

## Proposed Amendment in Section 28 of The Contract Act, 1872

### **Introduction**

Any undertaking between two individuals or groups of individuals results in a contract. From morning till evening, day in and day out, we might have entered into innumerable contracts like purchasing vegetables from a vendor, buying a ticket to watch a movie or getting a piece of work done. Every human relationship is built upon a contract. Communities and nations coexist on the basis of a viable contract. Thus, we see contract as an inherent and underlying part of every human transaction. It is a binding agreement to get something done, sold or bought and there may be a price or a consideration - implied or explicit.

A contract, in simple words, is a binding legal agreement that is enforceable in a court of law. That is, a contract is an exchange of promises for the breach of which the law will provide a remedy. The law relating to contracts is to be found in the Contract Act 1872. The law of contracts differs from other branches of law in a very important respect. It does not lay down so many precise rights and duties which the law will protect and enforce; it contains rather a number of limiting principles, subject to which the parties may create rights and duties for themselves, and the law will uphold those rights and duties. Thus, we can say that the parties to a contract, in a sense make the law for themselves. So long as they do not transgress some legal prohibition, they can frame any rules they like in regard to the subject matter of their contract and the law will give effect to their contract.

As per s. 2(h) of the Contract Act 1872, a contract is an agreement enforceable by law. Section 10 of the Contract Act deals with the relation between a contract and an agreement. As per s. 10, "All agreements are contracts if they are made by the free consent of the parties competent to contract, for a lawful consideration and with a lawful object, and are not hereby expressly declared to be void." Every contract is an agreement, but every agreement is not a contract. An agreement becomes a contract when the following conditions are satisfied:

1. There should be some lawful consideration for it.
2. The parties must be competent to contract.
3. The consent of the parties is free.
4. Their object is lawful.

An important requirement for the formation of a valid contract is that the parties must contract for a lawful object. An agreement the object of which is opposed to the law of the land maybe either unlawful or simply void, depending upon the provision of the law to which is opposed. Sections 23 of the Contract Act deal with unlawful agreements. Section 2(g) of the Contract Act deal with void agreements. As per s. 2(g), "An agreement not enforceable by law is void." The following agreements are declared to be void:

1. Agreement of which consideration and objects are unlawful in part.
2. Agreements without consideration.
3. Agreements in restraint of marriage.
4. Agreements in restraint of trade.
5. Agreements in restraint of legal proceedings.

6. Unmeaning agreements.
7. Wagering agreements.
8. Agreements to do impossible acts.

The Contract draws distinction between an agreement which is only void and the one in which the consideration or object is also unlawful. An illegal agreement is one which is actually forbidden by the law; but a void agreement may not be forbidden, the law merely say that if it made, the courts will not enforce it. Thus every illegal contract is also void but a void contract is not necessarily illegal.

Through this report, I would like to enlighten the readers on agreements in restraint of legal proceedings which are declared to be void by the law as per s. 28 of the Contract Act 1872. I will be discussing various aspects of s.28 with the help of various case laws.

### **Agreements in Restraint of Legal Proceedings**

It is a well known rule of the English law that “an agreement purporting to oust the jurisdiction of the courts is illegal and void on grounds of public policy.” Thus, any clause in an agreement providing that neither party shall have the right to enforce the agreement by legal proceedings is void. Agreements stipulating no intention to contract or a gentleman's agreement which is an agreement that relies upon the honour of the parties for its fulfilment, rather than being in anyway enforceable by law is not in violation of s.28.

Section 28 of the Contract Act renders void two kinds of agreement, namely:

1. An agreement by which a party is restricted absolutely from enforcing his legal rights arising under a contract by the usual legal proceedings in the ordinary tribunals.
2. An agreement which limits the time within which the contract rights may be enforced.

Section 28 of the Contract Act 1872 states that:

“Every agreement, -

1. 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

2. which extinguishes the right 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.

Exception 1 - Saving of contract to refer to arbitration dispute that may arise. - This section shall not render illegal a contract, by which two or more persons agree that any dispute which 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 in respect of the dispute so referred.

Exception 2 - Saving of contract to refer questions that have already arisen - Nor shall this section render illegal any contract in writing, by which two or more parties agree to refer to

arbitration any question between them which has already arisen, or affect any provision of any law in force for the time being as to references to arbitration.

