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Enabling Penalties and Missing the Goal: Rethinking Nepal's Erroneous Jurisprudence and Practice Concerning Liquidated Damages, and its Application in the Nepalese Public Procurement Regime

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Abstract

Liquidated damages are damages that are pre-determined by the parties to a contract before any actual damage takes place. Liquidated damage clauses act as limitation-of-liability clauses in contracts and serve a significant commercial purpose. However, if such clauses are not regulated, they can lead to potential misuse. For example, when excessively high and unconscionable liquidated damages clauses are imposed, such clauses ought to be classified as unenforceable penalties. It is in this regard that various jurisdictions had, early on, adopted a compensatory-penal dichotomy (rule against penalties) wherein compensatory liquidated damages clauses (based on a genuine pre-estimate of loss) were enforced and penal liquidated damages clauses were not. However, the rule against penalties, as developed in Nepal, requires liquidated damages to be compared against actual damages (rather than against a genuine pre-estimate of loss), thus creating an erroneous 'actual damages-penalty' dichotomy. Despite the existence of such a rule against penalties in Nepal (although erroneous in nature), Nepalese courts and arbitration tribunals, while adjudicating over liquidated damages clauses, ignore the rule against penalties and the probable penalty aspect of such clauses, and solely focus on the attributability of the damages suffered. Therefore, the existing Nepalese practice concerning liquidated damages is more erroneous than the existing Nepalese jurisprudence against penalties. The article refers to various foreign judgements and criticizes the practice concerning liquidated damages and the jurisprudence concerning penalties in Nepal and recommends the correct practice and jurisprudence that can be adopted. Since liquidated damages clauses are largely observed in Nepalese public procurement contracts and construction contracts, this article specifically highlights the error in the application of such jurisprudence and practice under various circumstances that arise during the enforcement of such agreements.

Keywords: *Liquidated Damages, Penalties, Public Procurement, Construction Disputes*

I. Introduction

Liquidated Damages ('LD' or 'LDs') or Liquidated and Ascertained Damages ('LAD' or 'LADs') are such damages which are pre-determined by the parties to the contract and are payable when

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a specified breach of the contract takes place, irrespective of what the actual loss may be.[1] Some examples of LDs include; bad leaver provisions, deposit amount forfeiture clauses,[2] withholding payment clauses, take-or-pay and take-and-pay clauses, money bonds, consent decrees, etc.[3] Therefore, when the parties to a contract determine the damages payable (in any form) even before any actual breach or damage takes place, such a clause is said to be an LD clause.[4]

However, while contractual party autonomy allows the inclusion of LD clauses in a contract, there can be instances where a party to a contract can misuse its bargaining power and include excessively high and unconscionable LD clauses (penalties).[5] While these clauses have been regulated due to substantial jurisprudential developments in many countries, the jurisprudence developed in Nepal and the practice in Nepalese courts and arbitration tribunals concerning the regulation of LD clauses has been lackadaisical, thus enabling penalties in civil disputes, which is not the objective (goal) of such clauses.[6] The existing jurisprudence against penalties in Nepal requires parties to establish 'actual damages' despite the prevalence of LD clauses, while the existing practice concerning LDs ignores the rule against penalties (although erroneous in nature), and enforces LD clauses as they are without having any regard to the probable penalty aspect of such clauses. Therefore, both the jurisprudence and the practice are gravely erroneous.

The application of LD clauses is largely observed in the Nepalese public procurement disputes since the Public Procurement Management Office ('PPMO') has issued a standard form of contracts for the procurement of works, goods, and services by the government entities, which include LD clauses (against delay), as has been suggested by the public procurement laws.[7] Therefore, this article specifically refers to the application of LDs in cases concerning public procurement (government contracts). Furthermore, since Nepalese courts and arbitration tribunals make extensive references to Indian jurisprudence, this article makes specific reference to Indian judgments, where appropriate.

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1 *Triple Point Technology, Inc. v. PTT Public Company Ltd.*, United Kingdom Supreme Court, 2021, UKSC 29, p. 74; Julian Bailey, *Construction Law,* Informa Law, New York, 2nd edition, 2016, p. 1185; *Steel Authority of India v. Gupta Brother Steel Tubes Ltd.*, Supreme Court of India, 2009, 10 SCC 63, p. 24 (where it was decided that parties can contract to make provision of LD applicable only for specified breach).

2 *Kailash Nath Associates v. Delhi Development Authority*, Supreme Court of India, 2015, 4 SCC 136; *Maula Bux v. Union of India*, Supreme Court of India, 1969, 2 SCC 554; *Fateh Chand v. Balkishan Das*, Supreme Court of India, 1963, SCC OnLine SC 49; *Godrej Projects Development Ltd. v. Anil Karlekar and Ors.*, Supreme Court of India, 2025, 4 SCC 259.

3 Fred Halbhuber, 'The Scope of Penalty Jurisdiction: A Critical Analysis of the Application of the Rule Against Penalties to Contentious Clauses', *The Oxford University Undergraduate Law Journal* p. 90, volume 11, 2022, pp. 93-94; J. Beatson, A. Burrows, J. Cartwright, *Anson's Law of Contract*, Oxford University Press, Glasgow, 31st edition, 2020, pp. 569-572; Rajesh Kapoor, *Avtar Singh's Contract & Specific Relief,* EBC Publishing, India, 13th ed., 2023, pp. 528-554.

4 But see *Muluki Dewani Sanghita* 2074 (National Civil Code 2017), Nepal, s. 537 (2) (This provision, that deals with LDs in Nepalese context, provides that LDs are determined at the time of entering into the contract. Nevertheless, this provision can be interpreted such that when parties agree on LDs after entering into a contract but before any actual damage ensues, then such agreement between the parties is a contract in itself, and therefore complies with the 'at the time of entering into the contract' requirement under the provision.)

5 Section IV(B) of the article; While contractual bargaining power can be misused to include excessively high LD clauses, it can also be misused to include excessively low LD clauses. See citations 16-19 below and the accompanying text therein.

6 Section IV and V of the article.

7 *Sarwajanik Kharid Ain*, 2063 (Public Procurement Act 2007), Nepal, s. 52(2)(n); *Sarwajanik Kharid Niyamawali*, 2064 (Public Procurement Rules 2007), Nepal, rule 121, 128(2)(c). However, see citation 82-84 below and the accompanying text therein.

II. Significance of LDs

LD clauses hold large importance in commercial practice since they provide certainty to the parties regarding their risks and liabilities.[8] It also serves as a deterrent to parties (that are subjected to LD clauses) from breaching the contract.[9] Such pre-determined damages also help the parties to make conscious decisions during the execution of the contract. In *Triple Point,*[10] it was decided that LD clauses serve two useful purposes: (a) avoiding the difficulty observed in the calculation of actual damage and; (b) limiting liabilities and providing certainty to the parties. The importance of LDs can be further discussed under the following headings:

A. Cap on Damages

LDs are considered as the exclusive remedy for the concerned breach.[11] The party that seeks damages is not entitled to claim damages that exceed the amount determined in an LD clause.[12] Furthermore, any provision of LDs would also restrict a party from electing to seek either liquidated or unliquidated (general) damages,[13] and the party is mandated to seek LDs. Even if an LD clause is determined to be a penalty or overall void, any reasonable compensation calculated as general damages also cannot exceed the amount so stated in such LD clause.[14] Therefore, LD clauses act as limitation-of-liability clauses.[15]

However, confusion arises when LDs are provided to be applicable at 'nil' or for nominal damages. In England, such clauses are said to limit a party's entitlement to general damages.[16] However, a different jurisprudence exists in Australia in this regard. In *Silent Vector,*[17] the parties had inserted 'N/A' next to a clause reading 'limit of liquidated damages', which was interpreted to mean that the clause would restrict recovery of LDs entirely but would allow the party to claim general damages. Similarly, there have been various judgements wherein it has been decided

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8 *Triple Point* (n 1), p. 35; *Eco World-Ballymore Embassy Gardens Co. Ltd v. Dobler UK Ltd.*, England and Wales High Court (Technology and Construction Court), 2021, EWHC 2207 (TCC); *Amev-Udc Finance Ltd. v. Austin*, High Court of Australia, 1986, 162 CLR 170; *Philips Hong Kong Ltd. v. Attorney General of Hong Kong*, Judicial Committee of the Privy Council, 1993, 61 BLR 41; see Julian Bailey (n 1) p. 1186.

9 Julian Bailey (n 1) p. 1186.

10 *Triple Point* (n 1), p. 74.

11 *Biffa Waste Services Ltd & Anor v. Maschinenfabrik Ernst Hese GmbH & Ors.*, England and Wales High Court (Technology and Construction Court), 2008, EWHC 6 TCC; *IPN Medical Centres Pty. Ltd. v. Van Houten, Supreme Court of Queensland, 2015, QSC 204*; *Camatos Holdings v. Neil Civil Engineering*, Court of Appeals, New Zealand, 1998, 3 NZLR 596; *but some courts have allowed parties to claim general damages even when a LD clause was prevalent in the contract. See Concrete Structures (NZ) Ltd. v. Waiotahi Contractors Ltd.*, High Court of New Zealand, 2012, NZCCLR 21 (wherein it was decided that the parties can seek general damages in substitute for LDs, citing *Mayor, Councillors, and Burgesses of Borough of Sydenham v. Poore*, Supreme Court of New Zealand, 1900, 19 NZLR 146)**; See also** *Crescendas Bionics Pte. Ltd. v. Jurong Primewide Pte Ltd.*, High Court of the Republic of Singapore, 2021, SGHC 189 (cap on LDs would not prevent the party from claiming general damages).

12 *Kailash Nath* (n 2) p. 43.1*; but see Buckingham Group v. Peel, England and Wales High Court (Technology and Construction Court), 2022, EWHC 1842 TCC* (where it was decided that a clause providing for a cap on maximum LADs would not be considered as a cap on overall liability).

