

CONTRACT OF INDEMNITY AND CONTRACT OF INSURANCE: A STUDY IN INDIAN SCENARIO

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ABSTRACT

Contract of insurance and contract of indemnity are the species of a same genus. All contracts of insurance are not contracts of indemnity. But all general insurance contracts are contracts of indemnity under section 124 of Indian contract Act is questionable one. In this paper, I proposed that the section 124 and 125 of Indian contract Act are applied to contract of insurance (except life insurance) also. Insurance and Guarantee are the species of a same genus .i.e., indemnity or in other words the contract of insurance and the contract of Guarantee are the development on contract of indemnity. Similarly, the doctrine of Subrogation has been introduced to carry out the fundamental rule that of indemnity. Every contract of Insurance, except life assurance, is a contract of indemnity and no more than an indemnity. Under English Law, the word "indemnity" carries a much wider meaning than given to it under the Indian Act. Under English law, a contract of insurance (other than life insurance) is a contract of indemnity. Life insurance contract is, however, not a contract of indemnity, because in such a contract different consideration apply. A contract of life insurance, for instance, may provide the payment of a certain sum of money either on the death on a person or on the expiry of a stipulated period of time (even if the assured is still alive) Indian Contract Act does not specifically provide that there can be on implied contract of indemnity.

KEYWORDS: *Contract, Indemnity, Insurance. Liability*

INTRODUCTION

Insurance primarily serves the purpose of granting security to people. It is a contract between two parties in which one party promise to protect other from losses in return of premium paid by other party. The Study of Principle of Indemnity with respect to contract of Insurance is of much importance because insurance is a Social welfare security and Indemnity in insurance compensates the policy holders for their actual monetary losses, which extends to the maximum amount of the policy of insurance. Insurance and Guarantee are the species of a same genus .i.e., indemnity or in other words the contract of insurance and the contract of Guarantee are the development on contract of indemnity. Similarly, the doctrine of Subrogation has been introduced to carry out the fundamental rule that of indemnity. Every contract of Insurance, except life assurance, is a contract of indemnity and no more than an indemnity. Under English Law, the word indemnity carries a much wider meaning than given to it under the Indian Act. Under English law, a contract of insurance (other than life insurance) is a contract of indemnity. Life insurance contract is, however, not a contract of indemnity, because in such a contract different monetary values apply. A contract of life insurance, for instance, may provide the payment of a certain sum of money either on the death on a person or on the expiry of a stipulated period of time (even if the assured is still

alive) Indian Contract Act does not specifically provide that there can be an implied contract of indemnity.

Contract of Indemnity and Contract of Insurance

Contract of indemnity is a special type of contract. The term indemnity literally means security or protection against a loss or compensation. According to Section 124 of the Indian Contract Act, 1872: A contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person, is called a contract of indemnity. Example: A contracts to indemnify C against the consequences of any proceedings which B may take against C in respect of a certain sum of money.

Contract of Indemnity

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OBJECT OF CONTRACT OF INDEMNITY

The object of entering into a contract of indemnity is to protect the promisee against unanticipated losses.

Parties to the Contract of Indemnity:

A contract of indemnity has two parties.

- The promisor or indemnifier
- The promisee or the indemnified or indemnity-holder

The promisor or indemnifier: He is the person who promises to bear the loss. The promisee or the indemnified or indemnity-holder: He is the person whose loss is covered or who are compensated

Parties to a Contract

There must be two parties, namely, promisor or indemnifier and the promisee or indemnified or indemnity-holder.

Protection of Loss

A contract of indemnity is entered into for the purpose of protecting the promisee from the loss. The loss may be caused due to the conduct of the promisor or any other person.

Express or Implied

The contract of indemnity may be express (i.e. made by words spoken or written) or implied (i.e. inferred from the conduct of the parties or circumstances of the particular case).

Essentials elements of a Valid Contract

A contract of indemnity is a special kind of contract. The principles of the general law of contract contained in Section 1 to 75 of the Indian Contract Act, 1872 are applicable to them. Therefore, it must possess all the essentials of a valid contract.

Number of Contracts

In a contract of Indemnity, there is only one contract that is between the Indemnifier and the Indemnified

Rights of Promisee/ The Indemnified/Indemnity Holder

As per Section 125 of the Indian Contract Act, 1872 the following rights are available to the promisee/ the indemnified/ indemnity-holder against the promisor/ indemnifier, provided he has acted within the scope of his authority.

Right to Recover Damages Paid in a Suit Section 125(1)

An indemnity-holder has the right to recover from the indemnifier all damages which he may be compelled to pay in any suit in respect of any matter to which the contract of indemnity applies.

