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Wayne Courtney

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## INDEMNITIES AND THE INDIAN CONTRACT ACT 1872

—Wayne Courtney\*

The Indian Contract Act, 1872 (“the Act”) contains several provisions that define the nature of a contract of indemnity and the rights of the promisee under it.<sup>1</sup> In English law the rules governing contracts of indemnity are largely a product of case law; statute affects only some aspects, most notably indemnity insurance. This is true also of a number of jurisdictions with a common law heritage, such as Australia, Canada, New Zealand and Singapore. The purpose of this article is to compare and contrast the treatment of contracts of indemnity under Indian law with that under English law and other uncodified jurisdictions around the Commonwealth. Indemnity insurance, with its statutory complications in various jurisdictions, can conveniently be put to one side. The focus is on contracts of indemnity as they exist in other contexts. Drawing upon developments in England and other uncodified jurisdictions, I will also make some observations about the indemnity reforms proposed by the Law Commission of India in its Thirteenth Report on the Indian Contract Act (“the Report”).

To begin, some history. By 1872, when the Act came into force, the English law on contractual indemnities could be said to have reached a stage of late adolescence or early adulthood. In the common law courts the basic nature of the claim on an indemnity had been established. Courts of equity also exercised a jurisdiction to enforce contracts of indemnity. The origins of that jurisdiction are murkier, though its nature was somewhat clarified by a raft of decisions in the 1860s and 1870s concerning transfers of shares in companies on the London Stock Exchange.<sup>2</sup>

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\* Faculty of Law, University of Sydney.

<sup>1</sup> Sections 124 and 125, Indian Contract Act, 1872. Sections 77 and 78 of the Malaysian Contracts Act, 1950 are in almost identical terms.

<sup>2</sup> See *Evans v. Wood*, (1867) LR 5 Eq 9; *Shepherd v. Gillespie*, (1867) LR 5 Eq 293 [affirmed *Shepherd v. Gillespie*, (1868) LR 3 Ch App 764]; *Hodgkinson v. Kelly*, (1868) LR 6 Eq 496; *Hawkins v. Malthy*, (1868) LR 6 Eq 505 [affirmed *Hawkins v. Malthy*, (1869) LR 4 Ch App 200]; *Cruse v. Paine*, (1869) LR 4 Ch App 441; *Castellan v. Hobson*, (1870) LR 10 Eq 47; *Nickalls v. Merry*, (1875) LR 7 HL 530. Similar principles developed where the shares were held on trust: *National Financial Co. ex p Oriental Commercial Bank, In re*, (1868) LR 3 Ch App 791; *Hardoon v. Behlilos*, 1901 AC 118 (PC).

Other features of the modern law were absent or inchoate. There was no real theory of construction of contracts of indemnity. The concept of the ‘scope’ of an indemnity, which is an integral part of modern thinking, was applied intuitively. Many contractual indemnities, express or implied, were set-pieces in particular contractual relationships: a principal might indemnify an agent; the drawer of an accommodation bill of exchange might indemnify the acceptor against liability upon it<sup>3</sup>, the assignee of a lease might indemnify the immediate assignor against loss arising from the assignee’s non-performance or non-observance of covenants in the lease.<sup>4</sup> Those examples still remain relevant, but indemnities nowadays are far more sophisticated devices and are used in a wider variety of contexts. Contracts may have detailed liability regimes involving exclusions, indemnities and insurance provisions. Promises of indemnity are often combined with guarantees in banking or financial instruments. Questions of enforcement have become more challenging: can an indemnity be enforced so as to protect third parties? How do common law rules on remoteness or mitigation of damage affect claims on indemnities? It is also probably fair to say that our understanding of contractual construction and scope has advanced considerably.<sup>5</sup>

So far as it reflected the then-prevailing English law on indemnities, the Act was in some respects deficient and in others ahead of its time. The Act does not, for example, describe the rights of the promisor.<sup>6</sup> It says little about enforcement by the promisee except in relation to lawsuits and compromises. Even there, it does not refer to equitable enforcement. Such deficiencies are not necessarily an obstacle as the Act is not treated as an exhaustive statement of the law of indemnity.<sup>7</sup> Gaps have been filled by later Indian case law developments. On the other hand, the Act was more forward-looking in its use of the concept of scope. Section 125 opens by referring to acts by the promisee “*within the scope of his authority*” and Section 125(1) refers to “*any matter to which the promise of indemnity applies*”. Sections 125(1) and 125(3) also settled the position of a promisee who is adjudged liable or who compromises an alleged liability. These points were unsettled in English law when the Act came into effect and the controversy remains unresolved.

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<sup>3</sup> See *Reynolds v. Doyle*, (1840) 1 Man & G 753 : 133 ER 536; W. Courtney, CONTRACTUAL INDEMNITIES, 6-10 (Hart Publishing, 2014).

<sup>4</sup> See note 34 and following.

<sup>5</sup> But see *Velugoti Sarvagna Kumara Krishna Yachendra Bahadur Garu v. Sobhanadri Apparao Bahadur Zamindar Garu*, (1948-49) 76 IA 120 : AIR 1949 PC 234.

<sup>6</sup> But see *Maharana Shri Jasvatsingh Fatesingji v. Secy. of State for India*, ILR (1890) 14 Bom 299; *SBI v. Moti Thawardas Dadlani*, (2007) 109 Bom LR 483.

<sup>7</sup> See *Gajanan Moreshwar Parelkar v. Moreshwar Madan Mantri*, AIR 1942 Bom 302; *Khetarpal Amarnath v. Madhukar Pictures*, AIR 1956 Bom 106.

## I. DEFINITION OF INDEMNITY

### A. The subject for analysis

Section 124 defines a contract of indemnity as: “*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*”. At the outset we must be clear about the concepts of ‘contract’ and ‘indemnity’. The definition given in Section 124 is, in one sense, incomplete: a contract is bilateral in character yet the definition accounts only for one party’s obligations and, even then, only for one type of obligation. The expression ‘contract of indemnity’ is sometimes used in the English cases in a more specific sense, to describe a contract in which the only, or only substantial, executory promise of one party is to indemnify another.

However, the basic point is that the proper subject of analysis is a *promise* of indemnity in a contract, not a *contract* of indemnity. A contract of indemnity, in the specific sense just mentioned, can then be approached in much the same way as a promise of indemnity that is merely one of many terms in a contract dealing with a larger subject-matter. Perhaps for this reason, the technical distinction between a contract of indemnity and a promise of indemnity appears not to have troubled the Indian courts. Indeed, Sections 124 and 125 also refer to the ‘promisor’ and ‘promisee’ and Section 125(1) refers to the ‘promise to indemnify’. The same mixed usage can be found in other jurisdictions.

The term ‘indemnity’ is elastic and may be used more generally to describe any arrangement under which a party is not to suffer loss. A distinction must be drawn between two kinds of ‘indemnity’ arrangements: first, those in which the essential concern of the undertaking is to protect the promisee exactly against loss; secondly, those in which the essential concern of the undertaking is not of that nature, though the promisee is incidentally or effectively indemnified against a loss. This article, and Sections 124 and 125, are concerned with the former arrangements. These are promises of indemnity in the strict sense. Usage of ‘indemnity’ in the latter sense is, nonetheless, quite common. It might be said that A’s payment of damages for breach of a contract with B, of an amount equal to B’s loss or B’s liability to another, ‘indemnifies’ B,<sup>8</sup> or that A’s guarantee to B provides an ‘indemnity’ to B against default by a third party, C,<sup>9</sup> or that A’s promise to B to pay C, a creditor of B, effects an ‘indemnity’ against B’s liability to C.<sup>10</sup>

<sup>8</sup> See *A. Krishnaswami Iyer v. Thatha Raghaviah Chetti*, AIR 1928 Mad 43; *Birmingham and District Land Co. v. London and North Western Railway Co.*, (1886) 34 Ch D 261, 276 (CA) (Fry, LJ); *Addis v. Gramophone Co. Ltd.*, 1909 AC 488, 491 (HL) (Lord Loreburn, LC); *Wertheim v. Chicoutimi Pulp Co.*, 1911 AC 301, 307 (PC); *Lexmead (Basingstoke) Ltd. v. Lewis*, 1982 AC 225, 273 : (1981) 2 WLR 713 : (1981) 1 All ER 1185 (HL) (Lord Diplock); *AMEV-UDC Finance Ltd. v. Austin*, (1986) 162 CLR 170, 194 (Mason and Wilson, JJ).

<sup>9</sup> *Harburg India Rubber Comb Co. v. Martin*, (1902) 1 KB 778, 784 (CA) (Vaughan Williams, LJ); *Bofinger v. Kingsway Group Ltd.*, 2009 HCA 44 at para 7.

