IN THE HIGH COURT OF KARNATAKA, BENGALURU

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DATED THIS THE 19TH DAY OF SEPTEMBER, 2023

BEFORE

THE HON'BLE MR JUSTICE KRISHNA S DIXIT

WRIT PETITION NO.1517 OF 2012 (GM-RES)

BETWEEN:

1. KARNATAKA EMTA COAL MINES LTD.,
   AN EXISTING COMPANY UNDER THE PROVISIONS
   OF COMPANIES ACT, 1956
   HAVING ITS REGISTERED OFFICE AT
   FLAT NO.104, MARIELLE APARTMENTS,
   #3, MAGRATH ROAD, BANGALORE – 560 025.
   REPRESENTED BY ITS MANAGING DIRECTOR.

2. EMTA COAL LIMITED (INCORPORATED IN
   CONVERSION OF EASTERN MINERALS AND
   TRADING AGENCY, A REGISTERED
   PARTNERSHIP FIRM UNDER
   PART IX OF THE COMPANIES ACT, 1956)
   HAVING ITS REGISTERED OFFICE AT 5B,
   NANDALAL BASU SARANI, (LITTLE RUSSEL STREET),
   KOLKATA – 700 071.
   REPRESENTED BY ITS CHAIRMAN AND
   MANAGING DIRECTOR.

…PETITIONERS

(BY SRI.ADITYA SONDHI., SENIOR COUNSEL A/W
MS. SHRISTI WIDGE, ADVOCATE
MR. MANU KULKARNI, ADVOCATE AND
MR. SHARAN BALAKRISHNA., ADVOCATE)

AND:

1. KARNATAKA POWER CORPORATION LIMITED
   A GOVERNMENT COMPANY UNDER THE PROVISIONS
   OF COMPANIES ACT, 1956
   HAVING ITS REGISTERED OFFICE AT

SHAKTHI BHAVAN, #82, RACE COURSE ROAD,
BANGALORE – 560 001.
REPRESENTED BY ITS MANAGING DIRECTOR.

2. STATE OF KARNATAKA,
REPRESENTED BY PRINICPAL
SECRETARY TO GOVERNMENT,
DEPARTMENT OF ENERGY,
VIKAS SOUDHA, AMBEDKAR VEEDHI,
BANGALORE – 560 001.

…RESPONDENTS

(BY SRI.V SRINIVASA RAGHAVAN, SENIOR COUNSEL A/W
SRI. ABHINAY V., ADVOCATE AND
MS. DEEPSHIKA PRABHU., ADVOCATE FOR R1;
SMT.SHWETA KRISHNAPPA., AGA FOR R2)

THIS WRIT PETITION IS FILED UNDER ARTICLES 226 AND 227 OF THE CONSTITUTION OF INDIA, PRAYING TO SET ASIDE THE IMPUGNED DEMAND DATED 12.12.2011 VIDE ANNEXURE-A ISSUED BY KPCL SEEKING TO RECOVER AN AMOUNT OF RS.52.63 CRORES FROM THE WRIT PETITIONER NO.1 COMPANY.

THIS PETITION HAVING BEEN HEARD AND RESERVED FOR ORDER, THIS DAY, THE COURT PRONOUNCED THE FOLLOWING:

ORDER

Petitioners being the companies incorporated under the provisions of erstwhile Companies Act, 1956, are complaining before the Writ Court against the letter dated 12.12.2011 issued by the first respondent-KPCL demanding from them a sum of Rs.52,63,00,000/-, by way of 'penalties'.

2. The relevant part of the impugned letter reads as under:

> *"…Please refer to our letters cited above, with regard to the recovery of penalties on the following issues:*
>
> *a. 'Non-commencement of supply of coal to BTPS' - amounting to 33 crores as per clause 10.2 of the Article 10 of Fuel Supply Agreement executed on 09.05.2007. As discussed in the 38th Board Meeting held on 19.11.2010 of KECML, the issue of recovery of penalty amounting to 33 crores, was referred to the Advocate General, Karnataka, who has opined for imposition of the penalty as per the terms and conditions of the Fuel Supply Agreement, which was informed vide our letter cited at ref (1) above.*
>
> *b. 'Recovery of difference in cost for arranging supply of coal from alternate sources'- amounting to 16.44 crores as per clause 10.5 of the Article 10 of Fuel Supply Agreement executed on 09.05.2007. As informed vide our letter cited at ref (2) above, the Technical Committee of KPCL had recommended for recovery of the penalty amounting to 16.91 crores as per clause 10.5 of the FSA. Further, the Advocate General, Karnataka, has also opined for recovery of difference in cost in respect of the entire supply of coal arranged by KPCL from alternate source.*
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> *c. 'Short supply after commencement of supply of coal to BTPS from the captive coal mines'*

> *- amounting to 5.72 crores as per clause 10.4 of the Article 10 of Fuel Supply Agreement executed on 09.05.2007. Out of the total recovery of 5.72 crores, an amount of 3.00 crores has already been recovered. The AG Auditors have objected for the non-recovery of the amount as per the clause 10.4 of the FSA.*
>
> *In this regard, KECML is requested to remit an amount of 52.63 crores immediately, in respect of the above issues, or else, KPCL will be left with no other alternative but to recover the amount from the payments released to KECML, since our Auditors are objecting for the non-recovery of penalty as per the clauses of the Fuel Supply Agreement executed on 09.05.2007..."*

3. After service of notice, the first respondent (hereafter 'KPCL') has entered appearance through its Panel Counsel; the second respondent-Government is represented by the learned AGA. The KPCL has filed its Statement of Objections on 20.07.2013 resisting the petition. Learned Sr. Advocate appearing for the KPCL made submission in justification of the impugned demand and the reasons on which it has been structured. This court hastens to mention that its suggestion to explore the possibility of arbitration, absence of such a clause in

the subject Agreement notwithstanding, was acceded to by the petitioners; however, the KPCL being a State *Government Company*, its learned Sr. Advocate expressed the constraints of his client in that regard.

