

NOTES AND COMMENTS

UNCONSCIONABLE CONTRACTS: A CRITICAL ANALYSIS OF INDIAN LEGAL SYSTEM

Unconscionable terms of the contract are those contracts in which, one party is strong and other party is weak but it do not come into purview of any of the terms and conditions mentioned in the Indian Contract Act, 1872. Thus courts have taken resort to different statutes to interpret the unconscionability in different forms of the statutes, to make the condition justifiable towards the weaker society. The paper have the insights how the unconscionable terms in the contracts are dealt with in India in absence of the explicit provisions relating to it and also how the protection is given by the Indian courts in such cases. The Unconscionable contract are those contracts, which no man in his senses and not under delusion, would make on the one hand, and which no fair and honest man would accept on the other. If a contract or term thereof is unconscionable at the time the contract is made a court may refuse to enforce the contract, or may enforce the remainder of the contract without the unconscionable term, or may so limit the application of any unconscionable term as to avoid any unconscionable result.

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¹ *UNCONSCIONABLE CONTRACT OR TERM* Available at:
http://www.lexinter.net/LOTWVers4/unconscionable_contract_or_term.htm
(Accessed: 10 November 2015 1:00 PM).

contracts, which no man in his senses and not under delusion, would make on the one hand, and which no fair and honest man would accept on the other.²In the landmark case of *Water Inland Company*, it has been laid down by the Hon'ble Judges of the Apex Court that it means those contracts wherein the situation is such that the weaker party's obtaining of goods and services or means of livelihood is only and strongly governed by the acceptance of terms imposed by the stronger party. Such a situation leaves the former party with only the choice of either to take it or to leave it.³ That devoid of the person from the bargaining power he has in the contract and thus makes the contract a source for the person to get exploited from the other party. Thus it is the reason the courts have to take the rigid view of the things and just devoid the people from exercising such uncluttered power, which can well be a source of the abuse.

In *Brojo Nath Ganguly*⁴ case, a question was posed that as to under which head would an unconscionable bargain be covered. If it fell under the head of undue influence it would render a contract voidable or else if it fell under the heading of being opposed to public policy, it would be void.⁵

Statutory Provisions Relating To Contracts

To fully understand the concept of unconscionability in Indian contract law, one must examine specific provisions of three different statutes. These include sections 14, 16, and 19A of the Indian Contract Act of

² Garner, B. A. (2011, Ed. 9) 'Unconscionable contract or term', *Black's Law Dictionary*, West Publishing Company.

³ *Central Inland Water Transport Corporation and Anr. v. Brojo Nath Ganguly and Anr.*, A.I.R.1986 SC 1571.

⁴ *Ibid.*

⁵ Network, L. E. N., (2015) *Unconscionable bargain in Indian law.*, Available at: <http://www.legalera.in/student-news-articles/item/12254-unconscionable-bargain-in-indian-law.html> (Accessed: 8 November 2015, 3.20P.M.).

1872; section 20 of the Specific Relief Act of 1963; and section 111 of the Indian Evidence Act of 1872.⁶

(1) Free Consent Section 14 of the Indian Contract Act of 1872 defines free consent as consent not caused by (1) coercion, as defined in section 15;

(2) Undue influence, as defined in section 16;

(3) Fraud, as defined in section 17;

(4) Misrepresentation, as defined in section 18; or

(5) Mistake, subject to the provisions of sections 20, 21, and 22

In other words, consent exists when there is no evidence of coercion, undue influence, fraud, misrepresentation, or mistake. The only relevant provision in the Indian Contract Act, 1872, which talks about the inequality of bargaining power as between parties and of the unfair advantage by one party over the other, is laid under Sec. 16 of the Act, which deals with 'undue influence'. It is only a combination of procedural and substantive unfairness.⁷ Undue Influence Section 16 of the Act defines undue influence in the following manner:

(1) A contract is said to be induced by undue influence where the relations subsisting between the parties are such that one of the parties is in a position to dominate the will of the other and uses that position to obtain an unfair advantage over the other.