### **Restraint of Legal Proceedings**

An agreement having for its object the restraint of an individual from enjoying the fundamental right of resorting to a court of law for redress and relief is invalid. Section 28 applies to agreements that wholly or partially restrain this right of the parties. A contract having a clause that no action should be brought up on it is void since it restricts both parties from enforcing their rights under the contract in a court of law. An agreement by a servant not to sue for wrongful dismissal is invalid; so is a condition restraining a transferee from enforcing his rights under the transfer in anyway. Take the case of a covenant in a separation deed providing that the wife would not apply to the divorce-court for maintenance, shall be void as being contrary to public policy. Similarly, a special agreement between an advocate and his client that the latter would not be sued for fees shall be void under this section.

It should be noted that an agreement, whereby the parties to a suit bind themselves before the judgement is passed in the court of first instance, to abide by the decree of that court and forego their right to appeal, is valid and binding. An agreement by which the parties agreed to a procedure to be adopted in a court deciding a case on merits and consenting that the decision will be binding on them was equivalent to providing that no right of appeal will be exercised. An agreement whereby a judgement-debtor engaged himself not to appeal against him in consideration of the judgement-creditor giving him time for the satisfaction of the judgement-debt is not prohibited by this section. The agreement not to appeal, for which the indulgence granted by the respondents was a good consideration, the appellant did not restrict himself absolutely from enforcing a right under or in respect of any contract. He forewent his right to question in appeal the decision which has been passed by an ordinary tribunal. Such an agreement is in our judgement prohibited neither by the language nor the spirit of the Contract Act, and an appellate court is bound by the rules of justice, equity, and good conscience to give effect to it and to refuse to allow the party bound by it to proceed with the appeal.

However, a clause in an arbitration agreement providing that the award shall be accepted by the parties and any objection thereto shall be null and void and shall not be put forth in any court of law shall be void as imposing a restriction on the right of the party affected to institute legal proceedings.

### **Limitation of Time**

An agreement which provides that a suit should be brought for the breach of any terms or agreement within a time shorter than the period of limitation prescribed by law is void. The effect of such an agreement is absolutely necessary to restrict the parties from enforcing their rights after the expiration of the stipulated period, though it may be within the period of the limitation. According to the Limitation Act, 1908, an action for breach of contract may be brought within three years from the date of the breach. Hence, a such contract is void under s.28 of the Contract Act.

Cases sometimes occur where parties agree to extend the period of limitation. No provision is made the section for agreements extending period of limitation for enforcing rights under it. There is hardly any doubt that an agreement which provides for a longer period of limitation than the law allows does not lie within the scope of this section. There is no restriction imposed upon the right to sue; on the contrary, it seeks to keep the right to sue subsisting

even after the period of limitation. It would, however be void under s.23, as tending to defeat the provisions of the Limitation Act 1908, s.3 which provides that every suit instituted after the period of limitation prescribed by the act shall be dismissed, although limitation has not been set up as a defence. Thus, contracts extending the period of limitation are void under section 23, as defeating the provisions of the Limitation Act.

### **Agreement Relating to Release or Forfeiture of Rights**

Under s.28 of the Contract Act in 1997, agreements reducing the period of limitation are distinguished from those which did not limit the time within which a party might enforce his rights, but which provided for a release or forfeiture of rights if no suit was brought within the period stipulated in the agreement. Under s.28, limiting the time for enforcing the rights is void. But a term in the contract that rights accruing thereunder to party would be forfeited or released, if the party did not sue within such short a time as given in the contract, would not fall within s.28. Clauses of this kind are usually found in policies of insurance.

In our opinion a clause providing that no suit shall be brought against the company in connection with the said later policy than one year after the time when the cause of action accrues is valid. The justification in this regard is that the effect of the agreement was not to limit the time but to provide for surrender of rights if no action was brought within that time. Such a clause is not hit by s.28 and is valid. The curtailment of the period of limitation is not permissible in view of S. 28 but extinction of the right itself unless exercised within a specified time is permissible and can be enforced. If the policy of insurance provides that if a claim is made and rejected and no action is commenced within the time stated in the policy, the benefits flowing from the policy shall stand extinguished and any subsequent action would be time barred. Such a clause would fall outside the scope of S. 28 of the Contract Act.