4. CASE OF THE PETITIONERS:

(a) Second Petitioner-Company and the KPCL entered into a Joint Venture Agreement on 13.09.2002 for establishing a Joint Venture Company to undertake development & mining activity. Accordingly, the first petitioner came to be incorporated as a Joint Venture Company for the purpose of development & operation of the Captive Coal Mines allocated to KPCL by the Central Government. The coal extracted from these mines was exclusively meant for the thermal power stations of KPCL. The second petitioner & its nominees on the one part hold 74% of the equity shares of first petitioner-company, and the KPCL on the other holds the remaining 26% of equity shares. It was the responsibility of second respondent to discharge the contractual obligations.

(b) The Coal Ministry of Central Government vide letter dated 10.11.2003 allocated certain Captive Coal Blocks in Chandpur district of Maharashtra to the KPCL for power generation in the thermal power stations at BTPS. A Notification to this effect came to be issued on 16.07.2004. The Central Government taking note of Official Site Clearance, granted prior approval on 31.01.2006 u/s 5(1) of the Mines and Minerals (Development and Regulation) Act, 1957. After formal compliances, a Mining Lease was executed between the first petitioner and the Government of Maharashtra on 25.09.2006. Keeping in view the Joint Venture Agreement, the first petitioner and KPCL entered into a Fuel Supply Agreement (FSA) on 9.5.2007 for recording the terms & conditions for supply of coal to BTPS for a period of 25 years. It also provided for furnishing financial securities to the said petitioner.

(c) The allocation of subject Coal Blocks in favour of first petitioner, and Central Government's Notification

dated 16.7.2004 referred to above were put in challenge in W.P.Nos.10788/2006, 12867/2006 & 17828/2006; the challengers had obtained interim orders of stay. These cases to which KPCL was also impleaded as a respondent were before this court and the Nagpur Bench of Bombay High Court. Particulars of these cases and of SLP (C) No.1310/2007 arising from one of them, are furnished in a tabular form by the petitioners. The subject SLP was dismissed on 5.4.2007. W.P.No.17828/2006 came to be dismissed by this court on 2.7.2008.

(d) After all the litigations came to an end, the first rake of coal was dispatched from the Captive Coal Blocks by the first petitioner-company to BTPS on 29.9.2008. Governmental processes and the litigations caused delay in the commencement of mining activities and dispatch of coal. The factors that caused such delay were beyond the control of petitioners and therefore, the impugned demand could not have been raised. Even otherwise, this delay was condoned by the KPCL and

therefore it could not have turned around and raised the demand on an assumed contra substratum. Learned Sr. Advocate appearing for the petitioners also argued that subject clauses of Fuel Supply Agreement do not authorize the KPCL to quantify damages and levy penalty *sans* judicial determination.

In support of above submissions, learned Sr. Advocate pressed into service certain Rulings.

5. THE CASE OF KPCL IN BRIEF:

(a) Several statutory processes as averred in the petitions and the Agreements in question are not in dispute. First petitioner committed breach of terms of these Agreements, which authorize determination of damages for the same; therefore the compensation having been normatively quantified, the impugned demand cannot be faltered. The purpose of incorporating the subject terms in the Agreement, is to authorize KPCL to assess the damage/loss and determine the compensation/penalty payable by the petitioners on

account of their breach; an argument to the contrary would defeat such a purpose; the Agreement having been entered into with eyes wide open, petitioners are not justified in placing their own interpretation on the subject clauses thereof to their advantage and to the detriment of KPCL.

(b) It is not that what the KPCL has done is final, since petitioners can dispute the same in an appropriate suit proceeding; the case involves disputed questions of facts and therefore, Writ Petition is not the right redressal. Learned Sr. Advocate highlighted the breach of Agreement and sought to justify the impugned recovery of damages/penalty *inter alia* banking upon audit objections. He contended that the word 'penalty' employed in the subject Agreement should not be literally construed when it only meant liquidated damages.

(c) The case in W.P.No.2923/2003 was filed before the Nagpur Bench on 18.7.2003 *inter alia* on the

ground that allocation of coal mines could not be done in favour of non-Maharashtrians. The KPCL came to be impleaded vide order dated 21.2.2006, when the allocation was already done on 10.11.2003; there was no interim order in this case. The case in W.P.No.10788/2006 was filed before this court on 3.8.2006 challenging the Central Government Notification dated 16.7.2004 which had specified KPCL to be the end user of coal. On 4.8.2006, stay was granted for a period of four weeks 'if the impugned notification was not given effect to'; the said Notification was already given effect and therefore, there was no stay; this case came to be dismissed as withdrawn on 22.11.2006. The case in W.P.No.2923/2003 was filed before the Nagpur Bench challenging the allocation of coal mines to the KPCL; however, it too was dismissed on 10.8.2006; the challenge to dismissal in SLP No.1310/2007 also met the same fate on 5.4.2007. In the meanwhile, W.P.No.12867/2006 came to be filed before this court on 13.9.2006 challenging the Central Government

Notification. There was no stay order in this case; that also came to be dismissed as withdrawn on 17.1.2007.

(d) The subject Fuel Supply Agreement came to be entered on 9.5.2007 and the present dispute concerns the same. Therefore, what all happened before, pales into irrelevance. Even otherwise, petitioners have not set out the full particulars to substantiate their allegation of delay attributable to the authorities whilst granting approvals and permissions post Agreement. Therefore petitioners' ground of attack on the impugned demand is unacceptable. The submission of petitioners that the subject clauses of the Fuel Supply Agreement cannot be invoked and that no amount is recoverable thereunder, is only a futile attempt to escape the liability. As per clause 2.1 of the Agreement, petitioners were obliged to deliver entire quantity of coal to be extracted from the designated coal mines inasmuch as they knew that BTPS was to be commissioned by July 2007 itself, its

requirement being approximately two million tonnes of coal.

(e) The relevant clause in the subject Agreement required issuance of a prior notice to the KPCL within two weeks of petitioners becoming aware of any force majeure. Despite repeated reminders, they failed to supply coal either from the designated mines or by otherwise outsourcing it. The breach of Agreement being apparently demonstrable, the impugned demand has been raised strictly in accordance with its terms. So contending, learned Sr. Advocate appearing for the KPCL prayed for the dismissal of Writ Petition. He too banked upon certain Rulings in support of his submission.