(2) In particular and without prejudice to the generality of the foregoing principle, a person is deemed to be in a position to dominate

⁶ Sarin, M. L. (1992) 'Contract Unconscionability in India', *Loyola of Los Angeles International and Comparative Law Review*, 14(1), pp. 569–580.

⁷ Law Commission of India, 199th Report.

*the will of another: (a) where he holds a real or apparent authority over the other, or where he stands in a fiduciary relation to the other; or (b) where he makes a contract with a person whose mental capacity is temporarily or permanently affected by reason of age, illness, or mental or bodily distress.*⁸

*(3) Where a person who is in a position to dominate the will of another enters into a contract with him, and the transaction appears, on the face of it or on the evidence adduced, to be unconscionable, the burden of proving that such contract was not induced by undue influence shall lie upon the person in a position to dominate the will of the other.*⁹

Illustrations (a) A, having advanced money to his son, B, during his minority, upon B's coming of age obtains, by misuse of parental influence, a 1992] Loy. LA. Int'l & Comp. L.J[bond from B for a greater amount than the sum due in respect of the advance. A employs undue influence. (b) A, a man enfeebled by disease or age, is induced by B's influence over him as his medical attendant to agree to pay an unreasonable sum for his professional services. B employs undue influence. (c) A, being in debt to B, the money-lender of his village, contracts a fresh loan on terms [that] appear to be unconscionable. It lies on B to prove that the contract was not induced by undue influence. (d) A applies to a banker for a loan at a time when there is stringency in the money market. The banker declines to make the loan except at an unusually high rate of interest. A accepts the loan on these terms.

This is a transaction in the ordinary course of business, and the contract is not induced by undue influence. 3. Power to Set Aside Contracts Induced by Undue Influence According to section 19A of the Act,

⁸ Singh, N. (2004) *Business laws*. 1st edn. New Delhi: Deep & Deep Publications, India., Pg 130.

⁹ *The Indian contract act, 1872*

when consent to an agreement is obtained by undue influence, the agreement is voidable at the option of the party whose consent was obtained. The contract may be set aside, either absolutely, or, if the party entitled to void it has received a benefit, upon such terms and conditions as the court deems just. a. Illustrations (a) A's son has forged B's name to a promissory note. B, under threat of prosecuting A's son, obtains a bond from A for the amount of the forged note. If B sues on this bond, the court may set the bond aside. (b) A, a money-lender, advances Rs. 100 to B, an agriculturist, and, through undue influence, induces B to execute a bond for Rs.200 with interest at six percent per month. The court may set the bond aside; ordering B to repay the Rs. 100 with such interest as may seem just.¹⁰

It is equity which intervenes in cases of harsh and unconscionable bargains such as in laws relating to penalties, forfeitures and mortgages. The Supreme Court of India has concluded that the doctrine is based substantially on the principles of English common law.¹¹ In the leading case of Tate v. Williamson,¹² Lord Chelmsford explained the doctrine of undue influence.

“Whenever two persons stand in such a relation that, while it continues, confidence is necessarily reposed by one, and the influence which necessarily grows out of that confidence is possessed by the other, and this confidence is abused, or the influence is exerted to obtain an advantage at the expense of the confiding party, the person so availing himself of his position will not be permitted to retain the advantage,

¹⁰ *Ibid.*

¹¹ *Ladli Prasad Jaiswal v. Kamal Distillery Co.*, [1964] 1 S.C.R. 270, 300 (India).

¹² [1866] 2 Ch. App. 55 (Eng.).

*although the transaction could not have been impeached if no such confidential relation had existed.”*¹³

Standing Of Indian Legal System

The doctrine of undue influence applies to transactions that prima facie reveal an unfair advantage to one party and those in which an unfair advantage is adduced from the evidence.¹⁴ Section 16 contemplates moral coercion, in contrast to the physical coercion found in section 15 of the Act. Only a person who is a party to the contract can raise the plea of undue influence and seek relief under section 16.¹⁵ On account of *U.Kesavulu Naidu v. Arithulai Ammal*¹⁶ it was held that until and unless it was demonstrated that the agreement was made under undue impact, no aid would be allowed on the ground of unconscionable nature of an agreement, which demonstrates the non-recognition of the idea of unconscionable deal. We have to differentiate between the two most important things that if the contract can be just revoked on the basis of undue influence or it can be made voidable only. This condition is made clear by the famous case of *Brojo Nath Ganguly*.