<sup>10</sup> *Wren v. Mahony*, (1972) 126 CLR 212, 227 (Barwick, C.J.).

## B. Scope of triggering events

The range of indemnities contemplated by Section 124 is much narrower than the English common law conception of indemnity, even in the limited sense I have just described. When read in conjunction with Section 125, which addresses actions against the indemnified party, it seems that the principal concern was with promises to indemnify against claims by or liabilities to third parties. This is, perhaps, not surprising in light of the historical development of indemnity contracts. Even in the late nineteenth century, most of the reported English cases concerned indemnities in this general form or, more specifically, indemnities against the promisor's breach of contract where such breach was likely to lead to a claim by a third party against the promisee.

From a theoretical perspective the choice of activating events is rather puzzling. Focusing on the activity of natural or juristic persons excludes losses caused by natural events, as are often the subject of contracts of indemnity insurance. Limiting the relevant actor to the promisor or third party is conceptually untidy. It is entirely possible, although perhaps not very common outside of insurance, for A to indemnify B against losses caused by B's own conduct. It is also possible for an indemnity from A to B to apply to losses attributable to concurrent causes, being acts or omissions of A, B and others. The definition would lead to some difficult questions of characterisation. Fortunately, by accepting that the statute is not exhaustive, these definitional problems seem not to have posed any serious obstacles to the development of Indian law.

Another limitation which has been suggested is that Section 124 of the Act covers only express promises of indemnity. Whether or not that interpretative gloss is correct,<sup>11</sup> implied indemnities have readily been recognised under Indian law.<sup>12</sup> In that respect the Law Commission's recommendation<sup>13</sup> to insert the words 'expressly or impliedly' after 'promises' in Section 124 is sensible and consistent with the case law. By way of comparison Section 145 explicitly refers to an implied promise by a principal debtor to indemnify the surety.<sup>14</sup> Earlier in its Report the Law Commission referred to an 'implied contract' of indemnity.<sup>15</sup> An

<sup>11</sup> In its Report, the Law Commission [at page 50] merely indicated that the amendment to the Act should 'provide clearly' that a promise of indemnity could be implied.

<sup>12</sup> *Partab Singh v. Izzat-Un-Nisa Begam*, ILR (1909) 31 All 583 (PC); *Tilak Ram v. Surat Singh*, AIR 1938 All 297; *Shanti Swarup v. Munshi Singh*, AIR 1967 SC 1315 : (1967) 2 SCR 312. As to whether *Secy. of State for India v. Bank of India Ltd.*, (1938) 2 All ER 797 (PC) actually involved an implied contract of indemnity, see note 53.

<sup>13</sup> The Report, at 84.

<sup>14</sup> Of course, there can also be an express promise from the debtor to indemnify the surety. Query whether there is a difference in result if an indemnified surety enters a reasonable compromise of a disputed claim by the creditor that was, in fact, invalid in law. *But see* Sections 125(3) and 145 ('rightfully paid'). See *Raghavendra Gururao Naik v. Mahipat Krishna*, AIR 1926 Bom 244; *Tarachand Lakhmichand Chuhan v. Gopal Lachiramkumar*, AIR 1959 MP 297. *But see* Courtney, *supra* note 4, at paras 6-35.

<sup>15</sup> The Report, at 48.

implied promise of indemnity may well appear in an implied contract, but it is important to recognise that the two concepts are distinct.

In some situations the contract itself is ‘implied’ or inferred from the circumstances. Illustrations in English law include: where a party accepts an accommodation bill of exchange upon the drawer’s request<sup>16</sup>; where a guarantor provides a guarantee to the creditor upon the debtor’s request<sup>17</sup>; and, in some cases at least, where one party requests another to perform some act which turns out to be injurious to the rights of a third party.

It is also possible for a promise of indemnity from A to B to be implied as a term into an *express* contract between A and B. This has been offered as one explanation in English law for the agent’s (B’s) indemnity from the principal (A), at least where the agency is contractual.<sup>18</sup> The owner, B, of a vessel under charter may undertake that the master will comply with directions given by the charterer, A, as to employment of the vessel or signature of bills of lading. Often there is an express indemnity from the charterer to the owner against the consequences of compliance with such orders; in the absence of an express term, a term may be implied.<sup>19</sup> Other instances are where an employer, B, is rendered vicariously liable for a tort committed by a negligent employee, A<sup>20</sup>; and in some circumstances where A promises B to perform precisely the same obligations B already owes to C.<sup>21</sup> These are all common law illustrations. An indemnity may also take the form of a contractual term implied by a statute.<sup>22</sup>

### C. Other obligations that resemble contractual indemnities but are not

The examples given above are contractual in nature. Obligations to indemnify arise in various other ways beyond the law of contract, whether by operation of the common law (including equity) or under statute.<sup>23</sup> Lord Wrenbury explained in *Eastern Shipping Co. Ltd. v. Quah Beng Kee*:<sup>24</sup>

<sup>16</sup> *Reynolds v. Doyle*, (1840) 1 Man & G 753 : 133 ER 536; *Yates v. Hoppe*, (1850) 9 CB 542.

<sup>17</sup> *A Debtor, In re*, 1937 Ch 156 : (1937) 1 All ER 1 (CA).

<sup>18</sup> P Watts and FMB Reynolds, *BOWSTEAD & REYNOLDS ON AGENCY*, paras 7-58 (19th edn., Sweet & Maxwell, 2010). *But see* Sections 222 and 223 of the Act.

<sup>19</sup> *Telfair Shipping Corpn. v. Inersea Carriers SA*, (1985) 1 WLR 553 : (1985) 1 All ER 243; *Triad Shipping Co. v. Stellar Chartering & Brokerage Inc. (The Island Archon)*, (1994) 2 Lloyd’s Rep 227 at 237 (CA) (Evans LJ). *See* note 44.

<sup>20</sup> *Lister v. Romford Ice and Cold Storage Co. Ltd.*, 1957 AC 555 : (1957) 2 WLR 158 : (1957) 1 All ER 125 (HL).

<sup>21</sup> *Hornby v. Cardwell*, (1881) 8 QBD 329 at 337 (CA) (Brett, LJ); *Birmingham and District Land Co. v. London and North Western Railway Co.*, (1886) 34 Ch D 261, 277 (CA) (Fry, LJ); *Travers v. Richardson*, (1920) 20 SR (NSW) 367 (SC). *See* Courtney, *supra* note 4, at paras 10-7, 10-10–10-13.

<sup>22</sup> *See* note 34.

<sup>23</sup> *A. Krishnaswami Iyer v. Thatha Raghaviah Chetti*, AIR 1928 Mad 43.

<sup>24</sup> *Eastern Shipping Co. Ltd. v. Quah Beng Kee*, 1924 AC 177 at 182-83 (PC).

“A right to indemnity generally arises from contract express or implied, but it is not confined to cases of contract. A right to indemnity exists where the relation between the parties is such that either in law or in equity there is an obligation upon the one party to indemnify the other. There are, for instance, cases in which the state of circumstances is such that the law attaches a legal or equitable duty to indemnify arising from an assumed promise by a person to do that which, under the circumstances, he ought to do. The right to indemnity need not arise by contract; it may (to give other instances) arise by statute.”

Different sources of indemnity can overlap. In English law, for example, a surety’s right to indemnity from the principal debtor can be justified in at least three ways: (1) on equitable grounds; (2) on an express or implied<sup>25</sup> *genuine* contract of indemnity; or (3) on the basis of unjust enrichment, deriving from cases brought using the old form of action for money paid by the plaintiff to the defendant’s use. Contemporary understanding of the law of obligations is more sophisticated and so we can perceive differences in these juristic bases that were not fully appreciated at the time of the Act.<sup>26</sup>

Care must, therefore, be taken in seeking analogies with some of the old English decisions, particularly those where the result could be justified on the basis of a real contract or, in the alternative, by a fictitious contract which supported a right to recoupment (‘indemnity’) on a basis that would now be labelled unjust enrichment. To illustrate the dangers, I take as an example a passage from the judgment of Willes J in *Roberts v. Crowe*<sup>27</sup>, which is referred to in Pollock and Mulla’s leading treatise on the Indian Contract Act.<sup>28</sup> Willes J observed that, where shares were sold and then subject to calls, the liability of the (unregistered) transferee to the transferor was ‘exactly analogous’ to the case of assignee and lessee. In each case the latter was liable for the former’s failure to perform, but the latter had a right to be recouped against the former. There then follows a quote from Willes J’s judgment in *Moule v. Garrett*.<sup>29</sup> Undoubtedly, the two situations share common elements: responsibility for the liability is thought properly to rest with the person who has the benefit of the property, even though the other may be liable and have to pay first. But the juristic analysis can be quite different.

