

7-1-1992

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Recommended Citation

Manmohan Lal Sarin, *Contract Unconscionability in India*, 14 Loy. L.A. Int'l & Comp. L. Rev. 569 (1992).
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Contract Unconscionability in India

MANMOHAN LAL SARIN*

I. HISTORICAL BACKGROUND

When Queen Elizabeth of England passed the Charter of 1600, it empowered the East India Company to create laws, in accordance with prevailing English law, that were necessary for the company's efficient operation in India. Subsequently, the Charter of 1726 introduced English common law and statutory law to the three Indian Presidency towns of Calcutta, Bombay, and Madras, resulting in much confusion among the native inhabitants.

The Statute of 1781 introduced customary laws designed to resolve disputes. Prior to the passage of this statute, English law applied indiscriminately to Hindus and Mohammedans alike.¹ The 1781 statute empowered the courts of Calcutta, Bombay, and Madras to resolve all disputes among the inhabitants regarding matters of succession, inheritance, rentals, and contract under Hindu law in cases involving Hindus, and Mohammedan law in cases involving Mohammedans.² In cases where litigants belonged to different religions, the courts applied the law governing the defendant.

The Statute of 1862 established the High Courts in Calcutta, Madras, and Bombay.³ These courts administered the applicable laws, as determined by the religion of the parties. In fact, the High Courts continued to apply sectarian law until the passage of the Indian Contract Act in 1872.

II. ENACTMENT AND INTERPRETATION OF THE INDIAN CONTRACT ACT

The Indian Contract Act of 1872 was composed of 266 sections covering such contract elements as the sale of goods, bailment,

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1. HERBERT COWELL, HISTORY AND CONSTITUTION OF THE COURTS AND LEGISLATIVE AUTHORITIES IN INDIA 56 (S.C. Bagchi ed., 6th ed. 1936).

2. *Id.*

3. An Act for Establishing High Courts of Judicature in India, 1862, 24 & 25 Vict., ch. 104 (Eng.).

agency, and partnership. The introduction of the Act was greeted with mixed reviews. The Civil Justice Committee in 1925 remarked that, while the Act was in some respects farsighted, it was not one of the best codes, and, in fact, required amendment. Consequently, a number of attempts were made to improve the law of contract. For example, after the passage of the Sale of Goods Act of 1930 and the Indian Partnership Act of 1932, the corresponding chapters of the Act were repealed.⁴ The Act does not cover all aspects of contract law, but, rather, has been supplemented by a number of other statutes. One commentator argued that such statutes should be consolidated and incorporated into the Act.⁵ The legislative trend following the enactment of the Act, however, went in the opposite direction.⁶ Separate legislation, such as the Negotiable Instruments Act of 1881, continued to be enacted on specific aspects of contractual transactions. In addition, sections of the Act were removed to create separate statutes, such as the Sale of Goods Act of 1930 and the Indian Partnership Act of 1932.⁷

The Indian Contract Act of 1872 applies to all Indians, regardless of religion. Although the Act is not considered a complete code,⁸ it nevertheless constitutes exhaustive legislation applicable to all Indian provinces. In interpreting the Act, it is usually not permissible to import the principles of English common law, unless the Indian statute cannot be understood without applying English common law principles.⁹

When hearing cases clearly covered by the statute, Indian courts are not required to refer to judicial decisions. This is because the language of the Act has never been modified or enlarged to encompass the principles or limitations established by the English common law. Indian courts, however, often rely on English common law principles regarding contract law where a statutory provision does not cover a specific issue. Although Indian courts examine and apply the language of the Indian Statutes, they often cite relevant decisions of other commonwealth courts, such as those in Australia and Canada, as well as courts in the United States.

4. LAW COMMISSION OF INDIA, THIRTEENTH REPORT OF THE INDIAN CONTRACT ACT OF 1872, at 2 (1958).

5. 1 THE ANGLO-INDIAN CODES 534 (Whitley Stokes ed., 1887).

6. LAW COMMISSION OF INDIA, *supra* note 4, at 2.

7. *Id.* at 3.

8. *Id.* at 2.

9. West Bengal v. M/S.B.K. Mondal and Sons, [1962] 1 Supp. S.C.R. 876 (India).

A. Relevant Provisions Under Indian Law

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

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.

2. 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 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.
- (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.

a. 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

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, 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.