In *Brojo Nath* case, the guidelines of the organization expressed the plan under which a representative could acknowledge the work of the enterprise or in option, leave the employment and along these lines get a small sum by method for pay. It was additionally said the administrations could be ended by outfitting a notification three months before end. The applicant tested this guideline as violative of Article 14 of Constitution of India since his occupation was additionally finished in the same way. This principle was a piece of agreement, which was

¹³ *Ibid.*

¹⁴ *Supra Note 11* on 14, Pg 301.

¹⁵ Subhas Chandra Das Mushib, [1967] 1 S.C.R. at 331.

¹⁶ *U.Kesavulu Naidu v. Arithulai Ammal*, [1912] I.L.R. 533 (Mad.).

charged to be out of line, unfair and absurd. The best a portion of this case was that the request was not documented on the grounds of fraud, coercion or misrepresentation. The court had decided for this situation that the standard of unconscionable statements would be accessible where the disparity between the gatherings was an aftereffect of circumstances. In this manner it unmistakably specified that there need not be any former connection between the two gatherings, which is as requested by sub-order. (1) Under Sec.16. Thus it separates the idea of undue impact and unconscionable deal, in this manner leaving space for making a different procurement for managing the cases including unconscionable deal. This is done in light of the fact that the substantive injustice in the event of unconscionable deal is subjective to diverse circumstances, which is further reliant upon the position of the gatherings.

Section 16(3) of the Act shifts the burden of proof from one party to the other when a contract is facially unconscionable and the other party is proven to have dominated the will of the former. A similar but more widely applicable rule is contained in section 111 of the Indian Evidence Act of 1872. Section 111 of the Indian Evidence Act of 1872 states that when a question exists as to the good faith of a transaction between parties, one of whom stands in a position of active confidence to the other, the party who is in the position of active confidence has the burden of proving good faith.¹⁷ The party asserting unconscionability need not produce direct evidence of actual undue influence the court presumes undue influence under the assumption that the stronger, more influential party used his or her superior bargaining position to obtain an advantage over the weaker party.

¹⁷ *Ibid.*

From the afore mention. d principles it can be resolved that one party must be at a severe disadvantage to the other party to contract, the weakness thus being exploited by the stronger party in some morally culpable manner which renders the resultant transaction overarching and oppressive.¹⁸

The Specific Relief Act of 1963 specifies the remedies available to a party, including specific performance, rescission, and cancellation. Judicial Discretion in Granting Specific Performance Section 20 of the Specific Relief Act of 1963 discusses the court's discretion in granting specific performance. Mere inadequacy of price is not a sufficient hardship so as to refuse the plaintiff specific performance¹⁹. The sorts of agreements to which such rule applies are not those agreements which are sullied by unlawfulness but rather applies to those agreements containing terms so unjustifiable and nonsensical, as to stun the still principals of the Court. Such types of contract have no regard for what is wrong or right thus are performed by the will of the one party and this is absolutely clear from the impact. It is irreconcilable with what is right or reasonable.²⁰ The guideline of value was additionally used to set aside brutal or unconscionable contracts for administrations which were rendered by vassals in trouble or unconscionable contracts which included hopeful beneficiaries, wherein a cash bank offered trade to the beneficiary out return for the property which the last anticipated that would acquire, along these lines getting such property at a gross underestimate. It is also violative of certain constitutional fundamental rights provided in constitution of

¹⁸ Delhi Transport Corporation v. DTC Mazdoor Congress and Ors, A.I.R.1991 S.C. 101.

¹⁹ Lakshminarayana, 1963 A.I.R. (Madras) at 24; see also Ramakrishna v. Palaniappa, 1963 A.I.R. (Madras) 17.