13 *Surrey Heath Borough Council v. Lovell Construction Ltd., Court of Appeals of England and Wales,* 1988, 42 BLR 25.

14 *Eco World (n 8)***;** *Kailash Nath* (n 2), p. 43.1; *Clydebank Engineering and Shipbuilding Co v. Don Jose Ramos Yzquierdo y Castenada*, House of Lords, 1904, UKHL 3; *Elsely v. J G Collins Insurance Agencies Ltd.*, Supreme Court of Canada, 1978, 2 SCR 916.

15 *IPN Medical Centres (n 11); Eco World (n 8)***;** *Pigott Foundations Ltd. v. Shepherd Construction Ltd.*, England and Wales Queen's Bench Division, 1993, 67 BLR 48; David Chappell, *Building Contract Claims,* Wiley-Blackwell, UK, 5th ed., 2011, pp. 65-66.

16 *Temloc Ltd. v. Errill Properties Ltd.*, Court of Appeal, 1987, 39 BLR 30.

17 *Silent Vector Pty Ltd t/as Sizer Builders v. Squarcini*, Supreme Court of Western Australia, 2008, WASC 246.

that a clause limiting LDs to 'nil' or nominal damages would not prevent a party from claiming general damages.[18] Such jurisprudence largely exists due to the existence of jurisprudence which requires a clear intention of the parties to exclude general damages.[19]

B. No Requirement of Precise Calculation of Damages

In commercial contracts, it is usually difficult to determine the exact damage that a party might suffer due to a breach of contract. Therefore, the parties themselves can fix the damages payable in case any breach of contract takes place. This helps parties to overcome the difficulties in assessing precise damages.[20] Further, it would not matter if the actual damage is greater or smaller than the LD amount fixed.[21]

1. Indian Jurisprudence

In *ONGC v. Saw Pipes*,[22] it was decided that the person claiming LDs is not required to prove the actual loss or damage suffered. The court would be competent to provide reasonable damages even if actual damages are not proven. However, the judgment in *ONGC v. Saw Pipes* cannot be interpreted to mean that LDs can be claimed even if there is no damage caused by the breach.[23] The existence of damage (factum of loss) is a *sine qua non* to claim LDs.[24] However, such jurisprudence cannot be made applicable where an LD clause is sought to protect any legitimate interest.[25]

C. No Requirement to Mitigate Damages

A party that seeks enforcement of an LD clause is not required to mitigate the damage caused due to the breach,[26] unlike in situations where the party seeks unliquidated damages. It can be

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18 *Baese Pty Ltd v. RA Bracken Building Pty. Ltd.*, Supreme Court of New South Wales, 1990, 6 BCL 137; *Adapt Constructions Pty. Ltd. v. Whittaker & Anor*, Supreme Court of Australian Capital Territory, 2015, ACTSC 188; *Cappello v. Hammond & Simonds NSW Pty. Ltd.,* Supreme Court of New South Wales, 2020, NSWSC 1021; *Wentworth Shire Council v. Bemax Resources Ltd.*, Supreme Court of New South Wales, 2013, NSWSC 1047; *CS Phillips Pty. Ltd. v. Baulderstone Hornibrook Pty. Ltd.*, Supreme Court of New South Wales, 1994, 30 NSWSC 185; *Cappello v. Hammond & Simonds NSW Pty. Ltd.*, Supreme Court of New South Wales, 2020, NSWSC 1021 (where it was decided that nominal damages like $1 would not restrict a party from claiming general damages); but see *Onethree Pty Ltd. v. Seaman, New South Wales Civil and Administrative Tribunal, 2018, NSWCATCD 83 (Where $1 as LD was considered to be valid and the damages were limited to $1).*

19 *Baese Pty* (n 18); *Turner Corporation Ltd (Receiver & Manager Appointed) v. Austotel Pty Ltd.*, Supreme Court of New South Wales, 1994, 13 BCL 378; *H W Nevill (Sunblest) v. William Press & Sun*, Queen's Bench Division, 1981, 20 BLR 78; *Photo Production Ltd v. Securicor Transport Ltd.*, House of Lords, 1980, AC 827; *Hancock v. Brazier (Anerley) Limited*, Court of Appeals of England and Wales, 1966, 1 WLR 1317; *Billyack v. Leyland Construction Co. Ltd.*, England and Wales Queen's Bench Division, 1968, 1 WLR 471.

20 *Triple Point* (n 1), p. 74; *Eco World (n 8)*; *Clydebank Engineering* (n 14); *ONGC v. Saw Pipes*, Supreme Court of India, 2003, 5 SCC 705, p. 67.

21 *Triple Point* (n 1); *Amev-Udc* (n 8); *Adapt Constructions* (n 18); *Phillips Hong Kong v. Attorney-General of Hong Kong*, Privy Council, 1993, 61 BLR 41.

22 *ONGC v. Saw Pipes* (n 20), p.68; See *Maula Bux* (n 2); *GAIL (India) Limited v. Punj Lloyd Limited*, Delhi High Court, 2017, 240 DLT 610.

23 *Vishal Engineers & Builders v. Indian Oil Corporation Ltd.,* Delhi High Court, 2011, SCC OnLine Del 5124, p. 26.

24 *Kailash Nath* (n 2), p. 43.3; *MNTL v. Tata Communications Ltd., Supreme Court of India, 2019, 5 SCC 341, p. 11; Maharashtra State Electricity Distribution Company Ltd v. Maharashtra State Electricity Regulatory Commission*, Supreme Court of India, Civil Appeal no. 1843 of 2021, p. 33.

25 See Section V(A) of the Article.

26 *NPS, LLC v. Minihane*, Supreme Judicial Court of Massachusetts, 2008, 886 N.E.2d 670 (Mass.); *MSC Mediterranean Shipping Co. SA v. Cottonex Ansal*, England and Wales High Court, 2015, EWHC 283 (Comm); See generally George Perry, 'Recent Developments: Barrie School v. Patch: There Is No Duty for a Non-Breaching Party to Mitigate Damages When the Contract Contains a Valid Liquidated Damages Clause' *University of Baltimore Law Forum* p. 159,

logically argued that since damages payable are already pre-determined, mitigation of loss (by the party seeking LDs) can make no difference to the pre-determined LDs, which must, normally, be enforced as it is.

1. Indian Practice

However, there exists some jurisprudence, particularly in India, where the party that seeks enforcement of LDs is required to mitigate damages.[27] The courts in India developed such jurisprudence by erroneously extending the mitigation requirement developed in cases concerning unliquidated damages to cases concerning LDs.

III. Nepalese Practice Concerning LDs (All or Nothing Approach)

While jurisprudence concerning LDs has developed various pronouncements in various jurisdictions, such attention towards LD clauses has not been provided by the Nepalese courts, arbitration tribunals, and by parties in disputes alike. Despite the existence of Nepalese precedents against penalties (although erroneous in nature), the courts and arbitration tribunals in Nepal constantly fail to address the issue of penalties while dealing with LDs, and enforce them as they are – an 'all or nothing' approach (discussed in the paragraph immediately below).[28] A reason for such failure can be because the parties themselves fail to raise the issue of penalties[29] as the standard practice concerning LD clauses has been an 'all or nothing approach'.

Under the Nepalese practice, while adjudicating a dispute concerning LDs, only the attributability of the damages is adjudicated upon, which means that only the prevention principle is given due regard. The prevention principle provides that a party contributing towards the breach is not entitled to seek the advantage of its own breach.[30] This, however, is only one of the aspects that ought to be considered while adjudicating a dispute concerning LDs.[31] The Nepalese practice concerning the adjudication of disputes on LDs is limited to the issue of attributability and does not seek to determine if the LD clause itself is enforceable or not in the first place. Such practice creates an 'all or nothing approach'. For example, if 'A' seeks LD from 'B' at the rate of NPR 10,000/- against each day of delay for a total of hundred days (total LD claimed being NPR 1,000,000/-), and if 'A' is successful in establishing that the delay is entirely attributable to 'B', then 'A' will be awarded the whole of the LD claimed (i.e. NPR 1,000,000/-), and if the delay is attributable to 'A' entirely, then 'A' will not be awarded any LD. If only half of the delay is attributable to 'B' (i.e., for fifty days), then 'A' will be awarded half of the LD claimed (i.e., NPR 500,000/-). The rate or amount of LD is never in question, as under the standard Nepalese practice. No judicial mind is applied towards issues such as whether the LD claimed is a penalty or not, or if the LD clause is unenforceable in the first place due to any other reasons. It is for this reason (and for ease of understanding) that the author terms such a

volume 38:2, 2008; but see Lisa A. Fortin, 'Why there should be a duty to mitigate liquidated damages' *Hofstra Law Review* p. 285, volume 38, 2009.

27 *Manju Bagai v. Magpai Retail Ltd.*, Delhi High Court, 2010, Comp. Petition no. 193 of 2007, p.12-13; *Tower Vision India Pvt. Ltd. v. Procall Pvt. Ltd.*, 2014, Co. Pet. 458/2010 & CA No. 2179/2010; *Oil & Natural Gas Corporation Limited v. Oil Country Tubular Limited*, Bombay High Court, 2011, Arb. Petition no. 449 of 2007, p. 35.

28 *Everest Bank v. Rajiv Gajurel*, NKP 2071 (2014), volume 5, Decision no. 9165; *Nepal Airlines Corporation v. Anishman Shakya*, Supreme Court, 2079 (2022), Writ no. 078-CI-0057.

29 Courts cannot decide upon issues that have not been raised by the parties. See *Bhojraj Ghimire v. Ram Prasad Nayak*, NKP 2068 (2011), volume 1, Decision no. 8533, p. 8; *Arjun Prasad Bhandari v. Naresh Katuwal,* NKP 2080 (2024), volume 11, Decision no. 11203, p. 8

30 Julian Bailey (n 1), p. 1197-1201; David Chappell (n 15) p. 29; *Muluki Dewani Sanghita* 2074 (n 4), s. 10.

31 *BSNL v. Motorola India Pvt. Ltd.*, Supreme Court of India, 2009, 2 SCC 337.

standard approach as an 'all or nothing approach', as the applicable LD amount or rate is never under scrutiny, and the claim on LD is determined only on the grounds of attributability of the damages.