6. Having heard the learned counsel for the parties, having perused the Petition Papers and having adverted to relevance of the Rulings cited at the Bar, this court has framed the following questions for determination.

(i)	*Whether contractual disputes of the kind can be a subject matter of examination in writ jurisdiction… ?*
(ii)	*Whether Resp-KPCL is justified in seeking relegation of petitioners to the remedy of ordinary civil suit on the ground of disputed fact matrix… ?*
(iii)	*Whether principles of natural justice are invocable in the realm of private contract so that their violation, renders the impugned recovery bad… ?*
(iv)	*Whether the penalty mentioned in clause 10 of FSA is in the nature of liquidated damages and therefore the impugned demand is permissible…?*
(v)	*Whether the CAG Report & Advocate General's opinion prepared without petitioners participation, can be the basis for raising the impugned demand…?*
(vi)	*Whether on the fact matrix emerging from the record, the impugned demand in a wholesale way is sustainable…?*

Following is the discussion on these questions:

I. AS TO NON-INVOCABILITY OF WRIT JURISDICTION IN CONTRACTUAL MATTERS:

(a) There is no much dispute that the KPCL is a 'Government Company' of the State as defined u/s 617 of the erstwhile Companies Act, 1956 and now section 2(45) of the Companies Act, 2013. It is funded, financed & managed by the Government of Karnataka cannot be disputed; therefore, it answers the description of 'State'

u/a 12 of the Constitution of India in the light of Apex Court decision in *R.D.SHETTY vs. INTERNATIONAL AIRPORT AUTHORITY OF INDIA,* AIR 1979 SC 1628. That being the position, all its actions/inactions, whether contractual or otherwise, are liable to suffer judicial review under Articles 226 & 227 of the Constitution of India, although the extent of such *review* may not be that deep and that wide, unlike in cases involving violation of Fundamental Rights. Merely because matter is essentially contractual in nature, Writ Courts cannot readily decline indulgence and invariably relegate the parties to the civil remedies, despite there being public law elements in the action impugned. This view gains support from the Division Bench decision between the very same parties i.e., *EMTA COAL LIMITED vs. KARNATAKA POWER CORPORATION LIMITED*, ILR 2016 KAR 2025; this decision on being challenged by respondent-KPCL has been affirmed by the Apex Court vide 2022 SCC OnLine SC 664.

(b) The Apex Court in *UNITECH LIMITED vs. TELANGANA STATE INDUSTRIAL INFRASTRUCTURE CORPORATION* (2021) SCC OnLine SC 99 at paragraphs 38 & 40 observed:

> *'…It is necessary to postulate that recourse to the jurisdiction under Article 226 of the Constitution is not excluded altogether in a contractual matter. A public law remedy is available for enforcing legal rights subject to well settled parameters… Article 23.1 of the Development Agreement in the present case mandates the parties to resolve their disputes through an arbitration. However, the presence of an arbitration clause within a contract between a State instrumentality and a private party has not acted as an absolute bar to availing remedies under Article 226. If the State instrumentality violates its constitutional mandate under Article 14 to act fairly and reasonably, relief under the plenary powers of the Article 226 of the Constitution would lie…'*

The above observations come to the aid of petitioners since they have impugned the demand in question *inter alia* on the grounds of arbitrariness, unfairness & unreasonableness. In fact, as between the parties, there was a case before the Division Bench of this Court i.e., *EMTA COAL supra,* which too supports similar view.

This decision on being challenged by KPCL is affirmed by Apex Court in (2022) SCC OnLine SC 664.

II. AS TO AVAILABILITY OF ALTERNATE REMEDY AND RELEGATION OF PETITIONERS THERETO:

(a) It is an admitted position that the impugned demand has arisen under paragraphs of Article 10 of Fuel Supply Agreement. This Agreement is a product of *inter alia* certain statutory processes i.e., The Coal Mines Regulations, 1957, The Mines and Minerals (Development and Regulation) Act, 1957, etc. The establishment of the thermal project is also animated by statutory process, involving both the State Government & Central Government, although in varying extents. The fructification of the project in question is generation & supply of power which is regulated by both Parliamentary and State Legislations. The first respondent itself, as already mentioned is a State Public Sector Undertaking, and not a private entity. Viewed thus, it cannot be justifiably disputed that the FSA involves abundant public law elements and therefore, dispute of the kind arising

thereunder, cannot be said to be a pure & simple matter of private contract. The preliminary objection as to the maintainability of Writ Petition is answered in the negative.

(b) Merely because the dispute has arisen under the agreement, that *per se* cannot be a ground to decline indulgence in writ jurisdiction in all cases, as a matter of Thumb Rule vide *ABL INTERNATIONAL LIMITED vs. EXPORT CREDIT GUARANTEE CORPORATION OF INDIA*, (2004) 3 SCC 553. This view also gains support from *UTTAR PRADESH POWER CORPORATION LIMITED vs. C.G.POWER INDUSTRIAL SOLUTIONS LIMITED*, (2021) 6 SCC 15, which involved levy of certain amount in terms of an agreement like the one in the case at hands, on the basis of CAG Report. A Writ Court cannot deny access to an injured litigant quoting some jurisprudential theories. **Justice Oliver Wendell Holmes** of U.S. Supreme Court in *DAVIS vs. MILLS*, 194 U.S. 451 (1904) had observed:

> "*Constitutions are intended to preserve practical and substantial rights, not to maintain theories…".*