<sup>25</sup> *A Debtor, In re*, 1937 Ch 156 : (1937) 1 All ER 1 (CA).

<sup>26</sup> Rough parallels might be drawn: between (1) and Section 145 of the Act (insofar as Section 145 allows the surety to obtain relief before payment: *S.K. Mohideen Batcha Sahib v.K.A. Sheik Dawood Sahib*, AIR 1926 Mad 1035; *Sripatrao Sadashiv Uppe v. Shankarrao Sarnaik*, AIR 1930 Bom 331; between (2) as it concerns implied indemnities and Section 145; and between (3) and Section 69 of the Act.

<sup>27</sup> *Roberts v. Crowe*, (1872) LR 7 CP 629.

<sup>28</sup> F Pollock and D Mulla, *THE INDIAN CONTRACT ACT 1872*, 1341 (Nilima Bhadbhade ed., 14th edn., LexisNexis, 2014).

<sup>29</sup> *Moule v. Garrett*, (1872) LR 7 Ex 101.

These passages appear under the heading ‘Indemnity under Statutes’<sup>30</sup>, which is somewhat misleading. Both ‘indemnities’ might be regarded as creations of law, but they did not originate<sup>31</sup> under statute. In the share transfer cases courts developed several explanations of the indemnity. One perspective was that there was an implied collateral contract to indemnify or an implied promise to indemnify in the sale contract. That view was viable in courts of common law and courts of equity. Courts of equity sometimes proceeded by analogy with the position of a trustee who holds property wholly for the benefit of another: the property (the shares) being subject to a liability (calls). A third – common law – perspective, apparently suggested by the reference to *Moule v. Garrett*, would nowadays be explained on the basis of unjust enrichment. These three perspectives do not all possess the same characteristics. The indemnified party might, for example, be entitled to relief in advance of payment under the first two of them but not the third.

Moreover, the scope of the ‘indemnity’ may differ, as the lease situation demonstrates. Where a lease is assigned, privity of contract joins the lessee and immediate assignee. From at least the nineteenth century, English courts regularly implied a promise by the assignee to indemnify the lessee against default in payment of rent or non-performance of covenants in the lease.<sup>32</sup> Sums paid by the lessee to satisfy a liability which properly rested upon the assignee might, alternatively, be recouped by way of a claim for money paid; nowadays, in unjust enrichment. *Moule v. Garrett* was a significant case because it went further. There was no privity of contract between the plaintiff lessee and the defendants as second successive assignees. That decision stands on the basis of unjust enrichment.

#### D. Actions upon request: scope and juristic basis

A point that has excited some interest under Indian law concerns indemnification for acts performed upon request. There is a well-established line of authority which is said broadly to support the following proposition. Where one person requests another to perform an act which is not itself obviously (or known to be) tortious or wrongful; the latter complies with the request; and the act turns out to injure the rights of a third party; then the acting party is entitled to be indemnified by the requesting party. There was a reasonable amount of support for the proposition as at the time of the Act. The root of modern authority is usually taken to be the later decision of the House of Lords in *Sheffield Corpn.*

<sup>30</sup> Pollock and Mulla, *supra* note 28, 1341.

<sup>31</sup> *But see* note 34.

<sup>32</sup> Later, the indemnity came to be implied by statute. See Section 24(1)(b), Land Registration Act 1925; Section 77(1)(c), Law of Property Act 1925 (UK) (now repealed but unaffected in relation to tenancies prior to 1 January 1996). That indemnity can cover payments reasonably made in respect of alleged liabilities, even if the liabilities are actually invalid in law: *Scottish & Newcastle Plc v. Raguz*, (2008) 1 WLR 2494 : (2009) 1 All ER 763 : 2008 UKHL 65.



v. *Barclay*.<sup>33</sup> There have been numerous decisions since, including two of the Privy Council: *Secy. of State for India v. Bank of India Ltd.*<sup>34</sup> being of immediate relevance to Indian law, and *Yeung Kai Yung v. Hong Kong and Shanghai Banking Corpn.*<sup>35</sup>, an appeal from Hong Kong. With reference to *Sheffield and Bank of India*, the Indian Law Commission recommended that a new section 72A be inserted into the Act, providing for an implied indemnity in substantially the terms outlined above. The Law Commission also expressed the view that the obligation could be regarded as quasi-contractual, drawing support from remarks by Lord Davey in *Sheffield*, Lord Wright in *Bank of India* and by Professor Winkfield in relation to a debtor's liability to indemnify a surety.<sup>36</sup> There are two issues: the scope of the principle and its juristic basis.

Starting with scope, I will sketch three paradigms in which the principle was developed. In the oldest group of cases, a party was directed to deal with goods in a manner that infringed the interest of another, usually the true owner. The acting party might be a sheriff or bailiff who, pursuant to a warrant, levied execution against goods at the direction of another; or some other person who distrained goods at another's request; or a commercial party who sold, delivered or withheld delivery of goods upon instructions.<sup>37</sup> This is familiar ground. Some of these situations are described in the illustrations provided for the agent's indemnity in s 223 of the Act. Other cases involved execution against the debtor personally, or by registration of charges over the debtor's property.<sup>38</sup>

In the second line of cases the acting party has been requested to deal with stock, shares or a negotiable instrument. A typical instance is an application to register a transfer of stock or shares in a company, where the relevant documents (the certificates or transfers) have been forged or stolen.<sup>39</sup> The transfer is registered; the transferee sells the stock or shares to third parties; subsequently, the company (or registrar) incurs a loss because it must honour the transfer but also restore the stock or shares lost by the original holder. *Sheffield* itself was such a

<sup>33</sup> *Sheffield Corpn. v. Barclay*, 1905 AC 392 (HL) ("*Sheffield*").

<sup>34</sup> *Secy. of State for India v. Bank of India Ltd.*, (1938) 2 All ER 797 (PC) ("*Bank of India*").

<sup>35</sup> *Yeung Kai Yung v. Hong Kong and Shanghai Banking Corpn.*, 1981 AC 787 : (1980) 3 WLR 950 : (1980) 2 All ER 599 (PC) ("*Yung*").

<sup>36</sup> The Report, at 49-50. Why the latter was relied upon to justify a new provision is not clear. The point should already be covered by Section 145 or Section 69.

<sup>37</sup> *Adamson v. Jarvis*, (1827) 4 Bing 66; *Humphrys v. Pratt*, (1831) 2 Dow & Cl 288; *Betts v. Gibbins*, (1834) 2 Ad & E 57; *Toplis v. Grane*, (1839) 5 Bing NC 636; *Dugdale v. Lovering*, (1875) LR 10 CP 196. More recent examples include *Strathlorne Steamship Co. Ltd. v. Andrew Weir & Co.*, (1934) 50 Lloyd's Rep 185 (CA); *A/S Hansen-Tangens Rederi III v. Total Transport Corpn. (The Sagona)*, (1984) 1 Lloyd's Rep 194; *ED&F Man Ship Ltd v. Heng Holdings SEA Pte Ltd.*, 1998 SGHC 205.

<sup>38</sup> *Collins v. Evans*, (1844) 5 QB 820 : 114 ER 1459; *Taylor v. Robertson*, (1901) 31 SCR 615 (Canada SC).

<sup>39</sup> But see *Attorney General v. Odell*, (1906) 2 Ch 47 (CA) (registration of a forged transfer of a charge over land).

case, as was *Yung v. HSBC*.<sup>40</sup> In a variation on the same theme, a stolen or fraudulently-indorsed negotiable instrument may be presented for payment or renewal. The instrument is accepted as valid; the true owner later sues one or more of the parties involved for conversion; the party sued then claims indemnity from a person who presented or passed on the instrument for payment or renewal.<sup>41</sup> This was the position in the *Bank of India* case.

Charterparties, particularly time charterparties, comprise a third set of decisions. There may be an implied indemnity to the owner of the vessel against the consequences of the master complying with the charterer's instructions.<sup>42</sup> The decisions fall into two broad groups. In one group are situations where the master signs a bill of lading presented by the charterer, which then imposes upon the owner a responsibility more extensive than that which it has accepted, vis-à-vis the charterer, under the charterparty.<sup>43</sup> In the other group of cases, the owner claims indemnity against the consequences of the master following some direction of the charterer as to the employment of the vessel or the handling of cargo.<sup>44</sup>

It is tempting to generalise the *Sheffield* principle to account for many other circumstances in which an indemnity is recognised. The indemnity from a debtor to a surety, and from a principal to an agent, are obvious candidates. Yet, expressed simply in terms of an action upon request, the *Sheffield* principle is

<sup>40</sup> See *Westropp v. Solomon*, (1849) 8 CB 345; *Stuart v. Hamilton Jockey Club*, (1911) 18 OWR 493 (Ontario SC); *Bank of England v. Cutler*, (1908) 2 KB 208 (CA); *Guaranty Trust Co. v. Richardson & Son*, (1963) 2 OR 347 (Ont SC); *Royal Bank of Scotland Plc v. Sandstone Properties Ltd.*, (1998) 2 BCLC 429 (QB); *Cadbury Schweppes Plc v. Halifax Share Dealing Ltd.*, 2006 EWHC 1184 (Ch).