IV. Foreign Jurisprudence on LDs and Lessons for Nepal

Jurisprudence on LDs has been developing for centuries[32] in many foreign jurisdictions. Such foreign jurisprudential developments hold large importance for Nepal since the issues dealt with by such foreign judgements have almost never been dealt with by the Nepalese courts and arbitration tribunals. This Section discusses such foreign judgements concerning LDs propounded under various circumstances and how such judgements can be of use for Nepal.

A. Issue of Unilateral Determination

No party to a contract can have the exclusive and final right to determine the amount payable as LD.[33] Even if a party has the discretion to assess the LD arising out of a breach of a contract (which cannot be mis-used),[34] the same party cannot be said to have a final right to determine the LD payable due to a clear conflict of interest.[35] A breach of contract does not *eo instant* incur any obligation on the party at breach, but creates a right on the other party to sue for damages.[36] Therefore, a party to a contract cannot unilaterally and finality determine the LD payable, but can only sue to seek such LD (in case of a conflict).

By following the 'all or nothing approach', Nepalese practice (partially) allows unilateral determination of LDs since the amount or rate of LD is never questioned. Such practice opens an avenue where the party imposing the LD can impose excessively high LD, without any risk of adjudication concerning the amount or the rate of LD. This violates the fundamental right to fair trial by an independent, impartial, and competent court or judicial body.[37] Such practice opens avenues to enable penalties in contractual matters and should therefore be abolished.

B. Genuine Pre-estimate of Loss v. Penalty

[Before beginning with the discussions concerning genuine pre-estimate of loss (genuine compensation) and penalties,

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32 William H. Loyd, 'Penalties and Forfeitures: Before Peachy v. Duke of Somerset', *Harvard Law Review* p.117, volume 29:2, 1915; MP Ram Mohan et. al., 'Liquidated Damages in India: Concepts, Enforceability, and Drafting Considerations', *Working Paper No. 2024-12-02,* Indian Institute of Management Ahmedabad, 2024, pp. 5-9; Larry A. DiMatteo, 'An Examination of Judicial Reasoning – When a Penalty Is Not a Penalty', *The George Washington Law Review* p. 1846, volume 85:6, 2017, pp. 1847-1858.

33 *BSNL* (n 31); *JG Engineers Pvt. Ltd. v. Union of India*, Supreme Court of India, 2011, AIR SC 2477, p.17; *Winner Constructions Pvt. Ltd. v. Union of India*, Delhi High Court, 2016, Arb. P. 78/2016; see Rajesh Kapoor (n 3), pp. 536-538; but see *Mitra Guha Builders (India) v. ONGC*, Supreme Court of India, 2019, AIROnline SC 2447; *Vishwanath Sood v. Union of India*, Supreme Court of India, 1989 AIR 952 (where it was decided that disputes relating to LDs were not arbitrable as it was already finally decided by the superintending engineer).

34 *Mid-Essex Hospital Services NHS Trust v. Compass Group*, England and Wales Court of Appeal, 2013, BLR 265 *("[…] the relevant party [cannot] exercise its discretion in an arbitrary, capricious or irrational manner."*)

35 *JG Engineers* (n 33); *State of Karnataka Etc. v. Shree Rameshwara Rice Mills*, Supreme Court of India, 1987, AIR 1359; *Tulsi Narayan Garg v. The MP Road Development Authority,* 2019, AIR Online SC 1050, p. 11-12; But some judgements have upheld the contractual right of unilateral determination provided to one of the parties citing the reasons of party autonomy and limited court interference in contractual matter. See *Braganza v. BP Shipping,* Supreme Court of the UK, 2015, UKSC 17; see also *TAQA Bratani Ltd. v. RockRose,* England and Wales King's Bench Division, Commercial Court, 2020, EWHC 58 (Comm).

36 *Socimer International Bank Ltd v. Standard Bank London Ltd.*, England and Wales Court of Appeals, 2008, EWCA Civ 116, 66.

37 *Nepal ko Sambidhan* (Constitution of Nepal), art. 20(9).

it should be noted that the jurisprudence concerning compensatory-penal dichotomy has been subjected to change by the introduction of the 'legitimate interest test' in England and in other jurisdictions (discussed under Section V (A) below). However, a discussion on the compensatory-penal dichotomy (rule against penalties), although outdated (but not abolished),[38] is important to highlight how the Supreme Court of Nepal erred in its attempt to adopt such rule against penalties into the Nepalese jurisprudence.]

It is well established that LDs that are compensatory in nature are enforceable, while LDs that are in the nature of penalties are not. The test as to whether an LD clause is a penalty or not is a test of substance and not of form,[39] and therefore requires a careful application of the judicial mind. Nepalese courts and arbitration tribunals usually draw large references from the English and Indian jurisprudence, during their application of the judicial mind. Therefore, this Section specifically summarizes the jurisprudence in these jurisdictions concerning unenforceable penalties under the compensatory-penal dichotomy.

1. English Jurisprudence

The compensatory-penal dichotomy has existed for a long time in England.[40] LDs that are genuine pre-estimates of loss (i.e., compensatory) are enforceable[41] and LDs that are penalties are not.[42] If any LD clause is found to be disproportionately excessive, extravagant, or unconscionable in comparison to the greatest loss that could conceivably be proven (for the concerned breach), then such clause is a penalty.[43] The opportunity of the party, which is subjected to an LD clause, to appreciate what they were agreeing upon is also a relevant factor to determine whether an LD clause is in the nature of penalty.[44] Therefore, LD clauses in standard form of contracts can be penal in nature, depending on the circumstances of the case.

2. Indian Jurisprudence

The Indian legislation had sought to not adopt the English compensatory-penal dichotomy.[45] However, despite legislative attempts, the courts in India eventually read into the English compensatory-penal dichotomy within Section 74 of the Indian Contract Act, 1872.[46] In India as well, LDs are not enforceable if they are in the nature of penalty.[47] In *Kailash Nath Associates*,[48] it was determined that LD mentioned in a contract is only payable if it is

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38 J. Beatson (n 3) p. 568; George Perry (n 26), pp. 20-22; *Cavendish Square Holding BV v. Talal El Makdessi*, *ParkingEye Ltd. v. Beavis*, 2015, UKSC 67, pp. 36-39, 162-167, 251-265 (the Court noted that with regard to straightforward damages clauses, the compensatory-penal dichotomy test in *Dunlop* would be adequate to determine its validity).

39 *Clydebank Engineering* (n 14); J. Beatson (n 3) p. 569; *Dunlop Pneumatic Tyre Co Ltd v. New Garage & Motor Co. Ltd.,* House of Lords, 1915, AC 79 (it was decided that the use of the term penalty or LD in a contract cannot be considered to be a conclusive factor in determining the nature of the clause); *BSNL v. Reliance Communications Ltd.*, Supreme Court of India, 2011, Civil Appeal no. 6706 of 2010, p. 17; *Jobson v. Johnson*, Court of Appeal, 1989, 1 WLR 1926; *Andrews v. Australia and New Zealand Banking Group Ltd.*, High Court of Australia, 2012, 247 CLR 205.

40 The jurisprudence can be traced back to the case of *Astley v. Weldon,* House of Lords, 1801, 2 Bos & Pul 346.

41 *Dunlop* (n 39).

42 Ibid; *Cavendish* (n 38); *Eco World (n 8).*

43 *Eco World (n 8); Clydebank Engineering* (n 14); *Dunlop* (n 39).

44 *Eco World (n 8).*

45 *Fateh Chand* (n 2), p. 8*; ONGC v. Saw Pipes* (n 20), p. 51; *Union of India v. Raman Iron Foundry*, Supreme Court of India, 1974, 2 SCC 231, p. 11; Shivprasad Swaminathan, 'De-inventing the Wheel: Liquidated Damages, Penalties and the Indian Contract Act, 1872', *The Chinese Journal of Comparative Law* p. 1, volume 6:1, 2018, pp.8-11.

46 Shivprasad Swaminathan (n 45), pp.8-11.

47 *ONGC v. Saw Pipes* (n 20), p. 68; *KP Subbarama Sastri & Ors. v. KS Raghavan & Ors., Supreme Court of India*, 1987, AIR 1257

48 *Kailash Nath* (n 2), p. 43.1; *ONGC v. Saw Pipes* (n 20), p. 68; *Maula Bux* (n 2), p. 6.

a 'genuine pre-estimate of damages'. The Supreme Court of India has affirmed that the grounds to determine whether an LD clause amounts to a penalty are; (a) the character of the transaction and its special nature; (b) the relative situation of the parties; (c) the rights and obligations accruing from such transaction and, (d) intention of the parties.[49] Therefore, if there exists an LD clause in a standard form of contract (where there exists unequal bargaining power between the parties), the clause can be penal, depending on the circumstances of the case.[50] If any LD clause is incorporated in a manner that is burdensome or oppressive to the party that pays the LD in case of a default, such provisions are considered to operate *in terrorem,* and are thus considered to be a penalty.[51]

While the English and the Indian jurisprudences concerning the compensatory-penal dichotomy are largely similar, there exists one substantial difference in the jurisprudence between these two jurisdictions. The term *"whether or not actual damages or loss is proved to have been caused thereby"* as used under Section 74 of the Indian Contract Act, 1872, has been interpreted to mean that where it is possible for a party to prove actual damages or loss, such requirement of proof is not dispensed with.[52] It is only in cases where it is difficult or impossible to ascertain the quantification of damages that LD can be awarded (provided that they are a genuine pre-estimate of damage or loss).[53] Therefore, while English jurisprudence does not require the party invoking the LD clause to establish that it is impossible or difficult to prove actual damages, Indian jurisprudence does.[54] However, such a requirement undermines the commercial significance of LD clauses, which are included for the very reason that it gets difficult to establish a precise calculation of damages suffered.