B. The Doctrine of Undue Influence in India

1. The General Doctrine of Undue Influence

Section 19A of the Act empowers Indian courts to void a contract induced by undue influence. Yet, even before this Act, the equitable doctrine of undue influence grew out of a perceived necessity to grapple "with insidious forms of spiritual tyranny and with the infi-

nite varieties of fraud.”¹⁰ 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:

[W]henver 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, although the transaction could not have been impeached if no such confidential relation had existed.¹³

Section 16 of the Act defines “undue influence” in the particular context of contracts.¹⁴ This “particularization,” however, is but part “of a larger principle.”¹⁵ Justice Tek Chand of the High Court of Punjab expressed this larger principle in *Amir Chand v. Sucheta Kripalani*:¹⁶

The legal phrase “undue influence” denotes something legally wrong or violative of a legal duty. In order to establish undue influence it must be proved that the influence was such as to deprive the person affected of the free exercise of his will. It must amount to imposing a restraint on the will of another whereby he is prevented from doing what he wishes to do or is forced to do [that] which he does not wish to do.

An advice, argument, persuasion or solicitation cannot constitute undue influence. Honest intercession, even importunity, falls short of controlling a person’s free exercise of his will. A persuasion, which leaves a person free to adopt his own course, is not undue influence. Otherwise a suggestion or an entreaty from somebody, held in esteem, could be treated as undue influence. In the absence of proof that a person has been, in consequence of the alleged influence, deprived of free agency, no question of there being an undue influence arises.

It is not objectionable to exercise an influence by acts of kindness or appeals to the free reason and understanding. So long as

10. *Allcard v. Skinner*, 1886-1890 All E.R. 90, 99 (1887) (Eng.).

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

12. [1866] 2 Ch. App. 55 (Eng.).

13. *Id.* at 61.

14. *See Ladli Prasad Jaiswal*, [1964] 1 S.C.R. at 299.

15. *Id.*

16. 1961 A.I.R. (Punjab) 383.

the free agency of the other person is not prevented or impaired by obtaining a domination over the mind of another it cannot be deemed as an exercise of an undue influence. The essence of "undue influence" is that a person is constrained to do against his will [that which], but for the influence[,] he would have refused to do if left to exercise his own judgment. It has to be shown that a person's volition had thus been controlled by another whereby he could not pursue his own inclination, being too weak to resist the importunity and in view of the pressure exercised on his mind he could not act intelligently and voluntarily and had become subject to the will of the other who had thus obtained dominion over his mind.

The term "undue influence" is not susceptible [to a] precise definition but it suggests the overcoming of the will of one by the other who superimposes his will on the weaker party despite the latter's disinclination or effective resistance. Undue influence is a species of constructive flow. Undue influence is used in contradistinction to proper influence which may be secured through affection bestowed or from kindness indulged.

A friendly advice or an influence arising from gratitude or esteem is not undue influence unless thereby the functioning of a free mind is destroyed. Mere suggestions or appeals cannot have such an effect. An influence which exists from attachment or which results from arguments on appeals to the reasons and judgments is not undue.¹⁷

Thus, under this larger principle, undue influence is found where coercion and fraud overcome the functioning of another person's free mind. Once a position of dominance is established, it is deemed to continue until its termination is established. The person obtaining the advantage has the burden of proving that the executant adopted the transaction after the influence was removed.

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.¹⁸ The doctrine also applies to transactions involving gifts made under circumstances that disclose an unfair advantage by one party over the other.¹⁹

Traditionally, Indian courts have scrutinized cases involving one

17. *Id.* at 386.

18. See *Ladli Prasad Jaiswal*, [1964] 1 S.C.R. at 301.

19. *Subhas Chandra Das Mushib v. Ganga Prasad Das Mushib and Ors.*, [1967] 1 S.C.R. 331 (India); see also *Allcard*, 1886-1890 All E.R. at 93.

party's spiritual dominance over another,²⁰ and cases involving unscrupulous persons enriching themselves at the expense of expectant heirs. In such cases, even a trace of undue influence suffices to invalidate the transaction as unconscionable.²¹

2. The Doctrine of Undue Influence as Embodied in Section 16 of the Indian Contract Act of 1872

The principles underlying the doctrine of undue influence are embodied in section 16 of the Act.²² The idea of free consent in contracts triggers the possibility that undue influence may arise. Undue influence arises in this context when one party uses his or her influence to preclude the other party's exercise of free and deliberate judgment.²³ Similarly, a contract is rendered void whenever a confidence is betrayed and influence is abused.²⁴

Section 16 contemplates moral coercion, in contrast to the physical coercion found in section 15 of the Act. Sir Frederick Pollock stated the concept of undue influence in his book, *Principles of Contract*:

[Undue influence involves] an influence brought to bear upon a person entering into an agreement or consenting to a disposal of property which having regard to the age and capacity of the party, the nature of the transaction and all the circumstances of the case, appear to have been such as to preclude the exercise of free and deliberate judgment.