<sup>41</sup> See *Secy. of State for India v. Bank of India Ltd.*, (1938) 2 All ER 797 (PC); *Middle Temple v. Lloyds Bank Plc.*, (1999) 1 All ER (Comm) 193 (QB); *Linklaters v. HSBC Bank Plc.*, 2003 EWHC 1113 (Comm). But see *Guaranty Trust Co. of New York v. Hannay & Co.*, (1918) 2 KB 623 (CA) (bill of exchange presented for payment accompanied by forged bill of lading).

<sup>42</sup> See W Courtney, *Indemnities in Time Charterparties and the Effect of the Withdrawal of the Vessel*, 30(3) JOURNAL OF CONTRACT LAW 243 (2013).

<sup>43</sup> See *Moel Tryvan Ship Co. v. Krüger & Co.*, (1907) 1 KB 809 at 823-824 (Sir Gorell Barnes P) at 831-832 (CA) (Buckley, LJ); *Krüger & Co. Ltd. v. Moel Tryvan Ship Co. Ltd.*, 1907 AC 272 at 276 (HL) (Lord Loreburn, LC); *Elder Dempster & Co v. C.G. Dunn & Co. Ltd.*, (1909) 15 Com Cas 49 (HL); *Canadian Transport Co. Ltd. v. Court Line Ltd.*, 1940 AC 934 at 943-944 : (1940) 3 All ER 112 (HL) (Lord Wright); *Telfair Shipping Corpn. v. Inersea Carriers SA*, (1985) 1 WLR 553 : (1985) 1 All ER 243; *Naviera Mogor SA v. Societe Metallurgique de Normandie (The Nogar Marin)*, (1988) 1 Lloyd's Rep 412 (CA).

<sup>44</sup> See *Strathorne Steamship Co. Ltd. v. Andrew Weir & Co.*, (1934) 50 Lloyd's Rep 185 (CA); *Newa Line v. Erechthion Shipping Co. SA (The Erechthion)*, (1987) 2 Lloyd's Rep 180; *Athanasia Comminos, The*, (1990) 1 Lloyd's Rep 277; *A/S Hansen-Tangens Rederi III v. Total Transport Corpn. (The Sagona)*, (1984) 1 Lloyd's Rep 194; *Triad Shipping Co. v. Stellar Chartering & Brokerage Inc. (The Island Archon)*, (1994) 2 Lloyd's Rep 227 (CA); *ED&F Man Ship Ltd. v. Heng Holdings SEA Pte Ltd.*, 1998 SGHC 205 : (1998) 2 SLR(R) 630; *Ullises Shipping Corpn. v. Fal Shipping Co. Ltd. (The Greek Fighter)*, 2006 EWHC 1729 (Comm) : (2006) Lloyd's Rep Plus 99, 296. Cf *Aegean Sea Traders Corpn. v. Repsol Petroleo SA (The Aegean Sea)*, (1998) 2 Lloyd's Rep 39 (similar argument made in relation to bill of lading).

manifestly too broad. An agent's indemnity is not complete and does not extend to every loss or liability incurred in the course of the agency. The owner of a vessel is not protected against every loss sustained or liability incurred because the master complies with the charterer's instructions. An employee is not entitled to be indemnified by the employer against all costs incurred and injuries suffered in the course of performing work according to instructions. Indeed, if that were the case then regulation of safe working conditions and workers' compensation would have developed very differently in England. Furthermore, where the employee's act renders the employer vicariously liable to another, the common law indemnity goes in the opposite direction.<sup>45</sup> A person who enters a contract with a third party at another's request is not, for that reason alone, entitled to be indemnified against liability for breach of it. It would be peculiar if, as a general rule, an entity with a separate legal personality could obtain an indemnity from its members who make requests for action.<sup>46</sup>

There are also some striking examples of claims for indemnity failing on particular facts. The seller of a business falsified accounts and then requested his accountants to verify them; they did so in correspondence addressed directly to the purchaser.<sup>47</sup> The accountants were held liable to the purchaser in negligence but were not entitled to an indemnity from the seller. A dentist complied with a doctor's request to extract teeth from an unconscious patient assuming, without confirmation from the patient, that the patient had consented.<sup>48</sup> She had not. The dentist and doctor were held concurrently liable as tortfeasors with contribution, not indemnity, ordered between them.

It is difficult to find a single rationale that explains all of the examples of, and exceptions to, the *Sheffield* principle. I will not attempt to formulate one here. It seems relevant to consider factors such as the appropriate allocation of risk between the acting and requesting parties, the terms of any other contract between them, the nature of the loss claimed, and any independent carelessness by the acting party in complying with the request.

The proper juristic basis for the indemnity is, if anything, even more difficult to identify. English authority on balance favours the view that it is usually contractual<sup>49</sup>, though there are different perspectives on precisely what this entails. Lord Davey in *Sheffield* ventured a distinction between a contract of indemnity implied by law and a contract of indemnity implied or inferred from the circumstances. The former was relevant where the acting party was called upon to

<sup>45</sup> *Lister v. Romford Ice and Cold Storage Co. Ltd.*, 1957 AC 555 : (1957) 2 WLR 158 : (1957) 1 All ER 125 (HL).

<sup>46</sup> *J.H. Rayner (Mincing Lane) Ltd. v. Deptt. of Trade and Industry*, (1990) 2 AC 418 at 518 : (1989) 3 WLR 969 : (1989) 3 All ER 523 (HL) (Lord Oliver).

<sup>47</sup> *Downs v. Chappell*, (1997) 1 WLR 426 : (1996) 3 All ER 344 (CA).

<sup>48</sup> *Parmley v. Parmley*, 1945 SCR 635 (Canada SC).

<sup>49</sup> See the summary given in *Naviera Mogor SA v. Societe Metallurgique de Normandie (The Nogar Marin)*, (1988) 1 Lloyd's Rep 412 (CA).

perform a statutory or common law duty of a ministerial character. The latter was, it seems, relevant for other acts. The reason for the distinction is not entirely clear. Perhaps it stemmed from a concern about the voluntariness of the act of acceptance. Another possible obstacle is the ‘existing duty’ rule, which might deny the sufficiency of the consideration provided by the party acting in return for the requesting party’s promise of indemnity. However, Lord Davey expressly dismissed that rule.<sup>50</sup>

The approach in subsequent cases has been ambivalent. *Bank of India* is at one end of the spectrum. Lord Wright said that the ‘fiction of a contract implied by law adds nothing’<sup>51</sup>; he seems to have discounted the contractual analysis entirely. Both *Sheffield* and *Bank of India* were referred to in the later Privy Council decision of *Yung v. HSBC*. Lord Scarman quoted from the relevant part of Lord Davey’s judgment without specifically addressing the point. *Bank of India* was cited as a supporting authority. In *Yung* the acting party was performing a statutory duty of a ministerial character, yet Lord Scarman’s judgment refers to fundamental elements of contract doctrine. There was an offer to indemnify, which was accepted upon performing the request, and an intention to create legal relations.<sup>52</sup> That is hardly consistent with Lord Wright’s view in *Bank of India*.

Whether characterised as an implication of law or fact, the contractual model does not easily fit all cases. The problem is compounded by the tendency to formulate the indemnity in terms of a positive rule and to recognise that it might be implied ‘by law’. Dissatisfaction with the contractual analysis has prompted attempts to rationalise the indemnity on a different basis.<sup>53</sup> The law of unjust enrichment accounts for some cases, such as that of a surety who pays the debtor’s debt. It is inadequate as a general explanation because the implied indemnity is not confined to situations where the requesting party is enriched by the acting party’s conduct. Rather, the acting party seeks compensation for loss sustained by acting upon the request. The basis of liability does not seem to be tortious: the request need not involve a fraudulent (or, nowadays, negligent) misrepresentation by the requesting party.<sup>54</sup> It might be said that the requesting party encouraged

<sup>50</sup> *Sheffield*, at 404. His reasoning in this respect is far from compelling, though there are other reasons for reaching the same conclusion.