III. AS TO DENIAL OF WRIT REMEDY IN CASES INVOLVING DISPUTED FACTS:

(a) Learned Sr. Advocate appearing for the KPCL vehemently insisted upon relegating the petitioners to ordinary civil remedy on the ground of disputed facts, which cannot be easily determined under Articles 226 & 227 of the Constitution Court, regard being had to the usual constraints a Writ Court will have in matters like this. In support of this, he takes the court through several paragraphs of the FSA in general and paragraph 10 in particular. The ground of 'disputed facts' cannot be readily invoked to deny writ remedy in deserving matters. Almost all opponents in a petition like this would take such a contention, needs no research. What a Writ Court has to see is: whether there is sufficient material on record coupled with the pleadings of parties on the basis of which disputed fact matrix can be treated fairly and with no prejudice to anyone. It hardly needs to

be stated that even in large number of petitions involving violation of Fundamental Rights, the averments are almost invariably denied so that on this conventional ground, dismissal can be secured with ease. If such a ground is to be upheld, that would defeat the very purpose of incorporating Articles 226 & 227 with a broad terminology *qua* Article 32 of the Constitution and in distinction to English Law of Writs. The Apex Court in ***THE STATE OF UP vs. MOHD. NOOH, AIR 1958 SC 86*** observed *"…the rule requiring the exhaustion of statutory remedies before the writ will be granted is a rule of policy, convenience, and discretion rather than a rule of law…"*

(b) It hardly needs to be stated that in matters involving the complaint of violation of Fundamental Rights, a Writ Court has to invariably adjudge the case on merits, disregarding the "*ground of disputed facts"*. If facts are disputed, to adjudge the same appropriate modes such as issuing the commission or calling of

report may be adopted. Even in other matters which are animated with considerable public law elements, a Writ Court cannot readily deny relief to an injured litigant, mechanically quoting "*matter involves disputed facts",* if the pleadings coupled with the evidentiary material placed on record make due adjudication reasonably possible. Such cases are not *untouchable* to the writ courts. That pragmatic approach would serve the spirit of jurisdiction constitutionally vested in this court. After all, the doctrine of alternate remedy which more often than not avails to any litigant, is only a judicial invention and not a constitutional constraint; it is not a *China Wall* built between the Writ Court and the litigants. An argument to the contrary may risk the judicial process to ridicule of right thinking people.

(c) There is yet another aspect that assumes significance because of long pendency of this petition: the impugned order was made on 12.12.2011; Writ Petition came to be filed on 12.01.2012 i.e., within one

month; thus, no delay nor latches can be attributed to the petitioners; Statement of Objections came to be filed by the KPCL on 20.07.2013, i.e., a year & a half; petitioners filed Rejoinder on 7.1.2014; this Petition has been languishing in the court cupboards more than eleven years. The suggestion of this court to go for arbitration was readily accepted by the petitioners but refused by the KPCL vide Memo dated 11.8.2023. Years having rolled in the litigation process with no fault attributable any party, now relegating them to civil court, where again, years have to be spent, would certainly militate against the rules of reason & justice, to say the least. Therefore, matter having been heard at length, is being decided on merits.

IV. AS TO INVOCABILITY OF PRINCIPLES OF NATURAL JUSTICE IN CONTRACTUAL MATTERS:

(a) Conventionally speaking, the principles of natural justice belong to the domain of public law and therefore do maintain distance from the realm of private law, unless statute says otherwise. At times, these

domains share a blurred boundary, warrants no deliberation. The right question to ask is: 'whether a contract in question involves sufficient intrinsic material that would catapult it to the realm of public law…?' If answer is in the affirmative, ordinarily the principles of natural justice cannot be kept at a bay while adjudging the breach of terms of such a contract. After all, in a Welfare State like ours, John Rawls' "Justice as Fairness" happens to be an operational norm, whether one calls it a principle of natural justice or not.

(b) It hardly needs to be stated that we have an amalgam of *jus naturale and lex naturale* which assumes significance in the examination of contention of the kind advanced in the case at hand because of reports of two constitutional functionaries namely *the Comptroller and Auditor General of India (*Article 148) and *the Advocate General for the State* (Article 165). These reports have played a vital role in the shaping of impugned demand, is apparent from the record. In fact, that is one of the

contentions of KPCL. That being the position, the principles of natural justice peep in, more particularly, when the petitioners had no opportunity of participation in the audit proceedings, as such; nor did the Advocate General have their say in the matter when he "*opined for recovery of difference in cost in respect of the entire supply of coal arranged by KPCL from alternate source*". That opinion was based only on the material unilaterally furnished by the KPCL. When the impugned demand is founded on the reports/opinions of two constitutional functionaries, the contention that the matter does not involve sufficient public law elements, is difficult to countenance.

(c) Petitioners on being served with a copy of Audit Report (vide KPCL's letter dated 11.8.2010 at Annexure-V), had put forth their version vide letters dated 25.8.2010, 7.3.2011 & 23.3.2011 explaining as to why the adverse Audit Objections are unsustainable. There is no due consideration of these. Thus, the impugned demand suffers from the vice of non-

consideration of relevant material and denial of a reasonable opportunity of hearing to the stakeholders. A perusal of the correspondence between the battling parties as is available from record shows that the first respondent-KPCL changed its stand prompted by AG's Audit Report and the opinion of the Advocate General, which were generated unilaterally. Therefore, petitioners case of violation of principles of natural justice, is substantiated.

This court on due consideration sees nothing repugnant in the above three sub-paragraphs to what has been discussed by the Apex Court in *RADHAKRISHNA AGARWAL vs. STATE OF BIHAR, (1977) 3 SCC 457,* paras 20, 23 & 25. This decision was vigorously pressed into service by the learned Sr. Advocate appearing for the KPCL.

V. AS TO KPCL CONDONING DELAY AND WAIVING OF PENAL ACTION:

(a) Meaning & Scope of Article 10 of Fuel Supply Agreement assumes importance, since this article

happens to be the jugular vein of dispute. It has the following text:

> *" Article 10 - PENALTY:*
>
> *10.1. The Supplier has agreed to commence supply of coal to BTPS on commissioning which has been rescheduled July 2007.*
>
> *10.2 The delivery period stipulated in 10.1 above for the supply of coal as envisaged in Article- 5 shall be the essence of the contract. In the event of failure to commence the delivery of coal within the stipulated time specified above, Purchaser shall impose a penalty at a rate of 1/2% of initial contract value of Rs.330.09 crores i.e. Rs. 1.65 crores for every week's delay subject to a maximum of 10% of the contract value of Rs.330.09 crores i.e. Rs.33.00 crores.*
>
> *10.3 In the event of delay in commencement of mining operation or washery or due to non-availability of railway siding or for any other reason, Supplier shall arrange coal supply from any other source with the same specification and the landed cost of coal at BTPS from alternate source shall not be exceeding the price under Annexure - II. In such an event, it shall be the responsibility of Supplier to get all clearances from statutory authorities/Ministry of Coal/Railways etc. for change of source of supply at no extra cost to Purchaser. Purchaser shall not take any responsibility in this regard. Further, when the Supplier delivers coal from alternative source, penalty as contemplated in clause 10.2 above shall not apply.*

10.4 After commencement of supply as per above, the quantity stipulated for the supply of coal shall be as per clause 5.1. of Article - 5 and shall be the essence of the contract. In the event of failure to adhere to the delivery schedules, Purchaser shall impose penalty at a rate of 5% of the landed cost of undelivered quantity of coal calculated on monthly and on C.I.F.D. BTPS basis.