²⁰ Balmer Lawrie and Co. Ltd. and Ors. v. Partha SarthiSen Roy and Ors.,[2013] 8 S.C.C. 345.

India. The court had decided for this situation that the rule of unconscionable conditions would be accessible where the imbalance between the two litigating parties was an aftereffect of circumstances. Along these lines it plainly specified that there need not be any earlier connection between those two litigating parties, which is as requested by sub-clause (1) under Sec.16 of Indian Contract Act. Subsequently it separates the idea of undue influence and unconscionable deal, along these lines leaving space for making a different procurement for managing the cases including unconscionable deal. This is done in light of the fact that the substantive unfairness, if there should arise an occurrence of unconscionable deal is subjective to diverse circumstances, which is further subordinate upon the position of the two parties.

In India, the Supreme Court pronouncements in litigations like *Brojo Nath Ganguly*²¹, *Balmer Lawrie*²², *Delhi Mazdoor*²³, *Ferro Alloys*²⁴ and *Phulchand Exports*²⁵ have been in relation to a party contracting with the state, usually a contract involving employment, and the contract being in violation of Article 14 and Sec. 23 of the Indian Contracts Act, 1872, which talks about contracts against public policy.

Thus this type of contract is also seen in the eyes of the law in the violation of the Article 14 also. As been held in various cases thus it is also in the violation of the freedom ensured by the Constitution of India to its citizens. Such a security is additionally given against the activity

²¹ *Supra* Note 3 at 21.

²² *Supra* Note 20 at 22.

²³ *Delhi Transport Corporation v. DTC Mazdoor Congress and Ors*, [1991] A.I.R. 101 (S.C.)

²⁴ *Ferro Alloys Corporation Ltd. v. AP State Electricity Board and Anr.* A.I.R.1993 SC 2005.

²⁵ *Phulchand Exports Ltd. v. OOO Patriot*, [2011] SCALE 475 (S.C.)

of the state where the Courts have decided that that the activity of the State in contractual field likewise must be reasonable and sensible. The prerequisite of Article 14 of the Constitution ought to augment even in the circle of contractual matters for directing the behavior of the State action. Materialness of Article 14 to every official activity of the State being settled, the State can't cast of its identity and activity unbridled force free by the necessities of Article 14 in the circle of contractual matters and case to be administered in that just by private law standards relevant to private people whose rights stream just from the terms of the agreement without much else. It is not as though the prerequisites of Article 14 and contractual commitments are outsider ideas, which can't exist together. Hence, add up to avoidance of Article 14 non-intervention which is fundamental to administer of law - from State activities in contractual field is not supported. This is all the more so when the advanced pattern is likewise to inspect the absurdity of a term in such contacts where the dealing force is unequal so that these are not arranged contracts but rather standard type of agreements between unequal's. Acquiring the State movement contractual matters likewise inside of the domain of legal survey is inescapable.

But on the other hand if we see the that the concept of the unconscionable terms is mostly applied to the standard form of contract or where there are contract for employment or for the various other general and standard contracts done by any company but there has been no major case law in the Indian courts in which the issue is decided between the two private parties. So in India until now there has been no instance where the two private parties has entered into the contract and courts has to cancel that contract due to the presence of the such unconscionable terms. The law of agreement has in late time to confront an issue, which is accepting new measurements. The issue has

emerged out of the current substantial scale and far reaching routine of closing contracts in institutionalized structure. Individuals upon whom such exclusion statements or standard structure contracts are forced scarcely have any decision or option however to follow. This gives an interesting chance to the titan organization to misuse the shortcoming of the person by forcing upon him terms, which may go to the degree of exempting the organization from all obligations under contract. It is essential and legitimate that their advantage ought to be secured. The courts have thusly concocted a few standards to secure the enthusiasm of such persons. The Indian court had been of view that generally the Standard form of the contract which are tilted towards one party and are not the neutral as a whole. But through tools of checking the unconscionable terms of contract, the courts have ensured that one party is not exploited to the larger extent. Mainly in the case of the employer and employee relationship where one has to ultimately accept the conditions. Thus that contract cannot be called as free contract but it is always seen.