<sup>51</sup> *Yung*, at 800.

<sup>52</sup> *Yung*, at 796, 798.

<sup>53</sup> PS Atiyah, *ESSAYS ON CONTRACT*, 292-293 (Clarendon Press, 1990). It proposes a test based principally upon reliance and benefit. N McBride, *A Fifth Common Law Obligation* 14 *LEGAL STUDIES* 35 (1994) regards the liability as part of an additional class of obligations beyond the conventional categories; that class also includes promissory estoppel and liabilities to pay for non-contractual services (compare with Section 70 of the Act). J Gleeson and N Owens, *Dissolving Fictions: What to Do with the Implied Indemnity?*, 25 *Journal of Contract Law* 135 (2009) argue for a non-contractual obligation that the law attaches to relationships where one party acts for another’s benefit. B Shaw, *Indemnities for Acts Done at Another’s Request*, 44 *UNIVERSITY OF BRITISH COLUMBIA LAW REVIEW* 331 (2011) attributes the liability to the law of unjust enrichment.

<sup>54</sup> *Sheffield*, at 399 (Lord Davey): “it makes no difference that the person making the request is not aware of the invalidity in his title to make the request, or could not with reasonable diligence

the acting party to adopt an assumption as the basis for conduct, and that the acting party relied upon that assumption to its detriment. Estoppel is, however, inapt because the acting party's objective is to obtain compensation for its loss in relation to a third party; it is not, as between itself and the requesting party, seeking to prevent the latter from departing from that assumption. For want of a better alternative, some commentators have concluded that the liability must be *sui generis* or belong to a novel class of obligations.<sup>55</sup>

The implied indemnity is a valuable but challenging concept. I would, therefore, respectfully suggest that close consideration be given to the wide range of Commonwealth case law and academic analysis, including more recent material, before implementing any amendment like that proposed as Section 72A. It might also be useful to consider the relationship between such a provision and Section 223. With reflection, a provision in narrower and more specific terms might be found to be more appropriate.

## II. LIABILITIES, COSTS AND COMPROMISES

### A. Section 125 of the Act provides:

**Rights of indemnity-holder when sued.**<sup>7</sup> The promisee in a contract of indemnity, acting within the scope of his authority, is entitled to recover from the promisor

- (1) all damages which he may be compelled to pay in any suit in respect of any matter to which the promise to indemnify applies;
- (2) all costs which he may be compelled to pay in any such suit if, in bringing or defending it, he did not contravene the orders of the promisor, and acted as it would have been prudent for him to act in the absence of any contract of indemnity, or if the promisor authorized him to bring or defend the suit;
- (3) all sums which he may have paid under the terms of any compromise of any such suit, if the compromise was not contrary to the orders of the promisor, and was one which it would have been prudent for the promisee to make in the absence of any contract of indemnity, or if the promisor authorized him to compromise the suit.

The sub-sections address two related but distinct points. Sub-section (1) establishes the conclusiveness of the liability, subject to the provisos mentioned. In a general sense this is a matter of *proof* of actual or potential loss within the scope

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*have discovered it*".

<sup>55</sup> See Gleeson and Owens, *supra* note 53.

of the indemnity. Sub-section (2) deals more directly with a matter of *scope*, namely, that costs incurred in proceedings should be recoverable, again subject to the provisos mentioned.<sup>56</sup> Sub-section (3) could be read as addressing either of these matters. That is, subject to the provisos, the compromise is treated as conclusive proof of an actual liability; or the scope of the indemnity is extended to cover a compromise of an alleged liability. The opening words of Section 125 and internal cross-reference in Section 125(3) to ‘any such suit’ favour the former interpretation.<sup>57</sup> Strictly, Section 125(3) applies only when a suit has been brought and not where a compromise is made beforehand. It has been accepted, however, that the indemnifier may still be bound in the latter situation.<sup>58</sup> It also appears that Indian courts, drawing upon some remarks in older English cases, have endorsed a further refinement which is not explicit in Section 125(3): if the indemnified party gives due notice of the claim or action and the indemnifier fails to intervene, then the indemnifier is precluded from asserting that the compromise was imprudent.<sup>59</sup> It is true that some support for that proposition can be found in those older decisions. Recent authorities are more circumspect; the proposition probably overstates the present law in England.

The English law in this area is tortuous<sup>60</sup>, a product of attempting to resolve fundamentally opposing policy concerns. Generally, the indemnifier should not be bound by a judgment against the indemnified party if it is not a party or privy to those proceedings. *A fortiori*, a settlement. Conversely, the indemnified party should not be left stranded by conflicting judgments which establish, and then deny, actual liability within the scope of the indemnity. A similar, albeit weaker, argument could be made for settlements reasonably concluded by the indemnified party. An additional factor, where the indemnifier fails to take advantage of an opportunity to intervene at an earlier stage, is that it might be perceived to be unfair<sup>61</sup> for it subsequently to dispute the outcome.

The starting point for analysis is usually taken to be Buller J’s judgment in *Duffield v. Scott*<sup>62</sup>, where the issues of costs and conclusiveness of judgments were intertwined. In dispute was the indemnified plaintiff’s claim for costs and

<sup>56</sup> But see *Bhawani Prasad v. Gopal Singh*, ILR (1888) 10 All 531; *Venkatarangayya Appa Rao v. Varaprasada Rao Naidu*, ILR (1920) 43 Mad 898.

<sup>57</sup> See *Alla Venkataramma v. Palacherla Manqamma*, AIR 1944 Mad 457: “the compromise will be treated as conclusive against the indemnifier subject only to its being attacked as an improvident transaction provided, of course, the compromise has been entered into bona fide and without collusion”.

<sup>58</sup> *Kali Charan v. Durga Kumwar*, ILR (1913) 35 All 168.

<sup>59</sup> *Kali Charan v. Durga Kumwar*, ILR (1913) 35 All 168; *Alla Venkataramma v. Palacherla Manqamma*, AIR 1944 Mad 457.

<sup>60</sup> Courtney, *supra* note 4, at paras 6-30-6-52.

<sup>61</sup> See *Nallappa Reddi v. Vridhachala Reddi*, AIR 1915 Mad 36; (‘monstrous’). But see *Ben Shipping Co. (Pte) Ltd. v. An Bord Baimne (The C Joyce)*, (1986) 2 All ER 177, 187.

<sup>62</sup> *Duffield v. Scott*, (1789) 3 TR 374 : 100 ER 628 (“*Duffield*”). Pollock and Mulla, *supra* note 30, at 1349, asserts that sub-s (1) states the law as summarised in *Lampleigh v. Braithwait*, 1615 Hobart 106 : 80 ER 255 (“*Lampleigh*”). That is incorrect. Perhaps this was originally intended as

expenses he had incurred in previous litigation brought by a third party. The defendant indemnifier objected on the ground that the plaintiff had not given notice of the action against him. Buller J said<sup>63</sup>:

“[T]here are cases which say that, to entitle a person to recover on a bond of indemnity, he must shew that he was compelled by law to pay the debt... The purpose of giving notice is not in order to give a ground of action; but if a demand be made which the person indemnifying is bound to pay, and notice be given to him, and he refuse to defend the action, in consequence of which the person to be indemnified is obliged to pay the demand, that is equivalent to a judgment, and estops the other party from saying that the defendant in the first action was not bound to pay the money.”

That passage is not free from difficulty.<sup>64</sup> From these rather uncertain origins the two issues began to diverge. Indemnification for reasonable costs of litigation is in English law nowadays approached as a question of the scope of the indemnity.<sup>65</sup> Where an indemnity is given in contemplation of liabilities to third parties, costs are usually regarded as included by implication if not mentioned expressly.<sup>66</sup> The issue of conclusiveness of liability is more controversial. After *Duffield* there developed a line of decisions accepting that a judgment against, and even a compromise by, the indemnified party could be conclusive as against the indemnifier, provided that the indemnified party had given notice of the claim or action and the indemnifier had refused to assume responsibility for the defence.<sup>67</sup> In well-known dicta in *Parker v. Lewis*<sup>68</sup>, Mellish LJ accepted that the principle encompassed compromises, while perhaps also eliminating the requirements of notice and refusal to defend for judgments.

Reception of the conclusiveness principle has been mixed. It is useful to compare three jurisdictions. Aspects of *Duffield* took root in the United States and grew into a firm rule.<sup>69</sup> According to Section 57(1) of the Restatement (2d) Judgments:

“[W]hen... an action is brought by the injured person against the indemnitee and the indemnitor is given reasonable notice of the action and an opportunity to assume or participate in its

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a reference to the extensive annotations to *Lampligh* in JW Smith, SMITH'S LEADING CASES, 164-166 (RH Collins and RG Arbutnot edss, 8th edn., Maxwell & Son, 1879).