10.5 Further, in the event of failure to supply coal from the allotted coal block or alternate sources by the stipulated time under Article - 5 & 10.1, Purchaser is at liberty to get the coal from any other sources and the additional cost if any incurred by Purchaser over and above the agreed rate, shall be to the account of Supplier.

10.6 The above mentioned penalties will be recovered from any of the running bills of Supplier or could be readjusted through legal process."

(b) The impugned demand seeks to recover the following sums of money by invoking the provisions of Article 10 of FSA:

(i) Rs.33 crores as penalty as per Article 10.2 of FSA dated 9.5.2007;

(ii) Rs.16.44 crore for alleged difference in cost for arranging supply of coal from alternative source under Article 10.5 of the FSA; and

(iii) Rs.5.72 crore towards penalty for alleged short supply of coal under Article 10.4 of the FSA.

Arithmetically in all, this amount works out to Rs.52.63 crore. The impugned demand notice in so many words says:

> '…*the Advocate General, Karnataka, has also opined for recovery of difference in cost in respect of the entire supply of coal arranged by KPCL from alternate source… the AG Auditors have objected for the non-recovery of the amount as per the clause 10.4 of the FSA… our Auditors are objecting for the non-recovery of penalty…*'

(c) It is pertinent to note that a sum of Rs.33 crore is sought to be recovered from the petitioners by way of **penalty** in terms of Article 10.2. Mr.Aditya Sondhi appearing for the petitioners is right in pointing out that, clause 10.2 of FSA prescribes ½ i.e., 0.5% as the minimum rate of penalty, maximum being 10%. The above levy of penalty in a huge sum of Rs.33 crore is admittedly arrived at by operating the *maximum rate* as instructed in AG's Audit Report. There is absolutely no intrinsic material either in the report of the Auditor General or in the opinion of the Advocate General or in the report of Technical Committee of the KPCL as to why

the minimum rate could not have been operated and that the maximum rate should be adopted. There is no justification for the pendulum to stick to the wrong extreme. It hardly needs to be stated that an Article 12 entity like the respondent-KPCL ought to have been fair & reasonable to the petitioner company. In all fairness it ought to have told the Audit Party and notified to the office of Advocate General the enormous discretion. Thus, there is an error of great magnitude apparent on the face of the record.

VI. AS TO REPORT OF 'C & AG' AND OPINION OF 'AG' BEING THE BASIS FOR IMPUGNED DEMAND:

(a) Petitioners vide letter dated 18.7.2007 at Annexure-G had sought for condonation of delay and requested for exemption from any penalty on the ground of *force majeure.* The KPCL having considered the same, conditionally acceded thereto vide letter dated 25/26.9.2007 at Annexure-J which reads as under:

> *"Please refer to the letters cited under reference above, praying for condonation of*

> *delay involved in the supply of washed coal to BTPS unit-1 and resultant extension of time.*
>
> *In this regard, the request of M/s. KECML has been examined in detail in terms of Fuel Supply Agreement and KPCL hereby agrees to condone the delay and exempt from any penal action involved in the delay in supply of coal to BTPS – Unit-1, provided M/s KECML agrees to deliver washed coal from alternative source, i.e., from WCL, without any additional financial implication to KPCL well before the synchronization and commercial operation of BTPS unit-I without affecting the commissioning schedule."*

Audit Report faltered the action of KPCL in condoning delay and thereby exempting the petitioners from any penal action.

(b) The fact demonstrable from the record remains that the arguable delay attributable to one party to the contract having been condoned by the other in its discretion, that too after examining the terms of FSA, the liability for penalty was waived in the fitness of things. Once that happened, the KPCL could not have levied penalty on the basis of Audit objections. No reason is assigned by the Auditing Party for faltering the

condonation of delay and waiving of penal action, especially when the same was acted upon by both the parties to the contract. Such a *volte face* offends the doctrine of estoppel u/s 115 of the Indian Evidence Act, 1872 and the doctrine of promissory estoppel in the light of *UNION OF INDIA vs. INDO AFGHAN AGENCIES, AIR 1968 SC 718.* At least, the KPCL ought to have explained to the Auditing Party the circumstances that resulted into condonation of delay and waiver of penalty. It is not that the KPCL had committed any error in relieving the petitioners from the penalty, that too after a deep deliberation of the matter.

(c) Ordinarily, the report of C&AG/AG cannot be the basis for fastening of liability on others, more particularly when the foundational facts on which such liability is sought to be levied, is disputed by one of the parties to the contract vide *UTTAR PRADESH POWER CORPORATION LIMITED, supra.* In fact, in *EMTA COAL supra* it is observed that the report of C&AG cannot be

the sole basis for fastening the liability. As already mentioned above, challenge to the same is negatived by the Apex Court. There is absolutely no discussion in the AGs report as to why it suggested for the levy of penalty at the maximum rate of 10% when apparently FSA also specified the minimum rate of ½ ie., 0.5%, as already mentioned above. No explanation is offered by the KPCL either in its pleadings or in the arguments as to what prompted it to go for the extreme of 10%, besides placing reliance on the AGs Report. There is no intrinsic material much less the discussion in the said report too, that justifies the suggestion for levying penalty at the maximum rate.