The courts rightly held in *Superintendence Company of India (P) Ltd v. Sh. Krishan Murgai*,²⁶

"It is well settled that employees covenants should be carefully scrutinized because there is inequality of bargaining power between the parties; indeed no bargaining power may occur because the employee is presented with a standard form of contract to accept or reject. At the time of the agreement, the employee may have given little thought to the restriction because of his

²⁶ AIR 1980 SC 1717. See also § 2-302. *Unconscionable contract or clause*, Available at: <https://www.law.cornell.edu/ucc/2/2-302> (Accessed: 12 November 2015, 4:30 P.M.).

eagerness for a job; such contracts "tempt improvident persons, for the sake of present gain, to deprive themselves of the power to make future acquisitions, and expose them to imposition and oppression."

Reflection of The Courts

Two types of the unconscionability of contract are there Procedural and substantive. In India procedural has been well defined and deliberated upon. A contract or a term is procedurally unfair if it has resulted in an unjust advantage or unjust disadvantage to one party on account of the conduct of the other party,²⁷ or the manner in which or the circumstances under which the contract has been entered into or the term thereof has been arrived at by the parties.²⁸

While in India the Substantive Unconscionability has been one which is less deliberated upon even by the courts. It is well define in the Michigan legislature, It states that If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract²⁹, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.³⁰ The courts have at many instances have struck down the clauses which are unfair and seems to be in category of Unconscionable terms. at the point when one side is in an extraordinarily solid and in summoning

²⁷ Nilima Bhadbhade, Contract Law in India, Wolters Kluwer law and business Publications, Ed. 1 ,2010, Pg.132.

²⁸ Recommendation of Law Commission of India, 199 Report.

²⁹ § 2-302. *Unconscionable contract or clause*, Available at: <https://www.law.cornell.edu/ucc/2/2-302> (Accessed: 12 November 2015, 4:30 P.M.).

³⁰ Uniform Commercial Code (Act 174 of 1962), Section 2.302.

position and the other, a truly frail side, go into an understanding for exchange of a property for a thought which is tangibly low and horribly insufficient, and even a typical man won't waver for a minute to remark that the weaker party has been completely tricked. In such a case the courts won't allow the solid party to push the weaker party to divider.

The courts have struck down the penal clause in various cases. Law is well-settled that a penal stipulation to pay the sum agreed on breach of contract cannot be enforced.³¹ Similarly, if the court finds that the real purpose for which a stipulation has been incorporated in the contract is that by reason of its burdensome or oppressive character it may operate in *terrorem* over the promisor so as to drive him to fulfill the contract, then the provision will be held to be one by way of penalty.³²

Also courts on various instances have just stricken down the variation clauses which appeared to the court that are favoring a one party.³³ At the other instance the courts has awarded the escalation for delay despite non-existence of escalation clause.³⁴ Indeed, even without an escalation statement in an agreement, the courts have permitted pay as heightening in costs on the ground that once it is found that postpone in execution of the agreement because of the behavior.³⁵ Where a condition in an agreement gives that a temporary worker needs to present a no claim authentication before any installment is made it him, the courts have held that such a statement would not suspend him from getting his cases settled upon through discretion if the endeavor was

³¹ Michel Habib, Raji Ayoub v. Sheikh Suleiman El Taji El Farouqui, AIR 1941 PC 101.

³² K.P. Subbarama Sastri v. K.S. Raghavan, AIR 1987 SC 1257 see also P.K. Achuthan v. State Bank of Travancore, Calicut, AIR 1975 Ker 47 (FB).