The two elements necessary to set aside a contract under section 16 reflect the basic principles of undue influence. Under subsection 1, the person seeking to avoid the transaction must prove that the other party was both in a position to dominate the will of the other,²⁵ and that he or she used that position to obtain an unfair advantage over the party seeking relief. Only a person who is a party to the contract can raise the plea of undue influence and seek relief under section 16.²⁶

The burden of proof in a case involving undue influence occurs in three stages. First, the party seeking to avoid the contract must

20. *Allcard*, 1886-1890 All E.R. at 93.

21. *Id.*

22. For the text of Section 16, see *supra* part II.A.2.

23. *Amir Chand*, 1961 A.I.R. (Punjab) at 386.

24. *Tate*, [1866] 2 Ch. App. at 61.

25. *Prasad v. Prasad*, 51 I.A. 101, 105 (1923) (India).

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

prove, either by evidence or by the special presumption of subsection 2, "that the other party to [the] transaction was in a position to dominate his [or her] will."²⁷ Second, the party seeking to avoid the contract must show "that the other party obtained an unfair advantage by using that position."²⁸ Once these two stages are reached, the burden of proof shifts under subsection 3. The party in a position to dominate must then prove that "such a contract was not induced by undue influence."²⁹

3. Onus of Proof

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.

a. The Burden of Proving Unconscionability Under 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. The following examples illustrate this good faith requirement: (1) If the issue of good faith is raised in an attorney-client transaction, the burden of proving good faith is on the attorney; and (2) If the issue of good faith is raised against a father by a son who has recently come of age, the burden of proving good faith is on the father. While section 16(3) of the Indian Contract Act of 1872 applies only to contract actions, section 111 of the Indian Evidence Act of 1872 applies to all transactions in which one party "stands to the other in a position of active confidence."

In India, where a vast majority of the population is ignorant, illiterate, and blindly follows one spiritual guru or another, there are innumerable cases of exploitation by spiritual leaders. For centuries, religious followers have given valuable property in an attempt to achieve "nirvana" or spiritual benefits in the afterlife. Parties have attacked these facially unconscionable transactions in courts of law.

27. *Ladli Prasad Jaiswal*, [1964] 1 S.C.R. at 300.

28. *Id.*

29. *Id.* at 301.

One early case, *Manu Singh v. Umadat Pande*,³⁰ was decided by the High Court of Allahabad in 1890. In *Manu Singh*, the elderly plaintiff deeded his entire estate to the defendant, a Brahmin who was his spiritual leader and who was highly respected in the community.³¹ The plaintiff made this gift to secure benefits for his soul in the after-life and in response to the defendant's recitation of the holy book called the *Bhagwat Gita*.³² Almost immediately, the plaintiff repudiated the deed and sued for its cancellation.³³

The Allahabad High Court held that the fiduciary relationship between the parties, the improvidence of the gift, the absurd reason for the gift, and section 111 of the Evidence Act of 1872 required that the burden be placed upon the defendant to prove that the transaction was made in good faith and without undue influence.³⁴ Absent such proof, the plaintiff was entitled to cancel the deed.³⁵

One class, Pardanashin women, is especially exposed to undue influence. Since these women do not appear in public and are not wise in the ways of the world, courts often come to their rescue.³⁶ As a result of judicial decisions, every person dealing with a Pardanashin woman must prove not only that the terms were fair and just, but that they explained the terms of the contract or transaction and that the woman understood them.³⁷ The courts impose this burden because Pardanashin women are "presumed to have an imperfect knowledge of the world, as by the pardah system they are practically excluded from social intercourse and communion with the outside world."³⁸ The special protection accorded to Pardanashin women is based on the two pillars of justice in Indian law, equity and good conscience.³⁹

C. *Avoiding an Unconscionable Contract*

A party who is induced by undue influence to enter into a contract may avoid the contract pursuant to section 19A of the Indian Contract Act of 1872. The party asserting unconscionability need not produce direct evidence of actual undue influence. Rather, the court

30. 12 Indian L.R. (Allahabad) 523 (1890).

31. *Id.*

32. *Id.* at 526.

33. *Id.* at 524.

34. *Id.*

35. *Manu Singh*, 12 Indian L.R. (Allahabad) at 524.

36. *See* Kharbuja Kuer v. Jangbahadur, 1963 A.I.R. (S.C.) 1203.

37. *See id.*

38. *Id.*

39. *See* Tara Kumari v. Chandra Mauleshwar, 1931 A.I.R. (Privy Council) 303.

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.

