NO COMPENDSATION FOR DELAY IN CONSTRUCTION CONTRACTS

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"We can only see a short distance ahead, but we can see plenty there that needs to be done."

- Alan Turing

INTRODUCTION

This paper analyses contract clauses which bar compensation on the occasion of any delay in performance of the contract. Such clauses are often seen in construction contracts. This paper also analyses the jurisprudence of such clauses, and its relation to the Indian Contract Act. In the later parts, the paper deals with the issue of delay and compensation in construction contracts and what are the factors the arbitrators and courts take into consideration while interpreting such contracts.

CONSTRUCTION CONTRACTS- DELAY AND COMPENSATION

Construction contracts are legally binding documents between the owner and the contractor. Most of these contracts entail completion dates. But, at times the contractors are not able to complete the projects within the stipulated time frame which leads to inordinate delay. There can be multiple reasons for delay in contracts, in some cases delay can be caused because of insufficient supply of materials, delay in execution, delay caused by force majeure events etc.

Delay can often lead to escalation in costs. Because of the rise in cost of performance, the contractor would expect to be paid more. Such a situation can often lead to a dispute between the parties to the contract. In cases of disputes, most of the parties enter into an arbitration proceeding, arbitration clauses form integral part of such contracts.

Some construction contracts have clauses restricting the responsibility to pay damages in case of delay. Courts have not identified a minimum quantity of delay in the project which is necessary to qualify as delay. In lieu of damages, the contractor/s are only entitled to an extension of time to complete their work. Some of these clauses contain an exception clause as well, which encapsulates the situations where no damage for delay clause would not apply such as, where the delay is caused by bad faith or fraud by one of the parties.

In Hudson's Building and Engineering contracts,[1] there is reference to no-damage clauses, they define it as an American expression, "used for describing a type of clause which classically grants extensions of time for completion, for variously defined ―delays".

The Indian Contract Act governs the question of delay in performance of the contract under Section 55 and 56. For instance if there is an unexpected rise in the price of material and labour then, it may frustrate the contract and the parties then would not be required to perform the contract. In contracts where time is of the essence of an obligation, failure to perform within the stipulated time would entitle the innocent party to terminate the performance of the contract and claim damages from the infringing party. [2]

IMPACT ON PUBLIC POLICY

An important issue which arises vis-à-vis the enforceability of the no damages for delay clauses is their impact on public policy. Such contracts purport to extinguish or waive the rights of a party to damages or an equitable adjustment arising out of unreasonable delay in performing the contract, thus it can be argued that such clauses are against the public policy.

Section 23 of the Indian Contract Act provides that the consideration or object of an agreement is unlawful if it is opposed to public policy. The term public policy has been scrutinized by the Supreme Court in a number of cases. In the case of *Indian Financial Association of Seventh*

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[1] I.N. Duncan Wallace. *Hudson's Building and Engineering Contracts*, 11th ed, pp. 1098-9, London: Sweet & Maxwell.

[2] Chitty, Joseph, and H G. Beale, 1999. *Chitty on Contracts*, 28th ed, pp. 1106, London: Sweet & Maxwell.

Day Adventists vs. M.A. Unneerikutty and Another,[3] the Supreme Court discussed the meaning of expression public policy in Section 23 of the Indian Contract Act. The court cited a passage from Maxwell, interpretation of the statute, which read as follows "*Everyone has a right to waive and to agree to waive the advantage of a law or rule made solely for the benefit and protection of the individual in his private capacity which may be dispensed with or without infringing any public right or public policy. Where there is no express prohibition against contracting out of it, it is necessary to consider whether the Act is one which is intended to deal with private rights only or whether it is an Act which is intended as a matter of public policy....*" The court pointed out that the concept of public policy is not static and it changes with time. A law made for the benefit of an individual can be waived by a private person, however when such a law includes public policy elements, the law cannot be waived because then it becomes a matter of public policy or interest. In the case of *Centrotrade Minerals and Metal Inc. v. Hindustan Copper Ltd*,[4] the court pointed out that an agreement under no circumstance can violate the public policy.

The Delhi High Court in the case of *Simplex Concrete piles (India) Ltd. vs. Union of India*, [5] (hereinafter "*Simplex*") pointed out that Section 73 and 55 deal with effect of breach of contract in case of delay. The court held that both of these sections form the heart and foundation of the Contract Act. The court was of the view that the contract clauses which disentitled the parties form the benefit of Section 73 and 55 of the Act would violate Section 23 of the Contracts Act. Thus it was held that the no-damage for delay clauses were against the public policy.

The Delhi High Court in, *Public Works Department vs M/S Navayuga Engineering Co Ltd* [6](hereinafter "*PWD*") distinguished the *Simplex* case, the court pointed out that in *Simplex*, the contractor had no option to sue for damages in case of a breach, however in the *PWD* case once the contractual period was over the petitioner could have opted to not agree for the extension of the time period and thus could have sued for damages.