³³ S. Harcharan Singh v. Union of India, (1990) 4 SCC 647

³⁴ Anurodh Constructions v. DDA, 2005(3) RAJ 252 (Del)

³⁵ P.M. Paul v. Union of India, 1989 Supp (1) SCC 368

given under undue imp. t.³⁶ But on the other hand there have been the matters where the Supreme Court has just given a green signal to lot of one sided clauses in the contract of general nature³⁷ and matters that of the Arbitration.³⁸ The legal patterns saw above; obviously demonstrate a disparity of perspectives amongst the judgments. From one perspective are the dynamic judgments striking down uncalled for statements, though then again are judgments entirely deciphering uneven states of agreement. Thus, there is a need and need to formalize the law through a sanctioning to avoid inconsistency in judgments and law and keeping in mind the end goal to ensure the residents against out of line terms even in business contracts. In such manner the proposals of the Law Commission are extremely useful.

Conclusion

Basic test of "unconscionability" of contract is whether under circumstances existing at time of making of contract and in light of general commercial background and commercial needs of particular trade or case, clauses involved are so one-sided as to oppress or unfairly surprise party. Courts of equity did not share the reluctance of common law courts to police bargains for substantive unfairness.³⁹ Though mere "inadequacy of consideration" alone was not a ground for

³⁶ Jiwani Engineering Works (P) Ltd. v. Union of India, AIR 1981 Cal 101; See also Ambica Construction v. Union of India, (2006) 13 SCC 475, Bharat Coking Coal Ltd. v. Annapurna Construction, (2003) 8 SCC 154, State of Orissa v. Larsen & Toubro Ltd., AIR 2005 Ori 183, State of Orissa v. Larsen & Toubro Ltd., AIR 2006 Ori 45, Municipal Corp. of Greater Mumbai v. Jyoti Const. Co., 2003(3) Arb LR 489 : 2004(1) RAJ 165 (Bom).

³⁷ Ramnath International Construction (P) Ltd. v. Union of India, (2007) 2 SCC 453 See also Ch. Ramalinga Reddy v. Superintending Engineer, (1999) 9 SCC 610; Associated Engineering v. Government of A.P., (1991) 4 SCC 93.

³⁸ Executive Engineer vs Gangaram Chhapolia, (1984) 3 SCC 627: AIR SC 234 See Also, Russell on Arbitration, 17th Ed, p. 174.

³⁹ Pali, V. (2013) *Law related to standard form of contracts - corporate/commercial law - India*. Available at: <http://www.mondaq.com/india/article.asp?articleid=272948> (Accessed: 18 November 2015, 11.00 A.M.)

withholding equitable relief, a contract that was "inequitable" or "unconscionable" one that was so unfair as to "shock the conscience of the court" would not be enforced in equity.⁴⁰

After all this it can be safely concluded that India there are no separate law for the unconscionable terms of the contract unlike other countries in the world. The development have been there but it has been through the various pronouncements of the judges, thus there has been quite variation in those standings and thus has become very subjective to the courts to decide. In India also, the subject has been hotly debated over the years and the Law Commission, through its 103rd Report (1984) and 199th Report (2006), has suo motu published findings on this issue and recommended changes in the existing laws to guard against unconscionable clauses of contract. But so far nothing has fructified and the Legislature has not acted upon any of the said reports.⁴¹ Thus safeguard the interest of the various parts of the society it is the need of the day that our legislatures and policy makers have to go ahead and make a concrete law on it. So that the subjectivity in this part of law can disappear and the things can be rightly placed for the justice.

Rishabh Srivastava⁴²

Angad Ahuja⁴³

⁴⁰ *Ibid.*

⁴¹ P. C., Markanda, N. and Markanda, R. Markanda, *Unconscionable clauses in Construction Contracts*, Available at: <https://www.google.co.in/url?sa=t&rct=j&q=&esrc=s&source=web&cd=9&cad=rja&uact=8&ved=0ahUKEwia0JvYtZ7JAhXKRi4KHx4dDRMQFghSMAG&url=http%3A%2F%2Fcfiindia.com%2Fwp-admin%2Fdocuments%2FUnconscionable%2520Clauses%2520in%2520Construction%2520Contracts.docx&usq=AFQjCNGvDtSr45EsQzgJA1fcW8YUyY1gsg&bvm=bv.108194040,d.c2E> (Accessed: 20 November 2015, 5.00PM).

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⁴³ 8th Semester, BBA LLB(Hons.), Instiute of Law Nirma University