3. Nepalese Jurisprudence on Penalties

In 2010, the Supreme Court of Nepal provided two judgements that devised the Nepalese rule against penalties in civil cases. However, the jurisprudence developed by the Supreme Court is different than observed in India or England. The Supreme Court erred in its attempt to adopt the rule against penalties as developed in foreign jurisdictions.

a. Amar Adarsha Madhyamik Bidhyalaya v. Krishna Bahadur Shrestha[55]

In this case, the Supreme Court, having reference to Section 83(2) of the (then current) Contract Act, 2000 (2056 B.S.),[56] devised a rule against penalties in civil suits. The Court, based on the language used in Section 83(2), decided that courts are not bound to provide LDs as included in the contracts but that the LD amount is only to be considered as the upper limit of allowable compensation. Within such an upper limit

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49 *KP Subbarama Sastri* (n 47).

50 See MP Ram Mohan et al., 'Indian Law on Standard Form Contracts' *Journal of Indian Law Institute,* p.413, volume 62:4, 2020.

51 *K.P. Subbarama Sastri* (n 47); *Cellulose Acetate Silk Co Ltd v. Widnes Foundry*, House of Lords, 1933, AC 20.

52 *Kailash Nath* (n 2), p.43.6; *Maula Bux* (n 2), p. 6-7.

53 *Kailash Nath* (n 2) p. 43.1; *Fateh Chand* (n 2)*; Raman Iron Foundry (n 45), p.11 ("as the law in India is concerned, there is no qualitative difference in the nature of the claim whether it be for liquidated damages or unliquidated damages"*); *MNTL v. Tata Communications Ltd., Supreme Court of India, 2019, 5 SCC 341; Maya Devi v. Lalta Prasad, Supreme Court of India, 2014, AIR SC 1356.*

54 Shivprasad Swaminathan (n 45), pp.11-15.

55 *Amar Adarsha Madhyamik Bidhyalaya v. Krishna Bahadur Shrestha*, NKP 2068 (2010), volume 8, Decision no. 8635.

56 *Karar Ain* 2056 (Contract Act, 2000), s. 83 (2).

of allowable compensation, courts can determine the 'actual damages' payable.[57]

The Court decided that a breach of contract cannot lead to automatic payment of the LD determined in the contract. It was decided that if the amount of LD is excessive or unreasonable, the party that is claiming LD can gain 'unjust enrichment' and in such situations, the LD clause should be determined to be a penalty, which is not enforceable in a civil dispute.[58] The Court observed that in civil suits, even the State does not have the requisite authority to create laws to impose penalties.[59] It was further decided that if the amount of LD is in excess of the 'pre-estimation of actual loss' caused due to the breach of the contract, such LD is in the nature of a penalty. The judgement also established that the existence of a loss should be established to claim LDs.[60] It was further decided that where a party fails to establish (prove) the LD amount claimed, or if the LD claimed is in excess of the amount established (proved), courts cannot enforce the LD clause as it would result in legalization of penalties in civil cases. The judgement established that the party that is claiming LD must be able to prove and satisfy the court, based on evidence and reason, that the LD claimed is based on 'actual and reasonable damages'.[61]

b. Bekha Maharjan v. Pawan Kumar K.C.[62]

In this case, the Supreme Court devised a (slightly different) rule against penalties. The Court decided that courts should differentiate as to whether the LD clause is a 'penalty' or an 'actual pre-estimate of a loss'. It was decided that the concept of penalties is unknown to civil disputes,[63] and that where the LD claimed is more than 'actual damages', it becomes a penalty. The Court compared the relevant provisions under the old Contract Act of 1966 (2023 B.S.) and the (then current) Contract Act of 2000 (2056 B.S.) and observed that the provision under Section 15(2) of the old Contract Act, 1966 (2023 B.S.)[64] provided that the amount determined as damages (LD) as under the contract would be payable as damages in case of breach of contract, but the provision under Section 83(2) of the (then current) Contract Act, 2000 (2056 B.S.) provided that where any amount is pre-determined as damages, reasonable damages not exceeding the said amount can be provided.[65] Additionally, it was decided that Section 83(2) of the Contract Act, 2000 (2056 B.S.) provided a large discretionary power to the courts and that the courts are required to determine the 'actual damages' payable, within the limit determined by the parties.[66] Even where the factum of damages is proved, it is not necessary for courts to provide LDs as included in the contract. It was concluded that there exists no unconditional right of a party to a contract to claim LDs.[67]

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57 *Amar Adarsha* (n 55).

58 Ibid., p. 6

59 Ibid., p. 6

60 Ibid., p. 6

61 Ibid., p. 6

62 *Bekha Maharjan v. Pawan Kumar K.C.,* NKP 2067 (2010), Volume 5, Decision no. 8382.

63 Ibid., p. 5.

64 *Karar Ain* 2023 (Contract Act, 1966), s. 15 (2).

65 *Bekha Maharjan* (n 62).

66 Ibid., p. 5.

67 Ibid., p. 5.

The judgement in *Amar Adarsha* is slightly different from the judgement in *Bekha Maharjan,* as the latter does not make reference to the principle of unjust enrichment.

c. Critical Analysis of the Nepalese Rule Against Penalties

The current National Civil Code, 2017 (2074 B.S.), as under Section 537(2)[68] contains a provision similar to that under Section 83(2) of the Contract Act, 2000 (2056 B.S.). Therefore, the judgements in *Amar Adarsha* and *Bekha Maharjan* are applicable under the present Civil Code as well. Similarly, the criticisms concerning these judgements are relevant in the present context. The judgements in *Amar Adarsha* and *Bekha Maharjan* are concerning for various reasons. While the Court was correct in its conclusion that LD clauses form the upper limit for compensation, it has, however, severely undermined the commercial importance of LD clauses. The Court decided that a party that is claiming LD should establish the 'actual loss' caused due to a breach, instead of being required to establish that the LD applicable is a 'genuine pre-estimate of a loss'. Furthermore, despite the clear use of the term 'reasonable damages' under Section 83(2) of the Contract Act, 2000 (2056 B.S.), the Court decided that a party that is seeking LD would be required to establish 'actual damages'. The Court ignored the fact that one of the reasons that parties include an LD clause is because it mostly gets difficult to establish actual loss in civil disputes. By requiring parties to establish actual damages, the benefit of an LD clause under which the parties are only required to establish 'genuine pre-estimate of a loss' rather than 'actual damages', is lost. Therefore, the court has erred in deciding that an LD clause would be a penalty if the amount determined thereunder exceeds the 'actual damages' suffered. Furthermore, the use of the term 'pre-estimation of actual loss' in the judgement in *Amar Adarsha* is a paradox in itself.[69]

The judgement in *Amar Adarsha* has referred to the concept of unjust enrichment[70] while determining if an LD clause is a penalty or not. This further confirms that the Supreme Court intended to judge LD clauses based on 'actual damages', and that if an LD clause exceeds such actual damages, leading to unjust enrichment, the clause should be seen as a penalty. However this jurisprudence is erroneous. The purpose of an LD clause is to determine a 'genuine pre-estimate of a loss', which is not required to align with actual damages, and therefore, the concept of unjust enrichment is not applicable where the LD clause is applicable.[71] For example, if

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68 *Muluki Dewani Sanghita* 2074 (n 4), s. 537 (2).

69 Andrew Burr, *Delay and Disruption in Construction Contracts,* Informa Law, New York, 5th edition, p. 946 (where the author, while dealing with quantification of predictive losses quoted Francis Bacon, *Of Prophecies*, at p.35 "Dreams and predictions ought to serve but for winter talk by the fireside.")

70 The principle of Unjust Enrichment is applicable where a party gains anything more than it should have. See *Ram Prasad Bhandari v. Torand Karki*, NKP 2080 (2022), volume 3, Decision no. 11048; *Devi Khatri v. Dev Bahadur Gurung*, NKP 2079 (2022), volume 11, Decision no. 10969; *Tul Ratna Bajracharya v. Tara Shrestha Patrawangsha*, NKP 2077 (2019), volume 8, Decision no. 10548; *Radhe Shyam Singhaniya v. Tax Office of His Majesty's Government*, NKP 2050 (1993), volume 9, Decision no. 4795.

71 Alvin W.L., 'An Introduction to the Law of Unjust Enrichment', *Malayan Law Journal* p.i., volume 5, 2013 *"the agreed liquidated damages clauses ousted any unjust enrichment claim. The right to recover the part payment and damages for the delay were derived from the contractual terms. The causative event is the parties' consent and not unjust enrichment"*; It is only when a contract includes an unlawful penalty that general damages can be sought (within the limit of the amount determined in the LD clause) and unjust enrichment can be considered. See *Spirit Locker Inc. v. EVO Direct LLC,* United States District Court, E.D. New York, 2010, 696 F.Supp.2d 296, p. 305 (EDNY).

an LD clause provides that the damages payable for a breach of a contract is NPR 1,00,000/-, but the actual damages suffered is calculated to be only NPR 95,000/-, such LD clause would be a penalty under the current Nepalese jurisprudence since the party claiming LD has received an unjust enrichment of NPR 5,000/-, which is required to be restituted.[72] Under the current Nepalese jurisprudence, the LD clause in the example above would be a penalty, while under foreign jurisprudence, it would qualify as a 'genuine pre-estimate of a loss', and would therefore be enforceable.