<sup>63</sup> *Duffield*, at 630.

<sup>64</sup> See *Rust Consulting Ltd. v. PB Ltd.*, 2011 EWHC 1622 (TCC).

<sup>65</sup> Courtney, *supra* note 4, at paras 4-75-4-77.

<sup>66</sup> Courtney, *supra* note 4, at paras 4-76.

<sup>67</sup> Courtney, *supra* note 4, at paras 6-45.

<sup>68</sup> *Parker v. Lewis*, (1873) LR 8 Ch App 1035 at 1059-1060.

<sup>69</sup> *But see* PS Ware, *Vouching: In or Out?*, (42 WASHINGTON & LEE LAW REVIEW 121, 129 (1985).

defense, a judgment for the injured person has the following effects on the indemnitor in a subsequent action by the indemnitee for indemnification:

- (a) The indemnitor is estopped from disputing the existence and extent of the indemnitee's liability to the injured person; and
- (b) The indemnitor is precluded from relitigating issues determined in the action against the indemnitee if:
  - (i) the indemnitor defended the action against the indemnitee; or
  - (ii) the indemnitee defended the action with due diligence and reasonable prudence.<sup>70</sup>

In Australia, Mellish LJ's principle has been applied in a number of indemnity insurance decisions.<sup>70</sup> English insurance decisions are opposed: notwithstanding an adverse judgment against the insured, the insurer is entitled to require the insured to establish actual liability to the third party.<sup>71</sup>

For non-insurance indemnities the position remains unsettled.<sup>72</sup> The conclusiveness principle has not been well received in modern cases,<sup>73</sup> but it might survive in some weakened form as a set of factors that can raise an estoppel in favour of the indemnified party against the indemnifier. The most recent detailed consideration occurred in *Rust Consulting Ltd. v. PB Ltd.*<sup>74</sup> The indemnifier and indemnified party were part of the same corporate group. The indemnified party faced a large claim by third parties and, in the interests of the corporate group, a decision was made that the indemnified party would consent to judgment against it. The figure was significantly higher than the likely result if the proceedings had been contested. Two considerations underlying that decision were that the indemnified party, in any event, had no substantial assets to meet the claim, and that the group had received legal advice that the indemnifier would not be liable under the indemnity. The liquidators of the indemnified party later brought proceedings to enforce the indemnity.

<sup>70</sup> See *JN Taylor Holdings Ltd. v. Bond*, (1993) 59 SASR 432 at 440 (FC) (King, CJ); *CE Heath Casualty & General Insurance Ltd. v. Pyramid Building Society*, (1997) 2 VR 256 at 291 (CA), (Phillips JA); *VACC Insurance Co. Ltd. v BP Australia Ltd.*, 1999 NSWCA 427 (Fitzgerald JA).

<sup>71</sup> *Astrazeneca Insurance Co. Ltd. v. XL Insurance (Bermuda) Ltd.*, (2014) All ER (Comm) 55 at para 23 (Christopher Clarke, LJ).

<sup>72</sup> Courtney, *supra* note 4, at paras 6-46.

<sup>73</sup> See *Ben Shipping Co. (Pte) Ltd. v. An Bord Bainne (The C Joyce)*, (1986) 2 All ER 177.

<sup>74</sup> *Rust Consulting Ltd. v. PB Ltd.*, (2011) 1 All ER (Comm) 951; *Rust Consulting Ltd. v. PB Ltd.*, 2011 EWHC 1622 (TCC); *Rust Consulting Ltd. v. PB Ltd.*, 2012 EWCA Civ 1070.



On the basis that the indemnity covered only actual liabilities<sup>75</sup>, the argument ran that the indemnifier was estopped from denying that the consent judgment was conclusive of actual liability. Edwards-Stuart J held that there was no estoppel even though the indemnifier knew of the claim and gave approval to the consent judgment. The actions of the indemnifier and indemnified party, at the relevant time, were not referable to the enforcement of the indemnity. However, the indemnifier's involvement, or refusal to be involved, in the management of the claim is still generally a factor relevant to establishing an estoppel. As Akenhead J said:<sup>76</sup>

“The active participation of the guarantor or indemnifier in the proceedings, may, depending on the circumstances, level and scope of the participation, go much further to establish an estoppel against it. The positive concurrence by the guarantor or indemnifier with a consent judgment against the beneficiary will go further still.”

Section 125 of the Act can thus be commended for providing some welcome clarity when compared with English law.<sup>77</sup>

### III. ENFORCEMENT OF THE INDEMNITY BEFORE LOSS OCCURS

It is curious that the Act contains no further provisions about enforcement of the indemnity by the promisee. The Act came into effect shortly before the administration of law and equity was unified in England. At that time an indemnified party's action to enforce the indemnity under English law depended, in part, upon the nature of the loss.<sup>78</sup> The promise to indemnify was usually con-

<sup>75</sup> This point was reversed on appeal: *Rust Consulting Ltd. v. PB Ltd.*, 2012 EWCA Civ 1070 at para 22 (Toulson, LJ).

<sup>76</sup> *Rust Consulting Ltd. v. PB Ltd.*, 2010 EWHC 3243 (TCC) at para 45. But see *Frixione v. Tagliaferro*, (1856) 10 Moore 175 : 14 ER 459 (principals bound by foreign judgment against agent when they were aware of the action and had undertaken to provide evidence to support agent's defence); *Pettman v. Keble*, (1850) 9 CB 701 : 137 ER 1067 (principal not involved in defence but apparently authorising agent's compromise of claim by third party); *Nana Ofori Atta II v. Nana Abu Bonsra II*, 1958 AC 95 at 101-102 : (1957) 3 WLR 830 : (1957) 3 All ER 559 (PC).

<sup>77</sup> Another possible difference concerns the position of the indemnified party in relation to the third party. The English indemnity cases have focused primarily on indemnities against liabilities where the indemnified party is the debtor/defendant. It is not clear whether the conclusiveness proposition applies with equal force to situations in which the indemnified party is the creditor/claimant. Section 125 of the Act applies to both situations: *Ramaswami Sastri v. Kali Raghava Aiyangar*, (1917) 43 IC 124; *Ramchandra B. Loyalka v. Shapurji N. Bhowanagree*, AIR 1940 Bom 315.

<sup>78</sup> A fuller account is given in Courtney, *supra* note 4, at paras 1-18-1-23, 7-19. See *Osman Jamal and Sons Ltd. v. Gopal Purshottam*, AIR 1929 Cal 208; *Gajanan Moreshwar Parelkar v. Moreshwar Madan Mantri*, AIR 1942 Bom 302; *Alla Venkataramanna v. Palacherla Manqamma*,

strued to be a promise to keep the indemnified party harmless against the specified loss. Enforcement at common law was generally by way of a claim for damages for breach of contract. The contract would only be broken when the indemnified party actually sustained loss; at that point, by definition, the indemnifier had not kept the indemnified party harmless against loss. The damages award corresponded to the amount of actual loss. The remedies provided by the common law courts were, therefore, inefficacious to protect the indemnified party before loss occurred. Where the loss was merely anticipated, the indemnified party had to seek relief in a court of equity. Intervention in equity was said to rest upon the power of a court of equity to compel specific performance of a contract of indemnity. It would, however, be more accurate to say that equity operated by specifically enforcing a particular term of a contract – the promise to indemnify – rather than by way of ‘specific performance’ of the whole contract.<sup>79</sup>

The second piece of the puzzle is the concept of damnification. Identifying the point at which a potential loss crystallises into an actual loss can be critical. Before fusion, it could determine the appropriate forum – a court of law or equity – for action. It also had, and still has, consequences for the application of limitations statutes.<sup>80</sup> Indeed, many of the early English cases on damnification were limitations cases. There developed a default rule on damnification that applied to indemnities against claims by or liabilities to third parties.<sup>81</sup> In general, a mere claim, demand or action against, or liability of, the indemnified party is not an actual loss. Actual loss crystallises when the indemnified party pays money to the third party in respect of the claim or liability or, perhaps, when the indemnified party’s property is seized and sold in satisfaction of a liability. Thus, in practice, unless equitable relief is available, the indemnified party must pay first and recoup later.

Indian law has adopted a substantially similar default rule on damnification.<sup>82</sup> In its Thirteenth Report, the Law Commission was concerned by the failure of

AIR 1944 Mad 457; *Chunibhai Patel v. Natha Bhai Patel*, AIR 1944 Pat 185; *Abdul Hussain Shaikh Gulamali Jambawalla v. Bombay Metal Syndicate*, AIR 1972 Bom 252.

