

The Agency Contract: INDIA





1 Report on position in India regarding claims of agent in case of termination of contract.

INDIA



1.1 Introduction

In India, the relationship between Agent and Principal is primarily contractual in nature and is governed by the terms of contract entered into between them ("Agency Contract"). The law of agency derives its statutory base from Chapter X of the Indian Contract Act, 1872 ("Act"), which provides the framework of rules and regulations that govern formation and performance of any contract including the Agency Contract.

Section 182 of the Act defines 'Agent' as 'person employed to do any act for another or to represent another in dealings with third person'.

Any person, who is of the age of majority according to the law to which he is subject, and who is of sound mind, can employ an Agent¹. As between Principal and third person a person may become an Agent, so as to be responsible to his Principal according to the provisions contained in the Act². No consideration is necessary to create an agency³. The authority of an Agent may be express or implied⁴. An authority is said to be express when it is given by words, spoken or written⁵. An authority is said to be implied when it is to be inferred from the circumstances of the case and things spoken or written or in the ordinary course of dealing may account for the circumstances of the case⁶. An Agent having an authority to do an act has authority to do every lawful thing, which is necessary in order to do such act⁷. The Agent in doing that act must neither do anything that is illegal, not beyond the limits of his own authority, nor beyond the powers of his Principal. An Agent has authority in an emergency to do all such acts for the purpose of protecting his Principal from loss as would be done by a person of ordinary prudence, in his own case under similar circumstance⁸.

Several types of commercial agents have been recognized under Indian law, which includes inter alia brokers, auctioneers, del credere agents, persons entrusted with money for obtaining sales and insurance agents.

¹Section 183.

²Section 184.

³Section 185.

⁴Section 186.

⁵Section 187.

⁶Section 187.

⁷Section 188.

⁸Section 189.

2 Indemnities and/or compensation

INDIA

The right to claim indemnity arises primarily in the event of termination of the agency. An agency is terminated by the Principal revoking his authority; or by the Agent renouncing the business of the agency; or by the business of the agency being completed; or by either the Principal or Agent dying or becoming of unsound mind; or by the Principal being adjudicated an insolvent under the provisions of any act for the time being in force for the relief of insolvent debtors⁹. Where the Agent has himself an interest in the property which forms the subject matter of the agency, the agency cannot be terminated to the prejudice of such interest.¹⁰

The right to indemnity and/or the right to compensation to the Agent in the event of termination of the Agency Contract is subject primarily to the terms and conditions of the Agency Contract entered into between Principal and Agent. Since the Agent represents the Principal, the Agent has the right to be indemnified for all the lawful acts done by the Agent in the course of the agency. The Act contains specific provisions under Section 222 and 223, discussed in detail in subsequent paragraphs, for the payment of indemnity or compensation in the event of revocation of the Agency Contract by the Principal prior to its term.

Unless the Agency Contract provides for the payment of full indemnity, the indemnity payable to the Agent is generally equitable. There is no limitation on the amount of indemnity to which an Agent may be entitled to and it is the Court, which determines the amount of indemnity that may be paid.

⁹Section 201

¹⁰Section 202

2. Indemnities and/or compensation

The Courts in India, from time to time have held that an Agent can claim indemnity against the Principal, if the Agent is able to prove that he has actually incurred a loss or that loss is eminent due to the wrongful termination of the Agency Contract.

For an Agent to claim indemnity it is essential that the act done by him must be lawful. It is not sufficient that his acts are innocent or done in good faith. Further, it is important that the action in respect of which the Agent is claiming indemnity must have been performed in accordance with the authority conferred upon the Agent. There is no right to indemnity unless the Agent has acted within his express, implied or usual authority.

Subject to the terms of Agency Contract the Agent may, in addition to indemnity, claim compensation by way of damages, which may either be general or special.

General damages are those, which result from 'direct and proximate' consequences from breach of contract. Normally, what can be awarded is compensation for loss or damage, which can be directly or proximately attributed to the breach of contract. One way of assessing damages is the difference between the contract price and the market price on date of breach of contract, plus reasonable expenses incurred by him on account of the breach plus cost of suit in court of law.

Special damages or consequential damages arise due to existence of special circumstances. Such damages can be awarded only in cases where the special circumstances were foreseeable by the party committing the breach or were specifically known to the party.

3

3 Conditions of indemnity and/or compensation

INDIA



Subject to the terms of the Agency Contract, the Act provides for the following situations where an Agent has to be indemnified/ compensated by the Principal:

a) **Conditions for claiming Indemnity:**

- (i) Section 222 of the Act provides: -
“the employer of an Agent is bound to indemnify him against the consequences of all lawful acts done by such Agent in exercise of the authority conferred upon him”; and
- (ii) Section 223 of the Act provides: -
“where one person employs another to do an act, and the Agent does the act in good faith, the employer is liable to indemnify the Agent against the consequences of the act, though it causes an injury to the rights of third persons”.