Once a suit is filed seeking to avoid an unconscionable contract, and the plaintiff has discharged his or her initial burden, the defendant must prove by cogent and convincing evidence that the bargain was fair, just, and reasonable. Mere inadequacy of consideration, without more, is insufficient to make the bargain unconscionable,⁴⁰ though the court may take it into account in determining whether the consent was given freely. In this respect, the Bombay High Court has held that "inadequacy of consideration in conjunction with the circumstances of indebtedness and ignorance were facts from which it would have been . . . permissible . . . to infer use of undue influence."⁴¹

If a contract shocks the judicial conscience, the defendant will find it difficult to prove that the contract should be upheld. This does not mean, however, that the defendant automatically loses. For example, in loan cases, the lender invariably is in a position to dominate the will of the borrower and all such transactions can be termed unconscionable. The mere fact that the rate of interest is exorbitant is not enough, by itself, to cancel a contract, unless the plaintiff also establishes that the lender was in a position to dominate his or her will. The fact that the borrower was in urgent need of money does not place the lender in a position to dominate the will of the borrower. Thus, such a loan will not be set aside by a court even if it may seem to be unconscionable.

D. Enforcing an Unconscionable Contract

The Specific Relief Act of 1963 specifies the remedies available to a party, including specific performance, rescission, and cancellation. Prior to the original enactment of the statute in 1877, Indian courts were guided by the doctrines that evolved in English equity courts. The Specific Relief Act of 1963 provides for equitable remedies, and the grant or refusal of relief is still governed by the principles of justice, equity, and good conscience.

1. Judicial Discretion in Granting Specific Performance

Section 20 of the Specific Relief Act of 1963 discusses the court's discretion in granting specific performance:

40. Lakshminarayana v. Singaravelu, 1963 A.I.R. (Madras) 24.

41. Bhimbhat v. Yeshwantrao, 25 Indian L.R. (Bombay) 126 (1900).

- (1) The jurisdiction to decree specific performance is discretionary, and the Court is not bound to grant such relief merely because it is lawful to do so. The discretion of the Court is not arbitrary but sound and reasonable, guided by judicial principles and capable of correction by a court of appeal;
- (2) The following are cases in which the Court may properly exercise discretion not to decree specific performance:
 - (a) where the terms of the contract or the conduct of the parties at the time of entering into the contract or the other circumstances under which the contract was entered into are such that the contract, though not voidable, gives the plaintiff an unfair advantage over the defendant; or
 - (b) where the performance of the contract would involve some hardship on the defendant which he did not foresee, whereas its non-performance would involve no such hardship on the plaintiff; or
 - (c) where the defendant entered into the contract under circumstances which though not rendering the contract voidable, makes it inequitable to enforce specific performance.

Explanation 1—Mere inadequacy of consideration, or the mere fact that the contract is onerous to the defendant or improvident in its nature, shall not be deemed to constitute an unfair advantage within the meaning of Cl.(a) or hardship within the meaning of Cl.(b).

Explanation 2—The question whether the performance of a contract would involve hardship on the defendant within the meaning of Cl.(b) shall, except in cases where the hardship has resulted from any act of the plaintiff subsequent to the contract, be determined with reference to the circumstances existing at the time of the contract.

- (3) The Court may properly exercise discretion to decree specific performance in any case where the plaintiff has done substantial acts or suffered losses in consequence of a contract capable of specific performance.
- (4) The Court shall not refuse to any party specific performance of a contract merely on the ground that the contract is not enforceable at the instance of the other party.

Section 20(2) grants wide discretion to the court to decline specific performance of a contract that is otherwise valid and enforceable, solely on the ground that it is unconscionable or works an unfair advantage to the plaintiff over the defendant. Thus, although mere inadequacy of price is not a sufficient hardship so as to refuse the plaintiff

specific performance,⁴² a court may look at the particular facts of a case to determine whether the transaction is unconscionable and whether it should be specifically enforced. It is impossible to enumerate the illustrations in which specific performance should not be granted. Thus, the legislature properly left this decision to the court's discretion in accordance with sound judicial principles.

III. CONCLUSION

A contract that is unconscionable or results in an unfair advantage to one of the parties will not be upheld or enforced by a court of law in India. Considering the special social conditions prevailing in the country, especially the high degree of illiteracy and the practice of spiritualism, courts are inclined to protect the party whose will could be dominated or prevailed upon by another solely to gain an unfair advantage. The principles of justice, equity, and good conscience devised by courts of equity in England may not completely prevail in view of legislative enactments like the Indian Contract Act of 1872 and the Specific Relief Act of 1963. The courts, however, are still influenced by English principles and will apply them whenever a statutory provision is silent or inapplicable.

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