VII. AS TO CONDONATION OF DELAY & WAIVER OF PENALTY BEING CONDITIONAL:

(a) There is force in the submission of Mr.Srinivasa Raghavan appearing for the KPCL that the petitioners had agreed to commence supply of coal to BTPS, after its being commissioned w.e.f. 28.7.2008, the delivery period being essence of the contract; failure to

deliver accordingly, would justify KPCL's procurement from alternate source at the cost of petitioners. Added, petitioners had not issued fifteen days prior notice as required in terms of Article 13.1 and therefore, the KPCL had procured the coal. The condonation of delay & waiver of penal action vide KPCL's letter dated 25.9.2007 being conditional, petitioners cannot argue that there is no liability on their part to make reimbursement of cost of procurement. Going by the pleadings of the parties and the documents produced by them as Annexures, there does not appear to be much dispute that the KPCL procured coal from alternate source, petitioners having failed to supply. The action of KPCL in deducting the amount payable to the petitioners towards this cost cannot be faltered because of Article 10.6 which reads: "*The above mentioned penalties will be recovered from any of the running bills of Supplier or could be readjusted through legal process.*"

(b) The above being said, the liability of the petitioners for their failure to supply coal would be co-terminus with the actual costs of procurement from alternate source and that no extra amount by way of penalty or otherwise, could have been levied, as rightly contended by Mr.Sondhi. The contention of KPCL that where condonation of delay coupled with waiver of penal action is conditional, unless the condition is satisfied, petitioners cannot take benefit of the same, appears to be too farfetched an argument. What is being construed is a contractual condition and not a constitutional instrument of mandatory nature. Therefore, the true intent of subject letter needs to be ascertained from its text & context and the attending circumstances as reflected from the contemporaneous letter correspondences between the parties. When so done, it becomes crystal clear that the KPCL intended to recover actual costs and not anything more than that. An otherwise argument would offend the sense of justice & fair play.

(c) KPCL quantified the cost at Rs.9.81 crore whereas petitioners assessed it to be Rs.6.46 crore. The version of the petitioners emanates from sub-paragraphs (i) & (ii) of paragraph (g) of their letter dated 1.11.2008 at Annexure-O. They read as under:

> *"i) Coal cost in respect of supplies from KECML has been considered at Rs.1650.47 per MT as per the Price Schedule annexed to the Fuel Supply Agreement. It may kindly be noted that the WCL's notified price for 'D' grade coal vis-à-vis the Government duties and the Railway Freight have since been revised and pursuant to the Price Revision provision of the Fuel Supply Agreement, applicable per ton gross price of coal for first 1.0 mt supplies from integrated Baranj open cast project works out to Rs. 1955.92 as per the details attached herewith and marked as Annexure-I.*
>
> *ii) Accordingly, cost of 93511.66 mt of coal supplies from integrated Baranj open cast project would have been Rs.18,29,00,391/- resulting in reduction of above alleged claim of KPCL by Rs.3,35,13,612/-. Accordingly, the alleged claim as per revised calculation would have been reduced to Rs.6.46 crores against Rs.9.81 crores stated in your letter under reference."*

This letter obviously cannot be disputed, the same having been produced by the petitioners themselves. It needs to be construed in the light of contemporaneous letter correspondence.

(d) It is also forthcoming from the records that the management of KPCL had agreed to defer recovery of additional amount till after petitioners request for exemption from the claim i.e., Rs.8.97 crore was considered. Added, the KPCL admits that, the petitioners started regular supply from 26.9.2008. It hardly needs to be mentioned that the actual costs which the KPCL had incurred on account of procurement of coal from alternate source has to be reimbursed and petitioners disinclination to do this is not justifiable. That being said, the recovery of any amount over and above the actuals being penal in nature, is impermissible. This view gains support from the KPCL's letter dated 25.9.2007 which condoned delay and gave up '*any penal action*', should they deliver coal from alternate source "*without any additional financial implication to KPCL.*" Had it been the intent of KPCL that in addition to reimbursing the costs, penalty also needed to be paid, the text of the subject letter would have been much different.

VIII. AS TO CONTENTIONS BASED ON SECTIONS 73 & 74 OF THE INDIAN CONTRACT ACT, 1872:

(a) It needs no reiteration that what is being construed is principally Article 10 of FSA, which is reproduced above. Mr.Sondhi appearing for the petitioners argued that a claim for unliquidated damages does not give rise to an enforceable debt until the liability is duly adjudicated and damages are determined on the alleged breach of a contract; such a determination, according to him, has to happen at the hands of Civil Court, arbitration having been excluded in so many words and that the paragraphs of Article 10 only provide broad parameters for undertaking that exercise. He adds that the KPCL being a party to the contract cannot unilaterally decide the dispute and determine the damages payable by the other party i.e., his clients. Mr.Srinivasa Raghavan appearing for the KPCL *per contra* contended that, petitioners argument if accepted would defeat the very purpose of incorporating a provision like Article 10 in the FSA. These conflicting propositions need

to be examined in the light of sections 73 & 74 of 1872 Act, as construed by the Courts in a catena of decisions which both the sides have pressed into service.

(b) In *STATE OF KARNATAKA vs. SHREE RAMESHWARA RICE MILLS* (1987) 2 SCC 160, wherein a term of the contract read as under:

> *"12. In token of the first party's willingness to abide by the above conditions, the first party has hereby deposited as security a sum of Five Hundred Rupees only with the second party and for any breach of conditions set forth herein-before, the first party shall be liable to pay damages to the second party as may be assessed by the second party, in addition to the forfeiture in part or whole of the amount deposited by him. Any amount that may become due or payable by the first party to the second party under any part of the agreement, shall be deemed to be and may be recovered from the first party as if they were arrears of land revenue."*

Armed with the text of above clause, the State itself had adjudged the damages and issued a certificate of recovery, which the Deputy Commissioner was coercing as if the amount comprised therein was an arrears of

land revenue. The Apex Court faltered the same by observing:

> "7. …*The terms of clause 12 do not afford scope for a liberal construction being made regarding the powers of the Deputy Commissioner to adjudicate upon a disputed question of breach as well as to assess the damages arising from the breach…"*