Further, by deciding that the courts have large discretionary power to determine the damages payable, the judgment in *Amar Adarsha* has undermined the autonomy of the contracting parties.[73] The Court, while reading Section 83(2) of the Contract Act, 2000, (2056 B.S.), misinterpreted the provision and the use of the term 'reasonable compensation' therein. Based on the use of such a term, the Court decided that courts have discretionary power to determine the damages payable. However, where the parties to a contract have agreed upon a valid LD clause, the jurisdiction/power of a court is circumscribed by such a clause.[74] Minimal court interference has been an accepted rule with regard to valid LD clauses.[75] The use of the term 'reasonable compensation' in the provision cannot lead to the conclusion that the courts have been provided with a discretionary power to determine the damages payable by overriding the contractual party's autonomy. Courts are required to give effect to the clear and express intent of the parties,[76] and should first resort to a literal interpretation of the contractual provision.[77] Such jurisprudence has been propounded to protect contractual party autonomy and to restrict unnecessary court interference. Therefore, by enabling unnecessary interference in contractual matters, the judgment in *Amar Adharsha* has violated well-established jurisprudence concerning contract law.

Additionally, the Supreme Court in *Amar Adarsha* and *Bekha Maharjan* has exceeded its jurisdiction, which is circumscribed by legal provisions. Courts do not have the requisite authority to provide judgments against clear legislative provisions and intent.[78] Requiring parties to establish 'actual damages' despite the clear use of the term 'reasonable compensation' by the legislature under Section 83(2) of the Contract Act, 2000 (2056 B.S.) is gravely erroneous. Therefore, the judgements also violate the principle of separation of power as the Court essentially undertook a legislative function in them.[79]

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72 *Bekha Maharjan* (n 62), p. 7 (which discusses the principle of restitution).

73 *Muluki Dewani Sanghita* 2074 (n 4), s. 507; See *Pawan Raj Bhandari v. Ram Shrestha,* NKP 2078 (2021), volume 8, Decision No. 10724, p. 28.

74 *Krishi Samagri Sangsthan v. Milimili Enterprises*, NKP 2066 (2009), volume 4, Decision No. 8128, p. 9; *Umakant Jha on behalf of Mahakali Sinchai Pariyojana v. Appellate Court Patan*, NKP 2066 (2009), volume 5, Decision No. 8156. p. 10.

75 *Alfred McAlpine Capital Projects Ltd v. Tilebox Ltd.*, England and Wales High Court (Technology and Construction Court), 2005, 104 Con LR 39, p. 50; *Lordsvale Finance v. Bank of Zambia*, Queen's Bench Division,1996, 3 WLR 688; *Indian Airlines v. GLA International*, England and Wales King's Bench Division, 2002, EWHC 2361 (Comm).

76 *Himalayan Bank Ltd. v. Durgadevi Dhungel and Ors.*, NKP 2065 (2008), volume 2, Decision No. 7935, p. 7; See also, *Bangalore Electricity Supply Co. Ltd. (BESCOM) v. E.S. Solar Power Pvt. Ltd.*, Supreme Court of India, 2021, AIR 3418, p. 16

77 *Salt Trading Corporation, Nepalgunj v. Prachanda Bahadur Bum*, NKP 2072 (2015), volume: 9, Decision no. 9473, p. 3 (where it was decided that interpretation of contract must be done as per the rule of interpretation of laws.)

78 *Lok Bhakta Shumsher Ja.Ba.Ra. v. Rama Devi Rajbhandari,* NKP 2055 (1999), volume 11, Decision no. 6625, p. 20; *Government of Nepal v. Raju Lama*, NKP 2071 (2014), volume 5, Decision no. 9164, p. 5.

79 *Kamlesh Dwivedi v. Office of the Prime Minister and Cabinet Ministers and Ors.*, NKP 2067 (2010), volume: 9, Decision no. 8452, p. 10; *Kamlesh Dwivedi v. Office of the Prime Minister and Cabinet Ministers and others*, NKP 2064 (2007), volume 7, Decision no. 7866, p. 26.

The current Nepalese jurisprudence concerning LD clauses is problematic since it defeats the very fundamental purpose of such clauses. Further, the Supreme Court has also erroneously equated the concepts of unjust enrichment and penalties. These judgements have created an erroneous dichotomy of 'actual damages-penalty'. However, even so, the judgements in *Amar Adarsha* and *Bekha Maharjan* cases do not validate the 'all or nothing' approach, which has been a standard practice in Nepal. Therefore, while the jurisprudence laid down in *Amar Adarsha* and *Bekha Maharjan* unreasonable restrict the application of penalties, the 'all of nothing' approach (which is in practice despite the judgements in *Amar Adarsha* and *Bekha Maharjan*) is what enables the application of penalties.[80]

4. Lessons for Nepal

From the discussions above, some lessons that can be traced for Nepal are summarized as such:

a. Rethinking the Existing Rule Against Penalties

The discussions above establish that there is a need for Nepal to discard the flawed 'actual damages-penalty' dichotomy and adopt the 'compensatory-penal' dichotomy (along with the newly introduced 'legitimate interest test').

b. The Risk Concerning Standard Form of LD Clauses

Foreign judgements concerning LDs and the standard form of contracts[81] can also serve as a caution to the Nepalese Government regarding the strict use of LDs *via* a standard form of contract. Public procurement law provides that LDs can be levied normally at a rate of 0.05 percent of the contract amount against each day of delay.[82] The use of the term 'normally' implies that flexibility should be granted to employers under government contracts when determining the rates at which LDs can be applied. However, in practice, the standard form of bid documents drafted by the PPMO fixes the LD rate at 0.05 per cent of the contract amount against each day of delay. Such practices enable penalties that can make LD clauses in public procurement contracts unenforceable. Furthermore, noting the development in Nepalese jurisprudence against misuse of standard form of contracts, there already exists a risk where LD clauses in such contracts can be unenforceable.[83]

It has been well accepted that the government enters public procurement contracts on equal footing with private parties, and therefore cannot seek any special sovereign advantage in such contractual matters.[84] Additionally, the judgement in *Amar Adarsha*

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80 Section IV (B) (3) of the Article.

81 *Golden Bay Realty Pte. Ltd. v. Orchard Twelve Investments Pte. Ltd.*, The Court of Appeal of Singapore, 1991, UKPC 28, where it was decided that the rule against penalties is not applicable to statutory LDs.

82 *Sarwajanik Kharid Niyamawali*, 2064 (Public Procurement Rules 2007), Nepal, rule 121(a), 128(2)(c).

83 *Pawan Raj Bhandari* (n 73), para. 13; Also see Sankalpa Koirala, 'Questioning the 'Safe' in 'Safe Deposit Locker Services' of Class-A Banks vis-à-vis the International Jurisprudence on Contracts and Consumerism', *Kathmandu School of Law Review* p. 66, volume 13, 2024.

84 *Krishna Manandhar v. The Constituent Assembly*, NKP 2067 (2010), volume 3, Decision no. 8327; *Department of Roads v. Appellate Court, Patan*, NKP 2077 (2018), volume 3, Decision no. 10461; *NECT-Him Consult JV v. Ministry of Energy*, NKP 2074 (2016), volume: 1, Decision no. 9753.

itself, although erroneous with regard to its decision on penalties, has laid down a valid decision that in civil matters, even the State does not have the requisite authority to create laws to impose penalties. Based on such jurisprudence, the practice of fixed LD clauses–as used in the standard form of contracts drafted by the PPMO–can be unenforceable.

Therefore, the jurisprudence developed with regard to standard form of contracts, equal-footing in government contracts, restriction on the state to create laws to seek penalties, along with the erroneous 'actual damages–penalty' dichotomy and the principle of *contra proferentum* severely weaken the government's attempt to seek fixed LD under government contracts.[85]

V. Additional Foreign Jurisprudence and Lessons for Nepal

Since foreign jurisdictions have dealt with liquidated damages for centuries, they have developed advance jurisprudence on LDs, which complies with the modern economic system. Such jurisprudence contains great lessons for Nepal.

A. The Legitimate Interest Test

English jurisprudence adhered to the compensatory-penal dichotomy for a long time without any regard to the legitimate interest parties sought to protect through an LD clause.[86] However, this position changed in the combined case of *Cavendish Square Holding BV v. Talal El Makdessi* and *ParkingEye Ltd. v. Beavis* (hereinafter, referred to collectively as 'the combined case in *Cavendish*' and individually as '*Cavendish*' and '*ParkingEye*' respectively).[87] In the case of *Cavendish*, the respondent had agreed to sell their controlling stake in a company to the appellant where they were subjected to various restrictive covenants under the contract, which, if violated, would trigger an LD clause. The LD clause provided that the respondent would not be entitled to receive the final two installments and would also be required to sell their remaining shares to the appellant at a reduced valuation. In this, the Court determined that the LD clause was not a penalty.

The true test, as per the Court, was whether an LD clause was a secondary obligation which imposes a detriment on a contract breaker 'out of all proportion' to any 'legitimate interest' of the party (i.e. the party that is seeking LD) in the enforcement of a primary obligation.[88] Herein, it becomes important to differentiate between primary and secondary obligations. Primary obligations can simply be understood as considerations under contract,[89] while secondary obligations are contingent upon breach of primary obligations and act as alternatives to common law damages/general damages.[90]

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85 *Peak Construction (Liverpool) Ltd v. McKinney Foundations Ltd.*, England and Wales Court of Appeal, 1970, 1 BLR 111, p. 121.

86 *Philips Hong Kong* (n 8); Shivprasad Swaminathan (n 45), p. 3; Lord Atkinson, in *Dunlop,* had suggested a test to determine the propriety of interest sought to be protected. However, the eventual interpretation of *Dunlop* by the courts limited its scope of the compensatory-penal approach.

87 *Cavendish* (n 38).

88 Ibid, p. 32, 74; See *Vivienne Westwood Ltd. v. Conduit Street Development Ltd.*, England and Wales High Court, 2017, EWHC 350 (Ch).

89 *Cavendish* (n 38), p. 74

90 Fred Halbhuber (n 3), pp. 95-98; See *Photo Production Ltd. v. Securicor Transport Ltd.*, UK House of Lords, 1980, AC 827.