Rights to be enforced under the contract should continue to exist even beyond the shorter period agreed for enforcing those rights, to make such an agreement void under S.28. If, for example, beyond the shorter period agreed upon the rights under the contract cannot be kept alive, no limiting of the time to enforce the rights under the contract arises and hence the agreement putting a time limit to sue will not be hit by S.28. So, a condition in a contract that the rights thereunder accruing to a party will be forfeited or released if he does not sue within a time limit specified therein will not offend S.28. This is because, as per the contract itself, the rights accrued to the party cease to exist by the expiry of the limited period provided for in the contract. In such a case, in effect, there is no limiting of the time to sue. So, an agreement which provides for a simultaneous relinquishment of rights accrued and the remedy to sue for them will not be hit by S.28. But, at the same time, an agreement relinquishing the remedy only, by providing that if a suit is to be filed that should be filed within a time limit-the time limit being shorter than the period of limitation under the Limitation Act - will be hit by S.28. This is because the rights accrued continue even beyond the time limit as the same is not extinguished. In such a case, there is really a limiting of the time to sue prescribed by the Limitation Act. A clause contained in guarantee that the liability of the bank will be alive only for a period of six months after the expiry of the period of duration of the guarantee. Which is also specified in a Clause that the plaintiff's rights under the guarantee will also be forfeited by the end of that six months. There is an extinction of the right of the plaintiff under the contract and a discharge of the defendants from liability. So, the time limit imposed in such Clause cannot be hit by S.28 of the Contract Act.

Clauses found in insurance policies providing that the insurer should not be liable for loss or damage after expiration of twelve months from the happening of loss or damage unless a claim was subject to pending action or arbitration or clauses in bills of lading excluding

liability for loss or damage unless the plaintiff brought a suit within one year from date of delivery did not violate s.28. In short, an agreement providing for the relinquishment of rights and remedies was valid, and an agreement for the relinquishment of remedies only fell within the mischief of s.28.

### **The Proposed Amendment**

The proposed amendment of s.28 shall bring about the change that all clauses which reduced the normal period of limitation would be void to that extent. It'll prohibit clauses which seek to extinguish the right of any party thereto, or discharge 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.

Such clauses hinged not on the interpretation of the section, but on the construction of the contract, and that the principle itself is well recognised that an agreement providing for the relinquishment of rights and remedies is valid but an agreement for relinquishment of remedies only falls within the mischief of s.28, and no change was necessary in the section as it stood earlier.

By giving a clause in an agreement that shape and character of a provision extinguishing the right and not merely affecting the remedy, a party standing in a superior bargaining position can achieve something which could not have been achieved by merely barring the remedy. The amendment is also justified on the ground that it was necessary to make the law simpler. The the existing provision is illogical, based on a distinction too subtle.

The proposed amendment shall have a purpose, especially in contracts of insurance. This will ensure that the claims under the policy are made early, investigated promptly, thereby avoiding the likelihood of loss of important evidence. If claims were not made early, the insurers might be unable to meet a fraudulent claim.

### **Agreements Prescribing Jurisdiction**

S. 28 makes void only those agreements which absolutely restrict a party to a contract from enforcing the rights under that contract in ordinary tribunals. But this section has no application when a party agrees not to restrict his right of enforcing his rights in the ordinary tribunals but only agrees to a selection of one of those ordinary tribunals in which ordinarily a suit would be tried. Parties cannot by agreement confer jurisdiction on courts to try suits not cognizable under the ordinary law. The principle that the parties cannot by consent confer jurisdiction on a court or deprive a court of jurisdiction has been stated to apply to cases of inherent jurisdiction of a court over the subject matter of the suit, and the question of territorial jurisdiction as not being a question of inherent jurisdiction. Where, thus, two courts have jurisdiction to try a case, there is nothing contrary to law in an agreement between parties that disputes between them should be tried at the one court rather than the other.

If such contract is clear, unambiguous and explicit and not vague, it is not hit by this section. But an agreement, however cannot confer jurisdiction on the court which has no jurisdiction at all to entertain the suit; and if the court mentioned in the contract has no jurisdiction at all, the jurisdiction of other courts is not barred. Such a clause restricting jurisdiction applies also to proceedings in courts under the arbitration law.