Section 222 of the Act provides that an employer is bound to indemnify an Agent against all the consequences of all lawful acts done by such Agent in the exercise of the authority conferred upon him. By virtue of this section, under the Indian Law there is an implied contract between the Principal and the Agent whereby the Principal has to indemnify the Agent against the losses and consequences of all lawful acts done by such Agent in exer-

3. Conditions of indemnity and/or compensation

cise of the authority conferred upon him. For instance, where an Agent who is authorized to make contracts for the supply of goods, is authorized or is not forbidden to make those contracts in his own name, he becomes entitled to an indemnity against any personal liability in respect of any contract for the purchase of goods the moment he enters into such contract. His right of action in respect of this indemnity is not postponed to his satisfaction of the liabilities against which he claims indemnity.

It is important for the Agent to prove that the Agent has actually incurred a loss or that the loss is eminent.

Further, in order to claim indemnity under this section it is essential that the act committed by the Agent must be lawful. Indian courts have held that an Agent is entitled to indemnity even in respect of void, but not illegal contracts. It has also been held by the Indian Courts that the Principal has to indemnify the Agent even in respect of the payments, which the latter is compelled to make even though he is not legally liable to pay the same.

Section 223 of the Act provides that an Agent has to be indemnified against consequences of unlawful acts, which are not criminal, done by him in good faith and without the knowledge that such act is unlawful. This provision entitles an Agent to claim indemnity in respect of the acts done in good faith though they cause injury to the rights of third persons.

The right to indemnity entitles an Agent to recover his commission remuneration and all his expenses that he has incurred on the Principal's behalf.

It has been held by Supreme Court of India that the right of an Agent to obtain indemnity from his Principal is a matter entirely collateral to the main contract made by the Agent on behalf of the Principal, and is not affected by anything, which renders the main contract unenforceable.

Where the authority of the Agent has been properly revoked, he is entitled to recover the remuneration or commission already earned.

Where an Agent acts within the scope of his authority he is entitled to full indemnity. Where an Agent purchases goods on behalf of his Principal and renders himself liable for the price of goods, the Agent has the same rights with regard to the disposal of the goods as he would have had, if the relation between him and the Principal had been that of the seller and buyer. If, therefore, the Principal improperly refuses to accept, the Agent is entitled to re-sell the goods and hold Principal liable for any deficiency arising from the sale. The deficiency is the measure of loss in respect of which the Agent is entitled to be indemnified and reimbursed.

3. Conditions of indemnity and/or compensation

b) Conditions for claiming Damages/ Compensation: -

The general law of damages in India is contained in Section 73, 74 and 75 of the Act.

The Act provides that in the event of breach of a contract the non-defaulting party is entitled to receive compensation for any loss or damage caused to such non-defaulting party thereby. Such compensation is payable when the loss has arisen in the usual course of things from such breach, or which the parties knew, when they made the contract, to be likely to result from such breach of it. The party in breach must make compensation in respect of direct consequences flowing from the breach and not in respect of loss or damage indirectly or remotely caused.

When an obligation resembling those created by contract has been incurred and has not been discharged, any person injured by the failure to discharge is entitled to receive the same compensation from the party in default, as if such person had contracted to discharge it and broken his contract . In estimating the loss or damage arising from the breach of contract, the means that existed of remedying the inconvenience caused by the non-performance of the contract must be taken into account .

Where the contract provides for the payment of a specified amount or a penalty, by the defaulting party to the non-defaulting party in the event of breach, the non-defaulting party is entitled, whether or not actual damage or loss is proved to have been caused thereby, to receive from the defaulting party reasonable compensation not exceeding the amount so specified in the contract .

Under the Act a person who rightfully rescinds a contract is entitled to compensation for any damage, which he has sustained through the non-fulfillment of the contract .

The law pertaining to damages and compensation in the event of termination of Agency Contract is set out in Section 205, 206 and 225 of the Act.

(i) Section 205 of the Act provides as follows:-

3. Conditions of indemnity and/or compensation

“where there is an express or implied contract that the agency should be continued for any period of time, the Principal must make compensation to the Agent, or the Agent to the Principal, as the case may be, for any previous revocation or renunciation of the agency without sufficient cause”.

- (ii) Section 206 of the Act provides as follows:-
“reasonable notice must be given of such revocation or renunciation; otherwise the damage thereby resulting to the Principal or the Agent, as the case may be, must be made good to the one by the other”.
- (iii) Section 225 provides as follows: -
“the Principal must make compensation to his Agent in respect of the injury caused to such Agent by the Principal’s neglect or want of skill.”