With regard to the legitimate interest test, the Court in the combined case of *Cavendish* decided that an LD clause can be included for reasons other than to recover compensation for a breach. A party can have a legitimate interest which can extend beyond the prospect of pecuniary compensation flowing from the breach.[91] However, the Court decreed that a party to a contract cannot have any interest in unnecessarily punishing the defaulter. Criticizing the 'artificial classification' in the law concerning the compensatory-penal dichotomy, the judgement provided that first, whether there exists any legitimate business interest that is sought to be protected by an LD clause should be determined and second, whether the clause is extravagant, exorbitant, or unconscionable, despite the existence of a legitimate interest should be decided.[92] While introducing the legitimate interest test, it was clarified that 'penalty' and 'genuine pre-estimate of loss' are not natural opposites or mutually exclusive categories as considered under the compensatory-penal dichotomy.[93] However, the traditional 'genuine pre-estimate of damages' test and the jurisprudence developed therein was rightly not abolished by the Court, and continues to be a usual means to determine whether an LD clause is a penalty or not.[94]

Similarly, in *ParkingEye Ltd. v. Barry Beavis*, a condition attached to a parking service was that if any person failed to comply with the two-hour parking time limit, it would result in a parking charge of 85 Euros.[95] Barry Beavis challenged the condition as a penalty. In this regard, the Court decided that questioning whether the clause was a 'genuine pre-estimate of a loss' was not helpful since LD clauses cannot be considered a 'penalty' just because it is not a 'genuine pre-estimate of a loss'. The Court thus checked if the clause served any legitimate interest.[96] It was decided that a conditional primary obligation cannot be a penalty,[97] and that the true test is whether a secondary obligation imposes a detriment 'out of all proportion' to any legitimate interest of the party (i.e. the party that is seeking LD) in the enforcement of a primary obligation.[98] The test for penalty is based on whether the amount of LD is exorbitant or unconscionable with regard to the party's interest in performance of the contract.[99] Finally, the Court decided that the charge of 85 Euros was a conditional primary obligation and that it served a legitimate interest for the business since it ensured efficient use of the parking service and generation of income to run the scheme and therefore, could not be considered as a penalty.[100]

The test laid down in the combined case of *Cavendish* has been referred to in various UK jurisdictions. In *Gray v. Braid Group,* the clause in question required a shareholder, who, if dismissed from their employment or directorial role in the company due to gross misconduct, would risk losing the value added to their shares since their subscription.[101] The clause was found to serve a legitimate business interest and was therefore decided to be valid. In *Signia Wealth Ltd. v. Vector Trustees Ltd.*, the concerned LD clause provided that a private start-up company

91 *Cavendish* (n 38), p. 28.

92 Ibid, p. 31.

93 Ibid, p. 152.

94 J. Beatson (n 3) p. 568; George Perry (n 26), pp. 20-22; *Cavendish* (n 38).

95 *ParkingEye (n 38).*

96 Ibid, p. 32

97 Ibid, p. 14

98 Ibid, p. 32; See *Vivienne Westwood* (n 88), where a clause was found to be disproportionate to any 'legitimate interest' sought to be protected.

99 *ParkingEye* (n 38).

100 Ibid, p. 98.

101 *Gray v. Braid Group*, Court of Session, Inner House, Scotland, 2016, 8 WLUK 293.

would be entitled to receive a compulsory transfer of the company's promoter shares held by its employees, during their exit, at a significant undervalue.[102] Noting that the company was a start-up, it was decided that the company had a legitimate interest in ensuring that the shareholding was not diffused and remained retained with the company itself. Further, it was noted that the LD clause also incentivized the employees to retain and perform their jobs. Similarly, an increase in the rate of interest payable in case of default in payment has also been said to comply with the test laid down in the combined case of *Cavendish*.[103] Further, having reference to the loss of opportunity due to delay in project completion, it has been decided that the higher LD applicable (against delay) came within the ambit of the 'legitimate interest test'.[104] Referring to the combined case of *Cavendish*, it was decided in *Eco World,* while upholding an LD clause (against delay) that the employer had a legitimate interest in the timely completion of the project.[105] Further, in *Eco World,* the Court also noted that the parties were aware of the contractual clauses and that the contract was negotiated by sophisticated parties.

Various jurisdictions have adopted the legitimate interest test after the decision in the combined case of *Cavendish*. The charge of late payment fees has been found to protect legitimate interests of a lender.[106] The application of an interest rate against late payment, secured through a settlement agreement has been considered to fulfil the legitimate interest test.[107] The levy of an increased interest rate by a lender has been found to be in compliance with the legitimate interest test.[108] Rental and ancillary amount recoverable by a tenant (which was a primary school) upon the failure of the landlord to install a second lift, has been said to be a valid LD clause since the tenant has a legitimate interest in securing the construction of a second lift.[109] The forfeiture of deposited money (3.33 percent of the total contract amount) by a prospective buyer was decided to be within the legitimate interest of the seller who sought timely sale of the property. It was decided that the clause was also meant to prevent the seller from entering negotiations with other third parties for the sale of the property.[110] In all these cases, the concerned LD clauses were not considered to be a penalty.[111]

1. The 'Legitimate Interest Test' in India

Although various jurisdictions have adopted the legitimate interest test, India has not. While various Indian Courts have referred to the judgement in the combined case of *Cavendish,* the test has not been yet adopted in Indian jurisprudence.[112] A major reason can be because

102 *Signia Wealth Ltd. v. Vector Trustees Ltd.,* England and Wales High Court, 2018, EWHC 1040 (Ch).

103 *ZCCM Investment Holdings Plc. v. Konkola Copper Mines Plc., England and Wales High Court*, 2017, EWHC 3288 (Comm); See *Cargill International Trading Pte. Ltd. v. Uttam Galva Steels Ltd.*, High Court of Justice, Queen's Bench Division, 2019, EWHC 476 (Comm).

104 *GPP Big Field LLP v. Solar EPC Solutions SL*, England and Wales High Court, 2018 EWHC 2866 (Comm).

105 *Eco World (n 8).*

106 *Paciocco v. Australia and New Zealand Banking Group Ltd.,* High Court of Australia, 2016, HCA 28.

107 *Allups Holdings Pte Ltd. v. Phoon Wui Nyen*, High Court of Singapore, 2016, SGHC 144.

108 *Arab Bank Australia Ltd. v. Sayed Developments Pty Ltd.*, New South Wales Court of Appeal, 2016, NSWCA 328.

109 *Hobson Street Ltd. v. Honey Bees Preschool Ltd.*, Supreme Court of New Zealand, 2019, NZCA 122.

110 *Cubic Electronics Sdn. Bhd. v. Mars Telecommunications Sdn. Bhd.,* Apex Court of Malaysia, 2019, 2 CLJ 723.

111 Aditya Shiralkar, 'The Legitimate Interest Test (UK) on The Enforceability of Liquidated Damages Clauses And its Implications for Indian Law', *Supreme Court Cases* p. 37, volume: 2, 2021.

112 *Shalaka Patil & Vishesh Bhatia, 'Beyond the Old Rule: Should Cavendish Come to India?', Kluwer Arbitration Blog, 4 August 2022, available at* https://arbitrationblog.kluwerarbitration.com/2022/08/04/beyond-the-old-rule-should-cavendish-come-to-india/*, accessed on 30 July 2025*.

Indian High Courts are bound by the judgements by the Supreme Court of India, which has circumscribed the Indian jurisprudence to the compensatory-penal dichotomy.

However, there remains a potential for India to adopt the legitimate interest test. For instance, the Indian Supreme Court has accepted that the 'character of the transaction' and its 'special nature' must be considered while determining whether an LD clause is a penalty or not.[113] Therefore, the legitimate interest test can potentially be read into such jurisprudence by the Indian judiciary.

2. Lesson for Nepal

Judgements in Nepal have developed a strict (but erroneous) jurisprudence against penalties and have adopted a 'actual damages-penalty' dichotomy. Given the strict jurisprudence against penalties in Nepal, an LD clause which fulfils the legitimate interest test might not be enforceable. Therefore, there is a need to rethink the existing jurisprudence and adopt the legitimate interest test in the Nepalese context as well, as it is not the goal of the Nepalese law on contracts to restrict LD clauses that seek to protect a legitimate interest.[114]

B. **Uncertain LD Clauses**

LDs are not enforceable if they are uncertain. Claims of uncertainty (with regard to LDs) can arise, for instance, in cases where there are multiple completion dates; where there are multiple conflicting provisions governing LDs;[115] where the time is at large, etc.[116] Further, in the case of *Arnhold & Co Limited v. The Attorney of Hong Kong,* it was decided that if an LD clause provides for minimum and maximum LD applicable (range of applicable LD) but fails to provide a procedure to identify the applicable LD within the range, the LD clause is void for uncertainty.[117]

However, courts rarely hold LD clauses to be uncertain, because even in cases of uncertainty, if a court can find an interpretation that can give effect to the parties' intention, they are required to enforce the LD clauses based on such interpretation.[118] Nevertheless, issues of uncertainty, if not adjudicated carefully, can enable penalties which can be observed under the current 'all or nothing' approach in Nepal.

Nepalese parties to a contract should be aware of the clauses included in the contract. Any conflict within contractual clauses regarding LD can render an LD clause unenforceable. While the standard form of contracts drafted by the PPMO do not contain such conflicting clauses, nor do they contain an LD clause that provides for a range of applicable rates of LD, such clauses can be observed in private contracts. With regard to Nepalese public procurement contracts, a particular problem that can be observed concerns a situation where the employer themselves

113 citation 49 and the accompanying text therein.

114 Section VI of the article.

115 *Bramall & Ogden v. Sheffield City Council*, England and Wales High Court (Technology and Construction Court), 1983 29 BLR 73; *Taylor Woodrow Holdings Limited v. Barnes & Elliott Limited,* England and Wales High Court (Technology and Construction Court), 2004, EWHC 3319 TCC.

116 *Taylor Woodrow (n 115); Buckingham Group* (n 12); Julian Bailey (n 1) pp. 1205-1206; Andrew Burr (n 69) pp. 268-289; David Chappell (n 15) pp. 84-87.

117 *Arnhold & Co Limited v. The Attorney of Hong Kong*, High Court of Hong Kong, 1989, 47 BLR 129.