Although, it is open to the parties to agree that dispute relating to their contract will be subject to the jurisdiction of courts in a particular territory, to the exclusion of other courts, the parties who make their choice of tribunal will be bound by it, the enforcement in Pakistan

of such contracts is not imperative where the choice restricts them to a foreign court. But a Pakistani citizen making a contract while in Pakistan would not be able and cannot be permitted to avoid the applicability of the Pakistani law to the contract made in Pakistan or to be performed in part or whole of Pakistan. Where the option was exercised in bi-lateral agreement between parties to exclude Pakistani Courts. Although the parties lived in Connecticut, United States of America. They are very much having jurisdiction there and it is not as if the petitioner and the respondent are going to permanently reside in Pakistan. It was also manifestly shown that their inclination and intention was only to reside in United States of America. Hence, there is nothing wrong in the contract to have chosen except the Courts in Pakistan; thereby including the Courts in United States of America. Where the bill of lading provided that all disputes would be judged in the USSR according to the Merchant Shipping Code of the USSR. The plaintiff sued the shipping company at Karachi. The claim was small, the shipping company had its agents at Madras, and there was no difficulty in collecting facts and applying the law there. While holding that the courts in Karachi had jurisdiction, the court observed that in case of foreign jurisdiction clause, the question is not so much of freedom of contracts, and the parties are bound by their choice as of expediency in the light of what may be called the rule of convenience and the ends of justice in the particular circumstances of the case. It is open to the Court to consider the balance of convenience, the interest of justice and the circumstances when it decides the question of jurisdiction of the court in the light of the clause in the agreement between the parties choosing one of the several courts or forums which were available to them. Indeed, such a consideration is essential in the interest of international trade and commerce for the better relation between the countries and the people of the world.

The choice regarding the jurisdiction of courts should be clearly unambiguous and explicit. The party invoking the clause must strictly prove that the restriction applies to the proceedings under consideration. It is also necessary that important terms of this nature must be specifically brought to the notice of the parties whose rights are sought to be curtailed. The law requires that before making a person bound by any such clause in the agreement as to exclusive jurisdiction, it must be proved that the same was brought to the knowledge of the consignor in such a way that it should seem to be the result of a mutual assent. Where the original contracting party has been adequately informed, it will be a question of fact in each case whether the parties subsequently acquiring his rights will also be bound by the notified terms.

A contract between the parties with regard to the exclusion of jurisdiction of a court is not binding on a third party, unless the attention of such third party is specifically drawn to such a clause in the contract and he is made aware of the implications. Thus, where the suit was filed in the court at Lahore by the insurance company for recovery of damages for short delivery of goods which were delivered at Lahore, it was held that in absence of any evidence that the insurance company who was a third party was made aware of the implications of the lorry receipt and since no part of cause of action had arisen in Karachi, it was not open to say that the suit could be filed only in the court in Karachi as stipulated in the lorry receipt.

## **Exceptions**

### **Exception 1: Reference of Future Disputes to Arbitration**

This exception applies to contracts where the parties have agreed that no action shall be brought until some question of amount has been decided by the arbitrators. Thus, clauses are saved by this exception. The former refers to term in the contract which provides that, in the

event of a dispute arising, it shall be referred to arbitrators whose award shall be a condition precedent to any right of action in respect of the matters agreed to be referred is valid. It is a clause which requires as a condition precedent of the accrual of any cause of action that the arbitrator shall have made in an award. The latter clause is the one which provides that no claim shall arise, unless it is put forward in writing and an arbitrator appointed within a limited period. 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, that all disputes between the parties should be referred to arbitration, because that 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.

In order to conform to this exception, the jurisdiction of the courts must be excluded in all respects except in the matter which is the result of the arbitrator's award. This section does not forbid action for damages for breach of such agreement to refer to arbitration. A lawful agreement to refer a matter to arbitration can be made a condition precedent before going to the courts, and it does not violate s.28. All such cases have to be decided according to the Arbitration Act, 1940. A clause providing for arbitration and declaring that the Arbitration Act would not apply shall be void. The arbitration clause shall be valid. A clause in an agreement that except where otherwise provided in contract the decision of the superintending engineer shall be final, conclusive binding and upon certain matters therein mentioned does not constitute him an arbitrator and the clause is not contrary to s.28 of the Contract Act and is not hit by s.21 of the Specific Relief Act. It is also possible to contemplate an agreement appointing one of the contracting parties as an arbitrator for matters arising out of a contract. The decision given by such a person is binding on the party and no party can be heard to say that such decision is not binding being a decision by a person in his own cause, unless it can be shown to be arbitrary or otherwise unjust. The parties can also question the finality of such a decision despite any agreement.