(c) The ratio in the said decision has been reiterated by another Three Judge Bench in *TULSI NARAYAN GARG vs. M.P. ROAD DEVELOPMENT AUTHORITY,* (2019) SCC OnLine SC 1158. Ordinarily, where a party to the contract disputes alleged breach thereof, the party complaining cannot adjudge such dispute on its own and recover damages; it only can sue for damages. This broad view emanates from *JOSHI TECHNOLOGIES INTERNATIONAL INC vs.* UOI (2015) 7 SCC 728. The contention of Mr.Srinivasa Raghavan that the fact matrix of these cases being bit different from the one at hands, the broad proposition is not invocable, does not much impress the court. A ratio from a decision has to be churned out from the facts of the case, is true;

however, that does not mean that the fact matrix should be mathematically accurate. If no two things are ever identical, no two cases too, will not be. Invariably there will be some difference between the case at hands and the Rulings cited. What one has to see is the relevance of such difference to the proposition pressed into service. Such a relevance is not substantiated from the side of KPCL to repel the invocation of the above Rulings pressed into service by the petitioners.

(d) Mr.Sondhi is also right in telling that Article 10 of FSA is not a *carta blanche* readily availing to the KPCL to levy the sum named therein, disputed facts notwithstanding. In *KAILASH NATH ASSOCIATES vs. DELHI DEVELOPMENT AUTHORITY* (2015) 4 SCC 136, what is observed at paragraphs 43.1 & 43.6 supports the submission that view:

> *"43.1 Where a sum is named in a contract as a liquidated amount payable by way of damages, the party complaining of a breach can receive as reasonable compensation such liquidated amount only if it is a genuine pre-estimate of damages fixed by both parties and*

found to be such by the Court. In other cases, where a sum is named in a contract as a liquidated amount payable by way of damages, only reasonable compensation can be awarded not exceeding the amount so stated. Similarly, in cases where the amount fixed is in the nature of penalty, only reasonable compensation can be awarded not exceeding the penalty so stated. In both cases, the liquidated amount or penalty is the upper limit beyond which the Court cannot grant reasonable compensation.

43.6 The expression "whether or not actual damage or loss is proved to have been caused thereby" means that where it is possible to prove actual damage or loss, such proof is not dispensed with. It is only in cases where damage or loss is difficult or impossible to prove that the liquidated amount named in the contract, if a genuine pre-estimate of damage or loss, can be awarded.…"

IX. AS TO VERY OBJECT OF INCORPORATING ARTICLE 10 IN THE FSA; THE WORD 'PENALTY' IS A MISNOMER & IT ONLY MEANS LIQUIDATED DAMAGES:

(a) The contention of Mr.Srinivasa Raghavan that the very purpose of incorporating a clause like Article 10 in the FSA is to exclude judicial intervention so that parties themselves can work out a remedy, is too broad a proposition. It is partly true in a case where there is no genuine dispute as to the breach of contract and what is determinable is the liquidated damages that would be

within the contemplation of the parties to the contract. It is untrue when breach of contract is genuinely disputed warranting adjudication. In the latter, the intervention of court is not intended to be excluded. While construing such a clause, a host of factors enter the fray. Added, one has to decide whether the amount stipulated is such as to make it plainly the one put *in terrorem* or a genuine pre-estimate of the interest of the party complaining breach, in due performance of principal obligation. All this assumes significance because of KPCL's contention that the word 'penalty' employed in Article 10 means only damages and that it does not have penal character.

(b) Let me examine the above submission of Mr.Raghavan that what is stated as penalty in Article 10 of FSA or in the impugned order, is nothing but damages, in the light of what the standard text books on the subject say.

(i) "Chitty on Contracts", Thirteenth Edition, SWEET & MAXWELL at page 1681 says as under:

> *"**Damages fixed by the parties.** Where the parties to a contract agree that, in the event of a breach, the contract-breaker shall pay to the other a specified sum of money, the sum fixed may be classified by the courts as a penalty (which is irrecoverable) or as liquidate damages (which are recoverable). The clause is enforceable if it does not exceed a genuine attempt to estimate in advance the loss which the claimant would be likely to suffer from a breach of the obligation in question it is enforceable irrespective of the actual loss suffered…"*

(ii) "Cheshire, Fifoot & Furmston's Law of Contract", 16th Edition, in the chapter 'Remedies for Breach of Contract' at page 35, says:

> *"The parties to a contract may agree before hand what sum shall be payable by way of damages in the event of breach, as, for example, where a builder agrees that he will pay $50 a day for every day that the building remains unfinished after the contractual date for completion. A sum fixed in this manner falls into one of two classes.*
>
> *First it may be a genuine pre-estimate of the loss that will be caused to one party if the contract is broken by the other. In this case it is called liquidated damages and it constitutes the amount, no more and no less, that the plaintiff is entitled to recover in the event of breach without being required to prove actual damage. Secondly, it may be in the nature of a threat held over the other party in terrorem-a security to the promise that the contract will be performed. A sum of this nature is called a penalty, and it has long been subject to equitable jurisdiction…"*

(iii) ANSON'S LAW OF CONTRACT, 29th Edition, OXFORD at page 565 says:

> "*The parties to a contract not infrequently make provision in the contract for the damages to be paid on a breach of contract. Such provision does not exclude the application of the general rule that damages for breach are intended to compensate for the actual loss sustained by the claimant. It is a question of the proper construction of the contract to decide whether a sum fixed by the parties, however they may have described it, is a 'penalty', in which case it cannot be recovered, or a genuine attempt to 'liquidate', that is to say, to reduce to certainty, prospective damages of an uncertain amount, in which case the sum will be recoverable*…"

(c) The propositions laid down by the Apex Court in *KAILASH NATH supra* broadly echoes the view of the above jurists. Keeping all that in mind, the word 'penalty' employed in Article 10 of FSA cannot be equated to damages because: Clause is titled as "Penalty" as well as the sum recoverable is called as 'penalty'; the sum named in clause 10.2 & 10.4 of the FSA do not have any correlation with alleged loss, but it is a sum *in terrorem*, apparently being far in excess of contemplated damages; the said sums upto 10% of the contract value (10.2) and

5% of the landed cost (10.2) in addition to any sum for procuring coal from the alternate source, are penal in nature; the AG audit report calls the sum of Rs.33 crore a penalty; impugned notice mentions these sums as being imposed as penalties. The parties to the contract are not farmers, peasants or labourers; one is a Government Company and the other is a Private Company, both dealing in huge stakes running into crores of rupees. Since they have cautiously chosen the word 'penalty', it cannot be readily construed as 'damages' inasmuch as courts cannot rewrite the contract, although they may in appropriate cases construe its terms. Clauses in an agreement ought to be given the plane, literal & grammatical meaning of the expression employed by the parties. This view gains support from *M/S. ADANI POWER (MUNDRA) LTD. Vs. GUJARAT ELECTRICITY REGULATORY COMMISSION* (2019) 19 SCC 9.

