, depending on the contract in this regard, and the rules of conflict of laws.[17]

Even if it has been established that this clause binds the parties, there are some conditions which are to be met with for this to happen. Firstly, for an arbitration agreement to exist, it is necessary that a contract must be first drawn up between the parties. Where a contract wasn't in existence, the clause of arbitration cannot be invoked. Secondly, a contract appointing an arbitrator is *uberrima fides* and a confidence clause is necessary between the tribunal and parties. The reason behind this that when the arbitrators, beforehand, have a prejudice regarding the issue, injustice is bound to happen and that in the first place defies the entire purpose of the provision. Thirdly, when the contract is void, the arbitration clause doesn't stand. A dispute arising from and founded on the basis of a contract that has been rendered void because of, say illegal object, or otherwise, every part of the contract including the arbitration part is also void. Fourthly, the award of the arbitration contract has to be in accordance with the public policy. Anything adverse to the same is considered to be void. Fifthly, the arbitration agreement has the same standing as any other contract, i.e. it is only invoked when it isn't tainted with fraud, misrepresentation, mistake and undue influence, in which case it can be avoided. However, a

[16] "Khardah Co. Ltd. vs. Raymon and Co. Ltd., (1963) 3 SCR 183 : AIR 1962 SC 1810.
[17] G.K.Kwatra in *Arbitraion and Contract Law in SAARC Countries*, pp. 18"

party who out of free consent accepts a clause regarding the arbitration which may be against his own interest, say the arbitrator is the employee of the defendant, cannot go back on his words and claim the agreement to be unenforceable.

When we look into the role played by this particular exception in helping the parties solve their disputes amicably, the contribution has been immense. There have been many cases involving banks, commercial set-ups, insurance companies where arbitration has been a rescue for them when it comes to settling down of issues rather than going for litigation, since it includes dealing with a huge number of clients. Supposedly if all these clients decide to file a case in the court, it will be very cumbersome for the defendants.

Exception 3:

This exception has been recently incorporated in this section in the year 2013. ***The Law Commission composing the 97th report***[18] contended that gatherings to an agreement ought not be permitted to endorse a technique which smothers the privileges of a gathering to make a case under the agreement keeping in mind doing as such, the Law Commission was cognizant that their proposal would run as opposed to the fundamental decide that gatherings to an agreement ought to be allowed to choose activity of their substantive rights. However, the Law Commission thought that it was important to meddle with the opportunity of agreement on the ground that unequal bartering force of contracting gatherings could realize out of line medicine on termination of rights.

This exception can be understood as an section which may not render unlawful an agreement in composing by which any bank or money related foundation stipulate a term in a guarantee or any contract making a provision for insurance for extinguishment of the rights or discharge of any party thereto from any obligation under or in appreciation of such guarantee on the expiry of a predefined period which is at the very least one year from the date of happening or non-happening of a predetermined occasion for extinguishment or release of such gathering from the said risk. This new procurement, the same number of would call attention to, now empowers a bank or money related organization to confine the time inside which an assurance must be conjured by a recipient, with the end goal it should be respected. Given that time confinement conditions are not one of a kind to bank ensures; this new special case raises a worry with regards to the enforceability of restriction procurements found in different

[18] *"Law Commission Report No. 97- Section 28,Indian Contract Act,1872 https://www.latestlaws.com/library/law-commission-of-india-reports/law-commission-report-no-97-section-28indian-contract-act1872"*

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contracts.

As it were, this move to give extra solace to banks could be risky from different viewpoints. First off, the special case does apply to an assurance as well as applies to any agreement of a bank making a procurement for certification. Maybe unintended however an outcome of the new correction is that a bank may now have the capacity to repudiate obligation as for a whole understanding inasmuch as such an assention imagine an assurance (paying little respect to the underwriter). Aside from clear established concerns emerging with such a methodology, the change raises questions about enforceability of confinement procurements found in different contracts. Illustratively, constraint of guarantee cases is a vital element of an offer buy contract. Likewise, in numerous development contracts, impediment statements are assembled requiring the proprietor of an undertaking to bring a case inside stipulated time. The move to change Section 28 would demonstrate that so far as the administrators are concerned, such confinement procurements are to fall since they abhor security of the late revision.