Right to Recover Costs Incurred in Defending a Suit Section 125(2)

An indemnity-holder has the right to recover from the indemnifier all costs which he may be compelled to pay in any such suit if, in bringing or defending it, he did not contravene the orders of the promisor, and acted as it would have been prudent for him to act in the absence of any contract of indemnity, or if the promisor authorized him to bring or defend the suit. Right To Recover Sums Paid Under Compromise Section 125(3). An indemnity-holder also has the right to recover from the indemnifier all sums which he may have paid under the terms of any compromise of any such suit, if the compromise was not contrary to the orders of the promisor, and was one which it would have been prudent for the promisee to make in the absence of any contract of indemnity, or if the promisor authorized him to compromise the suit.

Commencement of Liability of Promisor/ Indemnifier

Indian Contract Act, 1872 does not provide the time of the commencement of the indemnifier liability under the contract of indemnity. But different High Courts in India have held the following rules in this regard:

- Indemnifier is not liable until the indemnified has suffered the loss.
- Indemnified can compel the indemnifier to make good his loss although he has not discharged his liability.
- In the leading case of Gajanan Moreshwar vs. Moreshwar Madan, an observation was made by the Chagla, J. That:
- If the indemnified has incurred a liability and the liability is absolute, he is entitled to call upon the indemnifier to save him from the liability and pay it off.

Thus, Contract of Indemnity is a special contract in which one party to a contract (i.e. the indemnifier) promises to save the other (i.e. the indemnified) from loss caused to him by the conduct of the promisor himself, or by the conduct of any other person. Section 124 and 125 of the Indian Contract Act, 1872 are applicable to these types of contracts. Again Chagla, J, stated that sections 124 and 125 are not exhaustive. The indemnified had his remedies when he suffered loss. But in equity in England he can sue when his liability has become absolute and need not wait until he has suffered loss. This remedy is available in Indian law also.

Origin and Development of Principle of Indemnity

Indemnity was restricted only to the loss occurred by human agency only as per the Indian Contract Act 1872. In *Gajanan Moreshwar vs. Moreshwar Madan*. It is stated: This definition covers indemnity for loss caused by human agency only. It does not deal with those classes of cases where the indemnity arises from loss caused by events or accidents which do not or may not depend upon the conduct of the indemnifier or any other person, or by reason of liability incurred by something done by the indemnified at the request of the indemnifier. Contractual document must state clearly the terms and conditions of indemnity. In *State Bank of India and another vs. Mula Sahkari SakharKarkhana Ltd*. It is stated: A document, as is well known, must be construed on the basis of the terms and conditions contained therein. It is also trite that while construing a document the court shall not supply any words which the author thereof did not use. The document in question is a commercial document.

Contract of Insurance

Insurance may be defined as a contract between two parties whereby one party called insurer undertakes, in exchange for a fixed sum called premiums, to pay the other party called insured a fixed amount of money on the happening of a certain event. It means protection against loss. It is the process of safeguarding the interest of people from loss and uncertainty. It is based on the contract. It is a valid agreement that incorporates certain terms and conditions. It may be described as a Social welfare device to reduce a risk of loss to life and property. Motor, Marine, Fire, and Life are the most common varieties of insurance. Whatever be the kind of the insurance or the risk insured against there are certain principles of insurance law. Every contract of insurance, except life insurance is a contract of indemnity, every contract of insurance is a contract of absolute good faith and requires some insurable interest to support it, without which it will be a mere wager. In order for an insurance contract to be legally binding, certain essential requisites must be stipulated in the contract. These elements are classified into two broad categories:

The essential elements of a general contract:

1-offer and acceptance, 2-consideration, 3-legal capacity, 4-legal purpose, 5-Free Consent

The essential elements of a contract of insurance:

1-indemnity, 2-insurable interest, 3-utmost good faith, 4-subrogation, 5-assignment and nomination, 6-warranties, 7-proximate cause, -return of premium.

The life policies can be assigned whether the assignee has an insurable interest or not. Life policies are frequently charged, assigned or otherwise dealt with, for they are valuable securities. The marine policy is freely assignable unless it contains terms expressly prohibiting assignment. It assigned either before or after a loss. A marine policy may be assigned by endorsement thereon or in another customary manner. In practice, a marine cargo policy is frequently endorsed in blank and becomes in effect a quasi-negotiable instrument.