[3] (2006) 6 SCC 351
[4] (2006) 11 SCC 245
[5] (2010) 115 DRJ 616
[6] 2014 SCC OnLine Del 1343

The Supreme Court in the case of *Ramnath International Construction (P) Ltd. vs Union Of India,*[7] *(*hereinafter *" Ramnath")* held no damage clause to be valid, however it is to be noted here that the clause imposed a clear bar on any claim for compensation of delays in which extension had been sought and obtained. Thus, here also it can be argued that the party had the option of not agreeing for the extension and sue for damage after ending the contract.

There has been no conclusive observation by the Supreme Court as to whether the no-damage-for delay clause is opposed to the public policy. But, the Delhi high court in the *PWD* case held such clauses to be in conformity with the public policy, whereas the court in the *Simplex* case took an opposite view. However, the court in the former distinguished the contract clause from the latter and as discussed above, pointing out that such clauses will not be against the public policy as long as the parties have the option to end the contract and sue for damages. However, if this observation is held to be valid by the Apex court, then it would repudiate the purpose of such clauses. Parties agree to enter into such contracts to avoid the already delayed process, the Delhi High Court should have taken this into consideration while deciding the public policy aspect.

IMPACT ON AWARD GIVEN BY ARBITRATOR

Construction contracts mostly entail an arbitration clause. Parties prefer to enter into arbitration in case of conflict rather than going to the courts, to save time. The major issue which arises in arbitration proceedings is that whether the arbitrator is bound by the clause which prohibits the parties for claiming damages in case of delay.

In *Ramnath* case, the arbitrator proceeded to award damages on ground of delay on the reasoning that the contractor is entitled to compensation, unless the employer establishes that the contractor has consented to accept the extension of time alone in satisfaction of his claim for delay. The Apex Court however held that the contract stipulated a clear bar on any claim for compensation for delays, in respect of which extensions have been sought and obtained. Thus, they pointed out that the arbitrator exceeded his jurisdiction in awarding damages,

[7] (2007) 2 SCC 453

ignoring the contract entered between the parties. On the other hand, in *Asian Techs Ltd vs Union of India,* [8] (hereinafter "*Asian techs*") case the Supreme Court held that the clause did not prevent the arbitrator to award damages. The two cases gave conflicting opinions.

The Delhi High court in the *Simplex* case, dealt with the controversy created by the two opposing views of the Apex court. The court opined that the judgment in the *Asian techs* case furthers the object of the Contract Act. However, the court refrained from commenting as to which of the two cases would prevail.

It is to be noted that both the judgments, *Ramnath* and *Asian techs* are decided by two judge bench and both cases deal with identical clauses. Further, *Asian techs* was decided after *Ramnath* but it does not refer to the latter in the judgment. However, *Ramanath* has been followed in subsequent cases[9] also by the Apex Court.

The Delhi High court in the *PWD* case, distinguished *Asian techs* and pointed out that in the latter, the respondent had given clear assurance to the appellant to continue the work and that the rates would be decided across table. And based on this the appellants went ahead with the work. The court pointed out that the respondent cannot claim that the appellant has no right to ask for further amount, given that they never finalized the rates "across table". And thus the court held that the arbitrator would have jurisdiction to award the same. Therefore, the Delhi High court observed that in a no-damage for delay clause, the arbitrator cannot award damages and by distinguishing the *Asian techs* case they pointed out that the court upheld the award by the arbitrator only because the respondent assured the appellant that they would settle the prices across table but later denied doing the same.

Thus, until the matter is decided by a higher bench of the Supreme Court it cannot be said which of the two conflicting judgments would prevail. However, considering the jurisprudence of the courts it seems likely that the arbitrator cannot grant an award exceeding the contract clauses.

[8] (2009) 10 SCC 354
[9] Oil & Natural Gas Corp vs M/S Wig Brothers Builders & Engineers Pvt. Ltd. (2010) 13 SCC 377.

CONCLUSION

The clauses to restrain claims for compensation in cases of delay are incorporated in the construction contracts frequently. The Apex court has ruled in favour of such clauses. However, certain aspects related to the same remain uncertain. Such clauses are comparatively new in the Indian jurisprudence and one can expect an Apex Court judgment in the long run, hopefully clarifying the aspects of such clauses.

While dealing with cases relating to such contract clauses, the courts should take into consideration the intention of the parties and the purpose of the clause. The courts should take a progressive view and hold the clauses to be in conformity with public policy, as such the clauses are for individuals in their private capacity, they do not impact the public at large and thus do not entail any public policy element. The courts should also consider the party autonomy in deciding the terms of the contract, and the arbitrators should refrain from exceeding their jurisdiction by going against the terms of the contract.