Under the Act, liability to pay compensation arises when the Agency Contract is terminated without sufficient cause or where the Principal fails to give a reasonable notice before the revocation of the Agency Contract or where any injury caused to such Agent due to Principal’s neglect or want of skill.

If the term of the agency is fixed in the Agency Contract, it is determined on the expiration of the term. The agency may be terminated before the expiry of the term in accordance with an express reservation in the contract or for a reasonable cause. If the Agency Contract is terminated by the Principal prior to its term without sufficient cause, the Principal is liable and must make compensation to the Agent for the previous revocation of the agency.

The Indian Courts have held that the following interalia will constitute ‘sufficient cause’ for the termination of agency:-

- (a) Loss of reputation by the Agent;
- (b) Incapacity of the Agent, whether physical or mental;
- (c) Misconduct on the part of Agent, if sufficient to justify dismissal; and
- (d) Taking bribes.

The Act provides that where there is no express or implied contract that the

3. Conditions of indemnity and/or compensation

agency should continue for any fixed period, reasonable notice must be given of the revocation or renunciation of the agency. In the event the Principal fails to give a reasonable notice to the Agent before the revocation of the agency, the Principal is liable to pay damages to the Agent for the loss incurred by the Agent due to such termination. Reasonableness varies from circumstances of each case.

In all indefinite mercantile or commercial contracts, the question whether the relationship of the Principal and Agent can be terminated by a reasonable notice or only by mutual consent is one of construction subject to the rules of law. There is no general rule of permanence. An agency may be terminated by various ways. If the termination of agency is inequitable or works an unjust hardship on the Agent, the law requires a reasonable notice to be given. An absolute power of cancellation of contract cannot be validly reserved in favour of one of the parties. Such a clause in the contract is absolutely illegal and irregular.

Under Section 225 of the Act, the Principal is liable to compensate the Agent in respect of any injury caused to such Agent due to Principal's neglect or want of skill. In order to entitle the Agent to compensation he must prove that:-

- (a) some injury was caused to him; and
- (b) such injury was caused by the Principal's neglect or want of skill.

The Agent cannot recover compensation, if the Principal proves that the Agent could have avoided the consequence of Principal's negligence by reasonable means. Further, the Agent cannot recover compensation, if the injury has resulted from the nature and circumstances of his employment, or if the injury is a natural and necessary consequence of his employment.

In addition to damages and indemnity, the Act gives additional right of lien to the Agent over the Principal's property. The Act provides that in the absence of any contract to the contrary an Agent is entitled to retain goods, papers and other property, whether movable or immovable, of the Principal received by him, until the amount due to himself for commission, disbursements and services in respect of the same has been paid or accounted for to him. The Agent's lien does not confer unrestricted authority on the Agent to deal with the Principal's property, this right is limited in nature and the Agent can retain the property till his dues are paid by the Principal. This right can be availed of as a defense if the Principal brings an action for the recovery of the prop-

3. Conditions of indemnity and/or compensation

erty in possession of the Agent. But this provision does not confer any authority on the Agent to sell or otherwise dispose of the property without the consent of the Principal in order to satisfy his lien.

Besides the aforesaid, there are no specific provisions under the Act, which entitle an Agent to claim indemnity against or compensation from the Principal and it is open to the parties to formulate the terms and conditions for claiming indemnity under the contract.

Indian Limitation Act governs the law pertaining to the period within which the Agent should file a suit for claiming compensation/ indemnity.

According to the Limitation Act, 1963 when an Agent sues the Principal for money spent by him on behalf of the Principal and recoverable under Section 222 and 223 of the Act, the suit should be filed within a period of three years from the date of payment and not when the agency terminates.

Suit for claiming compensation and indemnity should be filed within a period of three years from the date the right to sue has first arisen i.e. when the cause of action first arises. When the right to sue first arises largely depends on the facts and circumstances of each case.

4. Calculation of indemnity and/or compensation



INDIA

Unless the Agency Contract specifically provides for the payment of liquidated damages/ compensation in the event of determination of the Agency Contract, in computing the compensation/ indemnity payable to the aggrieved Agent the Courts in India apply the rules for assessing damages/ compensation for other contracts. There is no fixed rule for determining the measure of damages, but must depend on the circumstances of each case.

There is no specific provision under the Indian Contract Act or any other law regarding the calculation of indemnity and/or compensation.

For the computation of compensation payable to the Agent the Court may take into consideration the amount the Agent would have earned, if the contract would not have terminated.

5 Indemnity and/or compensation for distributors and franchisee

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nity or compensation payable to distributors and franchisee is governed by the terms of the relevant contract and the Act. There is no specific law in India, which governs the payment of indemnity/ compensation to the distributors and franchisee and it is open to the parties to determine the conditions for payment and the amount of compensation. Where the contract is silent the indemnity and compensation is determined in accordance with the Act.



CONTACT

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