118 *Taylor Woodrow (n 115*); *Eco World (n 8)*; *Buckingham Group* (n 12).

are at breach or, where the employer denies or fails to provide an extension of time as per the contract, rendering the time at large[119] (a type of uncertainty). Such problems can also be observed under private contracts. This would prevent the employer from seeking LD for the period when the time is at large.[120] It can simply be understood from the prevention principle that a party in breach cannot seek to recover damages from the other party.[121] While the current 'all or nothing' approach can address any dispute regarding causation of delay and the time being at large thereof, it fails to address, particularly under private contracts, the issues of uncertainty that arise due to reasons other than the time being at large due to employers' causation. Such shortcomings enable the enforcement of uncertain LD clauses (which can also qualify as a penalty).

C. Time as the Essence (India-Specific Issue)

Precedents concerning the interrelationship between LDs and time being the essence of the contract are largely observed in India. Courts in India have held that if a contract includes a clause for LD or for extension of time, then time cannot be said to be the essence of such contracts.[122] However, such jurisprudence has been subject to criticisms and it has instead been argued that inclusion of an LD clause instead establishes that time is of the essence.[123] The test to determine whether the time is of the essence ought to be of substance rather than of form. Nevertheless, the largely accepted (although erroneous) jurisprudence in India is that the inclusion of clauses like extension of time and LD, establishes that time is not the essence of the contract.[124] Considering such jurisprudence, the decision made by the Supreme Court of India in *Welspun Specialty Solutions v. Oil and Natural Gas Corporation Ltd.*[125] is concerning as the court ruled that since time was not the essence of the contract (due to the existence of LD clause against delay, and extension of time provision), LD cannot be levied against any delay by the contractor, as a delay cannot amount to a breach of such contract (where time is not the essence).[126] Therefore, it was decided that where time is not the essence, LD (against delay) cannot be levied.

The combined effect of such jurisprudence is that the inclusion of an LD clause establishes that time is not the essence of the contract, and since time is not the essence of the contract, LD cannot be levied, thus creating an inescapable cycle, rendering the LD clause obsolete.[127] It should therefore be noted that time as the essence of a contract is irrelevant to issues concerning LDs.[128]

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119 Julian Bailey (n 1), pp. 1205-1206

120 Ibid; *Hawlmac Construction v. Campbell River Co.*, Supreme Court of British Columbia, 1985, 60 BCLL 57; See *Rapid Housing v. Ealing Family Housing, Court of Appeal,* 1984, 29 BLR 5, where it was decided that since the time was at large, the employer cannot recover liquidated damages but can recover unliquidated damages if the work is not completed within a reasonable time.

121 Julian Bailey (n 1), pp. 1197-1202.

122 See *Hind Construction v. State of Maharashtra*, Supreme Court of India, 1979, AIR 720; Badrinath Srinivasan, 'The Law on Time as Essence in Construction Contracts: A Critique', *RGNUL Financial and Mercantile Law Review* p. 1, volume 8:1, 2021, p. 12-15.

123 *S. Daya Singh v. Som Datt Builders Pvt. Ltd.*, Delhi High Court, 2019, OMP 327/2010; Badrinath Srinivasan (n 122), p. 20.

124 See Badrinath Srinivasan (n 122).

125 *Welspun Speciality Solutions v. Oil and Natural Gas Corporation Ltd.*, (2022) 2 SCC 382.

126 See, David Chappell (n 15) pp. 75-77.

127 Badrinath Srinivasan, 'Case Note: Time as Essence and Liquidated Damages Clauses: A Critique of Welspun Specialty v. ONGC', *Australian Journal of Asian Law* p.119, volume 24:2, 2023, p.121.

128 Ibid, p. 121-122.

Such Indian judgements have recently been cited by parties to arbitration in Nepal. While such issues concerning the interrelationship between LD clauses and time as the essence have not reached Nepalese courts yet (therefore creating a lack of Nepalese jurisprudence on the matter), it can be concerning if arbitration tribunals and courts of Nepal remain unaware of the criticisms that Indian jurisprudence has had in this regard. Any adoption of such Indian jurisprudence can defeat the purpose of LD clauses.

D. Waiver of LD (India-Specific Issue)

In the case of *Welspun,* it was further decided that since ONGC did not charge any LD while providing the first two extensions of time, ONGC had waived its right to charge LD for any subsequent extensions.[129] The judgement was provided despite a clear provision of a non-waiver clause which provided that waiver, if any, should be clear, in writing, and with the approval of the competent authority. The judgement has been criticized—merely because a party chose not to invoke an LD clause for the first few delays or extensions, cannot mean that LD cannot be invoked for later delays or extensions.[130]

Nepalese contractors have sought to use *Welspun* and the jurisprudence concerning waiver thereunder to prevent employers from charging LD against subsequent extensions of time. On the other hand, employers have also sought to misuse non-waiver clauses. Therefore, a discussion concerning waiver and non-waiver is of importance to Nepal.

The standard form of contracts drafted by the PPMO include non-waiver clauses like that in *Welspun*. Such non-waiver clauses are the base on which employers under government contracts have sought to levy LD (against delay) retrospectively despite providing an unconditional extension of time (i.e. without any charge of LD). However, non-waiver clauses cannot be of recourse to employers who have clearly waived their rights. The doctrine of affirmation by election can help defeat such misuse of the non-waiver clause.[131] The doctrine provides that when a party has a choice between two inconsistent rights and the party chooses one of the rights, the other right gets waived. Therefore, if any party fails to apply LDs against delay and provides an extension of time, the right to apply for LD for that specific delay should be considered to have been waived. Therefore, any attempt to retrospectively apply LDs is not possible once they have been waived, as such an attempt violates the jurisprudence developed with regard to waiver.[132] However, LD can still be levied for subsequent future delays, unlike as decided in *Welspun*.

E. Breaking Down of the Contract Machinery

It is well accepted that LDs (against delay) cannot be levied after a contract has been terminated since a termination absolutely stops the concerned party from performing the contract.[133]

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129 See *Welspun* (n 125).

130 See Badrinath Srinivasan (n 127).

131 *Tele2 International Card Co. SA and Ors v. Post Office Ltd.*, England and Wales High Court, Queen's Bench, 2008, EWHC 158 (QB); See *Badri Kumar Basnet v. His Majesty's Government*, NKP 2051 (1994), volume 10, Decision no. 4985, p. 19.

132 *Pushpa Kamal Dahal (Prachanda) v. The Constitutional Council and* others, NKP 2067 (2010), volume 7, Decision No. 8406, p. 14; Nepalese Courts have also restricted the retrospective application of LDs. See *Dhurba Raj Thapa v. Appellate Court, Butwal,* NKP 2071 (2014), volume 6, Decision no. 9176; David Chappell (n 15), pp. 87-88

133 See *Triple Point (n 1); See British Glanzstoff Manufacturing Co. Ltd. v. General Accident, Fire and Life Assurance Corpn. Ltd.*, Scottish Court of Session, 1913, AC 143, where it was decided that LD clauses did not apply where the control of the contract had passed out of the hands of the party that is subjected to LD.

Similarly, if the contract machinery has broken down, due to the actions by one party, rendering the contract incapable of being performed by the other party, LDs (against delay) cannot be levied from the time when the contract machinery has broken down.

In Nepal particularly, employers in government contracts create difficulties for contractors to execute the contract. Employers should be aware that if such difficulties lead to a breakdown of the contract machinery, LD (against delay) cannot be applicable for the time period when the contract machinery has broken down. Such an issue can, however, potentially be addressed under the current 'all or nothing' approach where the causation of a breach is adjudicated upon.

F. Lack of Granularity

A single pre-determined LD amount (or rate) applicable against various kinds of breach shows a lack of granularity.[134] A lack of granularity can render an LD clause unenforceable.[135] If the fixed LD covers breaches of varying degrees of importance, the possible damage from which bear no relation to the LD fixed and which has never been estimated by the parties to the contract, such LD clauses are said to be a penalty.[136] If an LD clause provides for a single sum (or rate) as damages despite covering breaches which are of varying gravity, an application of such LD clause against a minor breach, can lead to a conclusion that such application is a penalty.[137]

The standard form of contracts drafted by the PPMO include pre-determined fixed LD clauses (against all delays), which are used as it is by the employers, without having regard to the nature of the project. While the specifications, drawings, bills of quantities, etc. are changed according to the requirements of the projects, the conditions of contract largely remain unchanged. LD clauses under such standard forms of government contracts are fixed. Therefore, despite the scale and the nature of the projects, LD clauses (against delay) in the standard form of government contracts remain unchanged. It is in this regard that the risk of lack of granularity ensues. Such risk, however, is not just limited to government contracts and can also extend to private contracts.

LD cannot be levied against delays concerning minor works in a manner that is applicable against delays concerning major works. Therefore, employers (whether under government or private contracts) must have regard to the scale and the nature of the project, and include LD clauses accordingly, as a lack of granularity can enable penalties. To avoid such risk of penalties in government contracts, employers should not be restricted by the LD clauses included in the PPMO's standard form of government contracts and should be allowed to have discretion in determining a project-appropriate LD clause.

[Note: While lack of granularity is a valid defense, it cannot be used in a manner that defeats the 'no requirement of precise calculation' objective of LD clauses, as discussed in Section – II of the article.]

G. Partial Possession

The partial possession of works by a party after partial completion and handover by another party

134 Larry A. DiMatteo (n 32), p. 1853; See *Ford Motor Co v. Armstrong*, Court of Appeal, 1915, 31 TLR 267.

135 *Lordsvale Finance* (n 75); See David Chappell (n 15) p. 63.

136 See *KP Subbarama Sastri* (n 47); *Micheal Habib Raji Ayoub and Ors. v. Sheikh Suleiman El Taji El Farouqui*, Privy Council, 1941, AIR PC 101.