It is also recommended that an amendment to the exception of substitute the words 'the parties will be bound by the award' for the words 'only the amount awarded in such arbitration shall be recoverable.' This clause was repealed by the Specific Relief Act 1877. Section 21 of that Act, and following new Section s.19-A of the Specific Relief Act should be added:

*'Save as provided by the Arbitration Act 1940, no contract to refer present or future differences to arbitration shall be specifically enforced; but if any person who had made such a contract other than an arbitration agreement to which the provisions of the said Act apply and has refused to perform it sues in respect of my subject which he has contracted to refer, the existence of such contract shall bar the suit.'*

### **Exception 2: Reference of Existing Question to Arbitration**

The exception saves any contract in writing by which two or more persons agree to refer for arbitration any question between them which has already arisen, though such a contract would now also be dealt with by the law relating to arbitration.

Resolution of disputes is governed by Arbitration Act, 1940 under which parties may by means of an agreement in writing to refer to arbitration disputes which have arisen between them in a contract. Where the parties agreed to refer their disputes to arbitration, they were held to be bound to do so. Certain excuse will not be enough to nullify the arbitration when the parties had accepted the agreement with full conscience. If a suit is filed in the same

subject matter as the arbitration agreement, the party desirous of reference to arbitration may apply to the court seeking reference, which the party must do before submission of the first statement of substance or dispute in the court. If the suit is in the same matter as the arbitration agreement, the court shall refer the parties to arbitration. The Arbitration and Conciliation Act 1996 allows discretion to the court in referring the matter. Section 77 of that act provides that the parties shall not initiate, during the conciliation proceedings any arbitral or judicial proceedings in respect of a dispute that is the subject matter of the conciliation proceedings except where such proceedings are necessary to preserve his rights.

## Conclusion

Agreements restraining legal proceedings are against public policy as it acts as a hindrance to the dispensation of justice. It places one of the parties to a contract in a more advantageous position than the other. Section 28 of the Indian Contract Act 1872 has corrected this imbalance and has been successful in ensuring that justice is served in the society.

<b>Proposed Amendment</b>	<b>Existing Provision</b>
<p><b>28. Agreements in restraint of legal proceedings, void</b></p> <p><i>Every agreement, -</i></p> <p><i>(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</i></p> <p><i>(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.</i></p> <p><i>Provided that this section shall not render illegal a contract in writing by which any bank or financial institution stipulate a term in a guarantee or any agreement making a provision for guarantee for extinguishment of the rights or discharge of any party thereto from any liability under or in respect of such guarantee or agreement on the expiry of a specified period which is not less than one year from the date of occurring or non-occurring of a specified event for extinguishment or discharge of such party from the said liability.</i></p> <p><b>Exception 1:</b> <i>Saving of contract to refer to</i></p>	<p><b>28. Agreements in restraint of legal proceedings void.</b> - <i>Every agreement, 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, is void to that extent.</i></p> <p><b>Exception 1.- Saving of contract to refer to arbitration dispute that may arise.</b> --<i>This section shall not render illegal a contract by which two or more persons agree that any dispute which 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 in respect of the dispute so referred.</i></p> <p><b>Suits barred by such Contracts.</b> --<i>When such a contract has been made, a suit may be brought for its specific performance, and if a suit, other than for such specific performance, or for the recovery of the amount so awarded, is brought by one party to such contract against any other such party in respect of any subject which they have so agreed to refer, the existence of such contract shall be bar to the suit.</i></p> <p><b>Exception 2.</b> --<i>Saving of contract to refer questions that have already arisen.</i> -- <i>Nor shall this section render illegal any contract</i></p>



*arbitration dispute that may arise: This section shall not render illegal contract, by which two or more persons agree that any dispute which may arise between them in respect of any subject or class of subject shall be referred to arbitration, and that only the amount awarded in such arbitration shall be recoverable in respect of the dispute so referred.*

**Exception,2:** *Saving of contract to refer questions that have already arisen: Nor shall this section render illegal any contract in writing, by which two or more persons agree to refer to arbitration any question between them which has already arisen, or affect any provision of any law in force for the time being as to references to arbitration.*

*in writing, by which two or more persons agree to refer to arbitration any question between them which has already arisen, or affect any provision of any law in force for the time being as to references to arbitration.*