POSITION IN INDIA

It has been noted above that section-124 recognizes only such contract as a contract of indemnity where there is a promise to save another person from loss which may be caused by the conduct of the promisor himself or by conduct of any other person. It does not cover a promise to compensate for loss not arising due to human agency. Therefore, a contract of

insurance is not covered by the definition of section-124. Thus, if under a contract of insurance, an insurer promises to pay compensation in the event of loss by fire, such a contract does not come within the purview of section-124. Such contracts are valid contracts, as being contingent contracts as defined in section-31. In *United India Insurance Co. vs. M/s. Aman Singh Munshilal*. The cover note stipulated delivery to the consigner. Moreover, on its way to the destination the goods were to be stored in a god own and thereafter to be carried to the destination. While the goods were in the god own, the goods were destroyed by fire. It was held that the goods were destroyed during transit, and the insurer was liable as per the insurance contract. According to section 124 of the Indian Contract Act, a contract of indemnity means, a contract by which one party promises to save the other from loss caused to him by the conduct of the promisor himself or by the conduct of any other person. A contract where one party promises to save other from loss which may be caused, either By the conduct of promisor himself or by the conduct of any other person. Definition given in Sec. 124 is very narrow. It includes only: Express promises to indemnify, and the loss caused by the conduct of the promisor or any other person. However, it does not include: implied promises to indemnify, and loss caused by accidents and events not dependent upon the conduct of the promisor or any other person. Section 124 does not cover a promise to compensate for loss not arising due to human agency *Gajanan Moreswar vs. Moreswar Madan*. Therefore, strictly speaking, contracts of insurance cannot be included in the definition. A contract of insurance can be described as a contract of indemnity under English law; it saves the promise harmless from loss caused by accident. It may not cover by section 124 but that section is not exhaustive. An insurance contract is really only a contract of indemnity under Indian law also. In case of insurance policy the party desiring to be protected from any loss or damage in consideration of payment of proportionate advance premium, the terms of insurance policy have to be strictly read. In the case of *New India Assurance Company Ltd. Vs Kusumanchi Kameshwra Rao & Others, 1997*, court held that a Contract of indemnity is a direct engagement between two parties thereby one promises to save the other harm. It does not deal with those classes of cases where the indemnity arises from loss caused by events or accidents which do not or may not depend on the conduct of indemnifier or any other person. Thus, if under a contract for insurance, an insurer promises to pay compensation in the event of loss by fire, such a contract does not come within the purview of section 124. Such a contract is valid contract as being contingent contract as defined in section 31. However, it was not the intention of the legislature, as it has been held by Justice M.C. Chagla that: Sections 124 and 125 of the Contract Act are not exhaustive of the law of indemnity and the Courts here would apply the same equitable principles that the Courts in England do." *Ganjanan Moreshwar v. Moreshwar Madan*

POSITION IN ENGLAND

A contract of insurance can be described as a contract of indemnity under English law, it saves the promise harmless from loss caused by the accidents. The word indemnity carries a much wider meaning than given to it under the Indian Contract Act. It includes a contract to save the promise from a loss, whether it be caused by human agency or by other natural factors also like an accident and fire. English Law has given a comprehensive definition which is as follows: "A promise to save another harmless from loss caused as a result of a transaction entered into at the instance of the promisor." Under English law, a contract of insurance is a contract of indemnity except life insurance. Life Insurance contract is not a contract of indemnity, because in such a contract life of men cannot be preciously valued and different considerations apply to different policy of insurance. A contract of life insurance, for instance, may provide the payment of a certain sum of money either on the death of a person, or on the expiry of a stipulated period of time (even if the assured is still alive). In such a case, the question of amount of loss suffered by the assured, or indemnity for the same, does not arise. Moreover,

even if a certain sum is payable in the event of death, since, unlike property, the life of a person cannot be valued, the whole of the amount assured becomes payable. For that reason also, it is not a contract of indemnity. From the above analysis under English law, the loss might be caused by a human agency or by other natural factor also.

CONCLUSIONS

Section 124 of Indian Contract Act 1872 does not exhaustive. It deals only with one kind of indemnity that is indemnity, which arises when loss is occasioned by the conduct of the indemnifier or of a third party. This Act does not specifically provide that there can be an implied contract of indemnity. As per the general insurance contract, the insurer is liable to compensate the insured if risk occurred due to accidents (like motor, marine and fire) subject to the terms and conditions of policy of insurance. In this type of contracts only actual loss is compensated by the insurer to the insured and not more than that. But in life insurance contract, a life of men cannot be precisely valued. So the life insurance contracts are not within the purview of contract of indemnity. However, in the general insurance contracts are contracts of indemnity and it attracts under section 124 of Indian Contract Act 1872 with certain terms and conditions of policy of insurance. The Law Commission of India in its Report (13th Report, 1958, on Indian Contract Act, 1872) has recommended the amendment of section 124. According to its recommendation, the definition of the Contract of Indemnity in section 124 is expanded to include cases of loss caused by events which may or may not depend upon the conduct of any person. It should also provide clearly that the promise may also be implied. To conclude and suggest that the principles of contract of indemnity has to be covered with the contract of insurance and the English law principles of indemnity has to be adopted in Indian law also.

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