137 See *Lake River Corp. v. Carborundum Co.,* US Court of Appeals for the Seventh Circuit, 1985, 769 F.2d 1284; See *Dunlop* (n 39).

can also impact the LD sought. For example, if a party completes 50 percent of the work and successfully hands it over to the other party, the damage arising from the remaining 50 percent of the work would be much less than the damage arising from a situation where 100 percent of the work is yet to be completed. Therefore, it can be argued that in such a situation, if a fixed LD is levied without having regard to partial possession, the LD levied can result in a penalty.

Some UK judgements have dealt with the issue of partial possession. The case of *Buckingham Group Contracting Ltd. v. Peel L&P Investments and Property Ltd* concerned the issue of application of LDs after partial possession. However, it was decided that since the contract only provided milestones for project completion and did not include any provision for transfer of partial possession, no issue of partial possession could arise.[138] In the case of *Bramall & Ogden v. Sheffield City Council,* it was decided that despite a provision for the application of LD for each incomplete dwelling, the contract failed to include a provision for partial possession of the completed dwellings, thus making the LD clause uncertain.[139] In the case of *Taylor Woodrow Holdings Ltd. v. Barnes & Elliott Ltd.,* it was decided that even though the contract provided for sectional completion and pro-rata adjustment of LD based on partial possession taken by the other party, the LD clause was inoperable due to uncertainty since the scope of work falling within each section of the work was not properly defined.[140] While these judgments highlight the importance of a clear provision of partial possession and a clear scope of work to avoid uncertainty, they however did not decide as to whether a lump-sum LD clause would establish the LD clause as a penalty, in cases of partial possession.

In *Eco World – Ballymore Embassy Gardens Co. Ltd. (EWB) v. Dobler UK Ltd.*, the parties had contracted to build three residential buildings.[141] The date of completion of the project was on 30 April 2018. EWB took partial possession of two buildings on 15 June 2018. It was therefore contended by Dobler that such partial possession impacted the LD recoverable by EWB. It was, however, decided that the contract did not contain any mechanism for reduction of LD and that there was no provision in the contract that required LD to be applicable by having regard to the nature, scope, and extent of any relevant part taken over. Therefore, it was decided that reduction of applicable LD could not be contended based on partial possession. The court decided that a single lump sum could be included as LD despite a provision of sectional completion. The judgement in *Eco World* highlights the courts' intention to enforce mutually negotiated LD clauses as they are. However, in the case of *Stanor Electric Ltd. v. R Mansell Ltd.,*[142] as a party had completed electrical installations in one of the two houses, and thus a fixed LD was sought against the party. It was decided that there was a presumption of penalty since 'a single sum was made payable by way of compensation on the occurrence of one or more or all of several events, some of which might occasion serious and others but trifling damages.' It was decided that such clauses were 'self-evidently a penalty.' The Court also refused to uphold the employer's attempt to levy a part of the LD since there was no contractual mechanism that allowed the employer to unilaterally reduce the amount of LD. Where the intent of reduction in LD based on partial completion of work is sufficiently clear from the LD clause itself, courts should give effect to such intent of the parties. For instance, in *MJ Gleeson v. Hillingdon Borough Council,* where the LD

138 *Buckingham Group* (n 12).

139 See *Bramall* (n 115); See *Avoncroft Construction Ltd. v. Sharba Homes (CN) Ltd.,* England and Wales High Court (Technology and Construction Court), 2008, EWHC 933 (TCC).

140 *Taylor Woodrow (n 115).*

141 *Eco World* (n 8).

142 *Stanor Electric Ltd v. R Mansell Ltd.*, 1988, CILL 399; David Chappell (n 15), pp. 47-51; See *Ariston SRL v. Charly Records Ltd.,* England and Wales Court of Appeal, 1990, EWCA Civ J0313-1.

clause provided that a fixed LD would be applicable for each incomplete dwelling against each week of delay, it was decided that LDs cannot be levied for dwellings whose possession were taken by the employer.[143]

The standard form of contracts drafted by the PPMO do not include LD clauses (against delay) that are subject to change based on partial possession. Similar LD clauses are largely repeated in private contracts as well. However, LD can be subject to change based on subsequent events.[144] One such subsequent event that can impact the recoverable LD, is partial possession by the employer. In such situations, if fixed LD is sought, without having regard to partial possession, it can potentially lead to a situation where the LD clause can be termed as a 'self-evident penalty' as observed in *Stanor*. While the judgement in *Eco-World* was reluctant to term the application of a lump-sum LD clause (even in case of partial possession) as a penalty, such fixed LD clause and its application are not entirely risk-free, as seen in *Stanor*.[145] Additionally, in cases where partial possession is taken (based on a provision of partial possession within the contract), a requirement of harmonious interpretation (while interpreting a contract), can potentially invite a risk where a fixed LD clause can be a penalty.[146]

[While partial possession is a valid defense, it cannot be used in a manner that defeats the 'no requirement of precise calculation' objective of LD clauses, as discussed in Section – II of the article.]

VI. Unrealized Potential for Rectification/Conclusion

As discussed above, there are substantial and concerning errors in the jurisprudence and practice concerning LDs in Nepal, and its application in the public procurement regime. However, there exists unrealized jurisprudential potential for rectification of such errors and shortcomings. Potential solutions can be found within the existing Nepalese jurisprudence itself. Foreign jurisprudence as discussed in Section V can also be introduced within the existing Nepalese jurisprudence.

As per Sec. 537 of the National Civil Code, 2017 (2074 B.S.), a 'reasonable amount' can be provided as damages if a contract has provided for pre-determined damages. Therefore, since the legislative intent of providing 'reasonable compensation' is clear from a plain reading of the provision, the 'actual damages-penalty' dichotomy established in *Amar Adardha* and *Bekha Maharjan,* and the 'all or nothing' standard practice with regard to LD can easily be abolished as they violate a clear legislative intent.[147] Further, after such abolition, the 'compensatory-penal dichotomy' along with the 'legitimate interest test' can also be read into Sec. 537 due to the use of the term 'reasonable compensation' within the provision. Further, the jurisprudence concerning 'granularity' and 'partial possession' can also be read into such use of the term 'reasonable compensation' within the provision. Additionally, the unnecessary judicial interference enabled by the judgement in *Amar Adharsha* (which provided judges with large discretionary power to determine the damages payable despite the presence of an LD clause) can also be resolved by providing due regard to the existing jurisprudence on recognition of party autonomy and circumscribed court jurisdiction (which cannot exceed beyond contractual

143 *MJ Gleeson v. Hillingdon London Borough*, 1970, 215 EG 165.

144 *Philips Hong Kong* (n 8).

145 The Court noted that the parties were aware of the contractual clauses and that the contract was negotiated by sophisticated parties, and therefore, could not be considered as a penalty.

146 *Muluki Dewani Sanghita* 2074 (n 4), s. 515(4)(5); See *Himalayan Bank* (n 76).

147 See *Lok Bhakta Shumsher Ja.Ba.Ra.* (n 78); *Raju Lama* (n 78).

clauses).[148]

The issue concerning 'unilateral determination' can be resolved by providing due regard to Article 20 (9) of the Constitution, which provides for a fundamental right to a fair trial before an independent judicial authority.[149] The issue concerning 'uncertainty' can be resolved *vide* the jurisprudence concerning enforcement of intent of the contracting parties and circumscribed court jurisdiction (which cannot exceed beyond contractual clauses).[150] Where any LD clause is unworkable due to uncertainty (i.e. where the intent of the parties is not clear), courts and arbitration tribunals cannot give effect to such clauses in a manner that creates a new contractual provision (by defeating contractual party autonomy), and would be bound to render them 'uncertain'.

The issues caused by the application of LD clause at a fixed rate of 0.05 per cent of the contract amount against per day of delay under government contracts can be resolved by complying with Rule 121 (a) of the Public Procurement Rules, 2007 (2064 B.S.), which provides that LD against delay should normally (and not mandatorily) be applied at 0.05 per cent of the contract amount against per day of delay. Therefore, the fixed rate of LD under standard form of government contracts drafted by the PPMO must be rethought upon.

Further, even if the standard form of public procurement contracts is redrafted to provide employers with flexibility in levying LD, the practice of levying fixed maximum LD amount/rate might continue. This is because, another reason why public officials under government contracts levy LD at such a fixed rate is because of a threat of allegation of abuse of authority by the Commission for Investigation of Abuse of Authority (CIAA) against such officials if they allow flexibility while levying LD against delays. To solve such issues, regard must be had to the case of *Dilli Ramand Acharya v. Sugat Ratna Kangsakar*[151] where it was decided by the Supreme Court that issues of corruption cannot arise in contractual matters. Therefore, the CIAA should not be allowed to interfere in commercial decisions (like levying of LD) made by employers under government contracts in compliance with the law. What can be observed is that there exists potential for the Nepalese judiciary and arbitration tribunals to rectify the existing errors in the Nepalese jurisprudence and practice concerning LDs by making use of the existing Nepalese jurisprudence and laws themselves. Foreign jurisprudence discussed under Section V above can also be read into the existing Nepalese jurisprudence. Therefore, noting the importance of LD clauses in a commercial context, there is a need to immediately rethink the existing erroneous jurisprudence and practice on LDs in Nepal, and adopt appropriate jurisprudence according to the circumstances of the case.

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148 *Muluki Dewani Sanghita* 2074 (n 4), s. 507; See *Pawan Raj Bhandari* (n 73); See *Krishi Samagri Sangsthan* (n 74); See *Umakant Jha* (n 74).

149 *Nepal ko Sambidhan* (n 37), art. 20(9).

150 See *Himalayan Bank* (n 76); See *Krishi Samagri Sangsthan* (n 74); See *Umakant Jha* (n 74); See generally *BESCOM* (n 76), where it was decided that it is not the duty of courts to enter into the intricacies of the human mind to determine the intent of the contracting parties.

151 *Dilli Ramand Acharya v. Sugat Ratna Kangsakar,* NKP 2069 (2012), volume 7, Decision no. 8859, p. 27.