<sup>79</sup> *But see* Section 12 of the Specific Relief Act, 1963.

<sup>80</sup> See *Shanti Swarup v. Munshi Singh*, AIR 1967 SC 1315 : (1967) 2 SCR 312; *Abdul Hussain Shaikh Gulamali Jambawalla v. Bombay Metal Syndicate*, AIR 1972 Bom 252.

<sup>81</sup> *Courtney*, *supra* note 4, at paras 6-23. Authorities include *Collinge v. Heywood*, (1839) 9 Ad & E 633 : 112 ER 1352; *Richardson; ex p Governors of St. Thomas’s Hospital, In re*, (1911) 2 KB 705 (CA); *British Union and National Insurance Co. v. Rawson*, (1916) 2 Ch 476 (CA); *Firma C-Trade SA v. Newcastle Protection and Indemnity Assn. (The Fanti) (No. 2)*, (1991) 2 AC 1 : (1990) 3 WLR 78 : (1990) 2 All ER 705 (HL). For other Commonwealth examples, see *Official Assignee v. Jarvis*, 1923 NZLR 1009 (CA); *McIntosh v. Dahwood (No. 4)*, (1930) 30 SR (NSW) 415 (FC); *Wren v. Mahony*, (1972) 126 CLR 212.

<sup>82</sup> See *Bhavani v. Anantha Kamthi*, ILR (1916) 31 Mad 556; (actual loss by loss of title to land); *Kalavakolanu Seetamma v. Poduri Narayanamurthi*, ILR (1920) 43 Mad 470 (no actual loss until indemnified party compelled to satisfy judgment); *Ranganath v. Pachusao*, AIR 1935 Nag 147 (incurring liability without payment was not actual loss); *Tilak Ram v. Surat Singh*, AIR 1938 All 297 (loss sustained upon execution sale of property); *Chunibhai Patel v. Natha Bhai Patel*, AIR 1944 Pat 185 (judgment without payment was not actual loss); *Alla Venkataramanna v.*

the Act to address the matter of enforcement of the indemnity before loss. That concern seems to have been prompted by differences of opinion among Indian courts as to whether such enforcement was possible.<sup>83</sup> The Law Commission accepted (in my view, correctly<sup>84</sup>) that it was, and recommended the addition of a new section 125A as follows:

#### IV. "RIGHTS OF INDEMNITY-HOLDER.

- (1) The promisee in a contract of indemnity acting within the scope of his authority may, where a liability has arisen against him in favour of a third party, obtain against the promisor, in an appropriate case, a decree compelling the promisor to set apart a fund out of which the promisor may meet such liability or directing the promisor to discharge such liability himself.
- (2) The promisee may institute a suit under this section even when no such suit as referred to in section 125 has been instituted, and irrespective of whether any actual loss has been sustained by the promisee or not.

*Explanation* — *The promisee is not precluded from obtaining relief under this section merely on the ground that the promisee's liability to the third party cannot effectively be enforced against him.*"

The section is directed at two distinct matters. The first is a matter of timing: at what point is the indemnified party able to enforce the indemnity? This is addressed partly in sub-section (1) ("*where a liability has arisen...*") and in sub-section (2) and the explanatory comment. The second matter concerns the form of the decree. Two forms are identified: setting apart a fund or compelling the promisor to discharge the liability. The text of the section also suggests that the appropriate order may vary depending upon the circumstances of the case.

There is, however, a critical prior consideration. Although a promise to indemnify generally signifies complete protection against a defined loss, the exact nature of the promise varies. It depends upon the construction of the contract.

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*Palacherla Manqamma*, AIR 1944 Mad 457 (payment constitutes actual loss but a mere demand or judgment does not); *Shanti Swarup v. Munshi Singh*, AIR 1967 SC 1315 : (1967) 2 SCR 312 (loss occurring upon execution of mortgage decree and not merely upon it being issued). See *Gajanan Moreshwar Parelkar v. Moreshwar Madan Mantri*, AIR 1942 Bom 302.

<sup>83</sup> The Report, at 50–51. The relevant authorities are noted in Pollock and Mulla, *supra* note 4, at 1343.

<sup>84</sup> *Osman Jamal and Sons Ltd. v. Gopal Purshottam*, AIR 1929 Cal 208 and *Gajanan Moreshwar Parelkar v. Moreshwar Madan Mantri*, AIR 1942 Bom 302 contain useful discussions of the English authorities recognising specific enforcement.

The two most common constructions are: to prevent loss to the promisee, and to compensate the promisee for a loss after it has occurred.<sup>85</sup> For convenience I will refer to these as the ‘preventive’ and ‘compensatory’ constructions respectively. There are statements in some English and Commonwealth cases to the effect that the construction of the indemnity depended upon the court: common law courts adopted compensatory constructions and courts of equity adopted preventive constructions.<sup>86</sup> This is misleading.<sup>87</sup> There was no difference in construction, only a difference in the effect given to the indemnity by way of remedy. Either construction is possible, though the preventive construction is predominant for indemnities against liabilities.

The order for specific enforcement compels performance of the promise of indemnity according to its terms. It is only available for, and consistent with, promises that are preventive in nature. Street CJ explained the position in *McIntosh v. Dalwood (No. 4)*<sup>88</sup>:

“In every case the contractual obligation must first be ascertained... If the obligation is merely an obligation to indemnify a person, in the sense of repaying to him a sum of money after he has paid it, no equitable relief is needed. Damages will provide an adequate remedy. If, however, the obligation on its true construction is an obligation to relieve a debtor by preventing him from having to pay his debt, equity will in such a case give relief in the nature of *quia timet* relief, and, instead of compelling the party indemnified first to pay the debt, and perhaps to ruin himself in doing so, will specifically enforce the obligation by ordering the indemnifying party to pay the debt.”

So, if the promise to indemnify is construed as being one to compensate for loss after the event, there is no cause for equity to intervene;<sup>89</sup> the promisee receives the full bargain by paying first and recouping later. This important distinction can, I suggest, be accommodated within the text of the proposed amendment, by subsuming it within the expression ‘in an appropriate case’. A similar distinction was recognised implicitly in *Chunibhai Patel v. Natha Bhai Patel*.<sup>90</sup> It was there contended that an indemnity in terms to ‘repay you the dues for which you would be liable’ could not be enforced until the promisee actually paid and so sustained a loss. Fazl Ali CJ appeared to accept that contention as correct in

<sup>85</sup> See Courtney, *supra* note 4, Chapter 2.

<sup>86</sup> See *Law Guarantee Trust and Accident Society Ltd., In re*, (1914) 2 Ch 617 at 638 (CA) (Kennedy, LJ); *Official Assignee v. Jarvis*, 1923 NZLR 1009 at 1016 (CA) (Salmond, J).

<sup>87</sup> See Courtney, *supra* note 4, at paras 6-7.

<sup>88</sup> *McIntosh v. Dalwood (No 4)*, (1930) 30 SR (NSW) 415 at 418 (FC). See *Firma C-Trade SA v. Newcastle Protection and Indemnity Assn. (The Fanti) (No. 2)*, (1991) 2 AC 1 : (1990) 3 WLR 78 : (1990) 2 All ER 705 (HL).

<sup>89</sup> *But see* Section 14(1)(a) of the Specific Relief Act, 1963.

<sup>90</sup> *Chunibhai Patel v. Natha Bhai Patel*, AIR 1944 Pat 185.

principle. It was, however, not decisive in the circumstances because the contract also contained a promise of indemnity in terms ‘to remove the said liability’.

This leads to the timing and form of relief. I will address these in reverse order for ease of analysis. The two types of order mentioned in Section 125A – to set apart a fund and to discharge the indemnified party’s liability – are both recognised forms of *quia timet* relief<sup>91</sup>, though the former appears relatively rarely nowadays.<sup>92</sup> The function of the two orders is slightly different. The order to establish a fund is, in general, calculated to safeguard the indemnified party’s position vis-à-vis the indemnifier. Of itself it is only an intermediate stage of protection. The fund must later be applied to discharge the indemnified party’s liabilities. In contrast, an order to discharge the indemnified party’s liability is a final and effective order for indemnification. When executed, the order effects proper performance of the promise to indemnify in respect of the relevant liability.