IV. CONCLUSION

LARSEN & Toubro Limited & Anr. vs Punjab National Bank & Anr. 28 july 2021

- Exception 3 to Section 28 of the Contract Act deals with curtailment of the period for the creditor to approach the court/tribunal to enforce his rights. It does not in any manner deal with the claim period within which the beneficiary is entitled to lodge his claim with the bank/guarantor.

Hon'ble Highcourt has clearly demarcated difference between –

1. As an established contract term that gives a period of grace beyond the period of validity of the guarantee for the Bank to request a default that has happened during the validity period, the claim period has been explained.
2. This claim term is not covered under section 28 of the Contract Act. It concerns the creditor's entitlement to exercise his claim under the bank guarantee in the event of a guarantee's refusal to pay before the relevant court.

Court further observed; "may now deal with another plea raised by the respondents, namely, that the **issue of prescribing the bank charges and the period for retention of security are matters of contract and this court cannot interfere in such contractual matters** especially as they are not contrary to any rules or regulations or stipulations framed by RBI."

This ruling has far reaching implications.

1. Banks may revise their proforma bank guarantee to provide for the suitable clause to take benefit of **"Exception 3 to section 28 of the Contract Act,"**

2. Banks may revise their proforma counter indemnity guarantee / application of the corporate debtor to provide for retention of margin money &/or security till such time the liability of bank is subsisting under **"Exception 3 to section 28 of the Contract Act,"**

3. IRP/RP to examine the claim of bank for bank guarantee in CIRP, in light of the rulings in this judgement.

As discussed earlier, sec 28 of the ICA talks about how blanket clauses like total restriction in seeking remedies in court for any breach of contract is void. However, the contract stands void only and up till the clause which renders it void. This section aims on preventing the infringement of rights of the man.

There are two aspects to this section of the Indian Contract Act which are given quite a lot of importance, and that is the law of limitation and the jurisdiction of proper courts. In the law of limitation, it basically seeks to protect any unfair treatment of one of the parties, where they are barred from approaching the court for remedies just because they were restricted by the time clause providing so. The courts have over a long precedence of cases, have set a standard time which caters to this particular aspect of this section. However, if the parties decide to decide on a time which exceeds the limitation period, that is fine and valid held by the courts. Then, we discuss the jurisdiction of proper courts. Apart from the tribunal or the court pre-decided on by the parties, the places from where the contract was finalized upon or the places from where the parties hail is also considered to be under the ambit of the exercising jurisdiction and are not barred merely because they were not mentioned in the contract clause.

We then discussed the topic of arbitration as an alternative to restraint in legal proceedings, it can be safe to assume that whenever the parties to contract decided to refer to a third unbiased party to settle any dispute arising out of the said contract, they are said to have entered into an arbitration agreement. These types of agreements can be entered into either while drawing up the contract or after the contract has been breached, the only quintessential to this is that there must have been a legal and existent contract. And the first and second exceptions, talk about questions pertaining to the issue of arbitration that arise before and after the contracts have been drawn. This new addition to this section, as exception 3 renders the same number of would call attention to, now empowers a bank or money related organization to confine the time inside which an assurance must be conjured by a recipient, with the end goal it should be respected.

 [ISSN 2581-9453]

Given that time confinement conditions are not one of a kind to bank ensures; this new special case raises a worry with regards to the enforceability of restriction procurements found in different contracts. Being relatively young, this section has drawn a lot of flak and criticism from the academicians.

Thus, we can draw the conclusion that section 28 of the Indian Contract Act, any restriction in legal proceedings renders the contract void. This acts as a great help to the people who are at a disadvantageous position in terms of technical grounds or something similar. Also the law of limitation is a great boon for the public which panders to the public which does not have adequate or required legal help or knowledge, the jurisdiction of courts is a very wide ambit that is to be taken in consideration in cases of a trial. This renders a great help for both the courts and the jury trying the case.

Also, it has also been seen that this process has been great help for the Indian Judiciary, since out of court settlements, or as we call it arbitration has reduced the stress on the judiciary by minimizing the number of cases that could have arose in situations where a single defendant can be sued by numerous plaintiffs, say in examples of banks, insurance companies, government undertakings, and many such cases. Plus, on a personal level it reduces the entire hassle of any individual who could be involved in a court proceedings. And also the clause pertaining to the banks, are a great help in some aspects, since they help the people who suffer a technical disadvantage.

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 [ISSN 2581-9453]