X. AS TO CAG/AG AUDIT REPORT AND OPINION OF THE ADVOCATE GENERAL BEING THE BASIS OF IMPUGNED DEMAND:

(a) The impugned order text of which is reproduced above specifically states "*The AG Auditors have objected for the non-recovery of the amount as per the clause 10.4 of the FSA.*" A portion of AG Audit Report was supplied to the Petitioners by the KPCL vide Letter dated 11.08.2010 at Annexure-V. The relevant part of the said Report reads as under:

> *"In short, as against the stipulate period for supply of coal in July 2007, KECML was able to commence supplies only in the month of September 2008 i.e., after lapse of 15 months from the scheduled date of commencement f supplies. This act of KECMl in non-adherence to the terms and conditions of FSA and also non-compliance to the obligation imposed by the Company in September 2007, entailed levy of penalty. The penalty at the rate of ½ percent of initial contract value of Rs.330.09 crore for every week's delay, from July 2007 to September 2008 (15 months or 60 weeks) that should have been levied form KECML worked out to Rs.33.00 crore (penalty at the rate of ½ per cent per week worked out to Rs.99.027 crore, but should be limited to the maximum of 10 per cent per cent of contract value). However, it is observed that the Company had not enforced recovery of this penalty, the reasons for which were not on record. Earliest*

action may be taken to recover the penalty of Rs.33.00 crore from KEMCL along with the applicable interest thereon, under intimation to Audit."

(b) Learned Sr. Advocate Mr. Sondhi is right in submitting that the Report of CAG i.e., Comptroller & Auditor General or of Auditor General for the State cannot be the sole basis for fastening financial liability on citizens more particularly when the Petitioner was not given an opportunity of participation in the AG Audit. The contention of Mr. Srinivas Raghavan, learned Sr. Advocate appearing for the KPCL that a copy of AG Report was furnished and therefore, Petitioners cannot complain of violation of principles of natural justice is difficult to agree with. In Service Jurisprudence, participation of the delinquent employee in the enquiry is one thing and supply of Inquiry Report to him is another. Both should concur in compliance, for an inquiry to be valid. An inquiry *sans* such participation indisputably being bad, does not become valid by the supply of Inquiry Report and by having delinquents view on that.

This norm applies to the case of petitioners, as well. An argument to the contrary would be tantamount to a ritualistic compliance of principles of natural justice. Had the Petitioners been permitted participation in the Audit proceedings, they could have shown the true position in terms of Article 10 of FSA. This breach does not justify the Audit Report being made the basis of impugned demand.

(c) Mr.Sondhi is also right in submitting that almost an identical question was treated by a Division Bench of this Court between the parties vide *EMTA COAL LIMITED AND ANOTHER vs. M/s KARNATAKA POWER CORPORATION LIMITED* ILR 2016 KAR 2025, wherein at paragraphs 33, 34 & 36, it has been observed as under:

> *"33. In ARUN KUMAR AGRAWAL vs. UNION OF INDIA reported in (2013) 7 SCC 1, the Supreme Court of India observed that reliefs could not be granted merely placing reliance on the report of CAG. Such report is, always, subject to parliamentary debates and it is possible that Public Audit Committee may accept the objection to the report of CAG and reject such report... The report of CAG has not yet*

> *been accepted either by the Public Accounts Committee or by the Committee of Public Undertakings…*
>
> *34. In PATHAN MOHAMMED SULEMAN REHMATKHAN vs. STATE OF GUJARAT reported in (2014) 4 SCC 156, the Supreme Court of India held that it would not be proper to refer to the findings and conclusions contained in the report of CAG, when such report has been subject to scrutiny by the Parliament…*
>
> *36. We find that the report of CAG cannot be the sole basis for any liability being caused or for that matter the sole basis for the prosecution to be launched…"*

This view has been reiterated by the Apex Court in its recent decision in *UTTAR PRADESH POWER TRANSMISSION CORPORATION supra* vide Para 60.

(d) One could have appreciated, if the petitioners were permitted to participate in the audit proceedings by furnishing entire material which prompted the Auditor General to direct the KPCL to levy & recover penalty. What applies to Audit Report more or less applies to what the office of Advocate General said, unilaterally. What papers were furnished to and what the learned Advocate General was briefed, is not forthcoming from the record.

Therefore, much credence cannot be attached to the opinion of the Advocate General also.

In the above circumstances, this Writ Petition succeeds in part; a Writ of Certiorari issues quashing the impugned order only to the extent it levies a penalty of Rs.33,00,00,000/- (Rupees thirty three crore) in terms of Article 10.2 of the FSA and also another sum of Rs.5,72,00,000/- (Rupees five crore & seventy two lakh) only in terms of Article 10.4 of the FSA; matter is remitted to the portals of first respondent-KPCL for the *de novo* determination of the amount payable by the petitioners toward the actual cost of procurement of coal from alternative source under Article 10.5 of the FSA in the light of the observations hereinabove made. The said exercise shall be accomplished within a period of eight weeks with the participation of petitioners. Contentions so far as this aspect is concerned, are kept open.

Amount deposited with the first respondent-KPCL pursuant to interim order dated 13.01.2012 shall be retained at its hands, subject to outcome of this remand.

Costs made easy.

Sd/-
JUDGE

Snb/