An order to discharge a liability is just one form of order for indemnification. Other forms are also used in English law; relief is discretionary and the particular form chosen in any case depends upon the circumstances. The most general kind of order directs the indemnifier to procure the release or discharge of the indemnified party from the liability. The method is left to the indemnifier’s discretion. Section 125A(1) appears to be similar but slightly narrower, as it refers only to discharge and not release. More particularly, the indemnifier may be directed to pay a specific sum to the third party, so as to discharge the indemnified party from the liability. In some circumstances, the indemnified party may even be entitled to call for payment in advance to itself, so that it can then use the funds to pay the third party. The exact scope of this last form of order is unsettled.<sup>93</sup> It is clear that such an order will not be made when the indemnifier is itself ‘concerned’ or ‘interested’ in the application of the funds it provides by way of indemnity.<sup>94</sup> A typical instance is where the indemnifier is also liable to

<sup>91</sup> *Richardson; ex p Governors of St. Thomas’s Hospital, In re*, (1911) 2 KB 705 (CA); *British Union and National Insurance Co. v. Rawson*, (1916) 2 Ch 476 (CA); *Firma C-Trade SA v. Newcastle Protection and Indemnity Assn. (The Fanti) (No. 2)*, (1991) 2 AC 1 : (1990) 3 WLR 78 : (1990) 2 All ER 705 (HL); *Osman Jamal and Sons Ltd. v. Gopal Purshottam*, AIR 1929 Cal 208; *Gajanan Moreshwar Parelkar v. Moreshwar Madan Mantri*, AIR 1942 Bom 302; *New India Assurance Co. Ltd. v. State Trading Corp. of India*, AIR 2007 Guj 517. But see *S.K. Mohideen Batcha Sahib v. K.A. Sheik Dawood Sahib*, AIR 1926 Mad 1035 (Orders 7 and 8).

<sup>92</sup> But see *Rowland v. Gulfpac Ltd.*, (1999) 1 Lloyd’s Rep Bank 86; *Papamichael v. National Westminster Bank Plc*, (2002) 1 Lloyd’s Rep 332; *Starlight Shipping Co. v. Allianz Marine & Aviation Versicherungs AG (The Alexandros T)*, 2011 EWHC 3381 (Comm) at paras 37-38.

<sup>93</sup> See Courtney, *supra* note 4, at paras 7-43-7-50.

<sup>94</sup> *Law Guarantee Trust and Accident Society Ltd., In re*, (1914) 2 Ch 617 (CA); *British Union and National Insurance Co. v. Rawson*, (1916) 2 Ch 476 at 482 (CA) (Pickford, LJ); *Osman Jamal and Sons Ltd. v. Gopal Purshottam*, AIR 1929 Cal 208; *Khetarpal Amarnath v. Madhukar Pictures*, AIR 1956 Bom 106.

the third party, such that it would have to make payment again if the indemnified party failed to discharge the liability.<sup>95</sup>

The timing of relief may depend upon the nature of the relief sought. The position for final orders for indemnification is clearest. In English law an order for specific performance may be made before the time for performance of one or more contractual obligations has arrived.<sup>96</sup> The form of the decree is moulded to fit the circumstances, so that a party is not compelled to perform before performance is due according to the contract. This perspective is not, however, directly applicable to promises of indemnity that are preventive in nature. A striking feature of such promises is that there is usually no particular time fixed for performance. So long as the indemnified party suffers no loss within scope, the indemnity is not breached. The object of specific enforcement is to compel the indemnifier to act so that loss – a breach – does not occur. This underscores the point, made earlier<sup>97</sup>, that relief is best regarded as a kind of specific enforcement, not specific performance in the strict sense. This does not mean that a contractual promise of indemnity is specifically enforceable at will. In general terms, relief is limited to situations in which loss is sufficiently imminent.<sup>98</sup>

The circumstantial factors identified in Sections 125A(1) and (2) are consistent with English law<sup>99</sup> and the position already reached by Indian courts.<sup>100</sup> To obtain an order for indemnification, there must be a clear, definite liability which is presently accrued. It is not necessary that the liability be established by judgment, nor that proceedings be commenced against the indemnified party. More intriguing is the explanatory comment to Section 125A, which *negates* a precondition that the liability can ‘effectively be enforced against him’. In *Khetarpal Amarnath v. Madhukar Pictures*<sup>101</sup>, Gajendragadkar J accepted that the right to enforce the indemnity arose once the indemnified party’s liability became absolute, but later added that the indemnified party had to satisfy the court of “the existence of a clear *enforceable* claim against him” (emphasis supplied).

‘Enforceability’ has been used in English and Commonwealth indemnity cases in various senses. It may be just another way of saying that the liability must be definite and presently accrued, rather than inchoate, future or contingent. Alternatively, it may indicate a further requirement:

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<sup>95</sup> *Rankin v. Palmer*, (1912) 16 CLR 285; *Osman Jamal and Sons Ltd. v. Gopal Purshottam*, AIR 1929 Cal 208.

<sup>96</sup> *Hasham v. Zenab*, 1960 AC 316 at 329-30 : (1960) 2 WLR 374 (PC).

<sup>97</sup> *Supra* note 81.

<sup>98</sup> See *Alla Venkataramanna v. Palacherla Manqamma*, AIR 1944 Mad 457.

<sup>99</sup> See Courtney, *supra* note 4, at para 7-24.

<sup>100</sup> *Gajanan Moreshwar Parelkar v. Moreshwar Madan Mantri*, AIR 1942 Bom 302; *Khetarpal Amarnath v. Madhukar Pictures*, AIR 1956 Bom 106.

<sup>101</sup> *Khetarpal Amarnath v. Madhukar Pictures*, AIR 1956 Bom 106.

- (1) that the third party's cause of action (and not merely the underlying 'liability') against the indemnified party has accrued (for example, a procedural requirement for a demand by the third party upon the indemnified party has been satisfied);
- (2) that the indemnified party has the financial means to meet the liability in full;
- (3) that the liability can, in fact, be enforced against the indemnified party's assets by legal process (for example, the indemnified party may have no property at all or, at least, none which can be reached from the jurisdiction in which judgment was given); or
- (4) that there is, in fact, some prospect of the third party taking steps to enforce the liability.

The position in English law seems to be as follows.<sup>102</sup> (1) is not essential if the only missing element (such as a demand) was intended to operate for the benefit of the indemnified party. (2) is not essential. (3) and (4) are unsettled. One view is, in essence, that if (2) is unnecessary then (3) should likewise be irrelevant. The other view emphasises the sufficiently imminent threat of actual loss as the reason for intervention: thus (4) and, by parity of reasoning, (3) might be relevant. Thus, if amendments were to be enacted, it might be helpful to clarify which of these senses of 'enforceability' (or some other sense) was intended by the explanatory comment.

The requirements for an order to set apart a fund are less stringent in some respects. This is not surprising if such relief is regarded as a protective, intermediate step. Two points of difference can be noted. First, there must be a reasonably clear or arguable case that a liability will fall upon the indemnified party.<sup>103</sup> This is consistent with Cozens-Hardy MR's observation in *Richardson, In re*<sup>104</sup> that the fund so established was to be used to meet liability 'as and when it arose'. This sets a lower threshold than the requirements of a clear and presently accrued liability, which generally apply to orders for indemnification. Insofar as the fund may be established before liability has arisen, it is slightly more generous to the indemnified party than Section 125A(1). Secondly, the exercise of the discretion to grant relief requires a balance to be struck between the severity of the protection and the perceived threat of dissipation of assets.<sup>105</sup> One factor, for

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<sup>102</sup> See Courtney, *supra* note 4, at paras 7-32-7-36.

<sup>103</sup> Rowland v. Gulpac Ltd., (1999) 1 Lloyd's Rep Bank 86 at 98; Papamichael v. National Westminster Bank Plc, (2002) 1 Lloyd's Rep 332 at paras 66, 68.

<sup>104</sup> Richardson; *ex p* Governors of St. Thomas's Hospital, *In re*, (1911) 2 KB 705, 709 (CA).

<sup>105</sup> Rowland v. Gulpac Ltd., (1999) 1 Lloyd's Rep Bank 86 at 98; Papamichael v. National Westminster Bank Plc, (2002) 1 Lloyd's Rep 332 at paras 64, 66.

example, may be that there is a clear indication that the indemnifier intends to ignore its obligations.

## V. CONCLUSION

The Indian law on contractual indemnities has in some respects diverged from English law and followed its own path. Such differences are, however, greatly outweighed by their similarities. The degree of consistency more than one hundred years after the Act is quite remarkable.

In this article I have endeavoured to provide some insights on developments in English law and to suggest tentatively how these might inform and influence Indian case law and any future amendments to the Act. In the Preface to the first edition of his commentary, with DF Mulla, on the Act, Pollock noted the tendency of Indian courts to follow too literally English decisions. He said: *“The best way to counteract such a tendency is not to neglect the letter of English judgments... but to enter more fully into their spirit and distinguish their permanent from their local and accidental elements.”*

I hope this contribution continues that tradition.