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Exclusion of Liability Clauses in Government Contracts

■ Mohit Goel & Sidhant Goel

As a matter of practise, most government contracts these days contain a clause that excludes any liability for payment of damages in case of any delay in execution of the works that may be attributable to the government undertaking / government corporation.

One such representative clause is reproduced below:

"In the event of any failure or delay by the Employer/Engineer in fulfilling his obligations under the contract, then such failure or delay, shall in no way affect or vitiate the contract or alter the character thereof; or entitle the Contractor to damages or compensation thereof but in any such case, the Engineer shall grant such extension or extensions of time to complete the work, as in his opinion is/are reasonable."

JUDICIAL PRECEDENTS GIVING EFFECT TO SUCH EXCLUSION CLAUSES

Such exclusionary clauses have been held to be applicable in several judgments to exonerate the government undertaking from liability for damages caused to the contractor due to delays. Courts have consistently held parties bound to such clauses. Reference may be had to the judgment, titled ONGC v. Wig Brothers, reported at (2010) 13 SCC 377, where the Hon'ble Supreme Court placed reliance on the its earlier judgment in Ramnath International Construction (P) Ltd. v. Union of India, reported at (2007) 2 SCC 453, to hold that "such a clause amounts to a specific consent by the contractor to accept extension of time alone in satisfaction of claims for delay and not to claim any compensation; and that in view of such a bar contained in the contract in regard to award of damages on account of delay, if an arbitrator awards compensation, he would be exceeding his jurisdiction". Given that an arbitrator is a creature of the Contract, the Hon'ble Supreme Court has held that the arbitrator would be exceeding his jurisdiction if he ignores the said express bar contained in the contract and awards compensation.

CONTRARY VIEW OF THE DELHI HIGH COURT ON SUCH EXCLUSION CLAUSES

There is, however, one case of the Hon'ble Delhi High Court, titled Simplex Concrete Piles v. Union of India, C.S. (OS) No.614A/2002, decided on 23 February 2010, which has taken a contrary view. In this case, (late) Justice Valmiki Mehta held that such exclusionary clauses are void under Section 23 of the Indian Contract Act, 1872 (the "Contract Act"), being contrary to the public policy of India. This case is currently pending in appeal before a Division Bench of the Hon'ble Delhi High Court, and it remains to be seen what the outcome would be.

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IS THE CONTRACTOR REMEDILESS IN THE FACE OF SUCH EXCLUSIONARY CLAUSES?

The way forward in such cases has been suggested by the Hon'ble Supreme Court in the case of General Manager, Northern Railway v. Sarvesh Chopra, reported at (2002) 4 SCC 45. Relying on Section 55 of the Contract Act, the Hon'ble Supreme Court held that the contractor was entitled to avoid the contract at its option on account of delay in performance of the contract by the employer and claim damages, thereby treating the delay in performance as a fundamental breach of the contract by the employer. The Hon'ble Supreme Court, however, cautioned that if the contractor does not avoid the contract and accepts the belated performance of reciprocal obligation on the part of the employer, the contractor cannot claim any compensation for any loss occasioned by the non-performance of the reciprocal promise by the employer at the agreed time, unless at the time of such acceptance, he gives notice to the employer of his intention to do so.

FACTORS REQUIRING CONSIDERATION

In the opinion of the authors, for the applicability of such exclusionary clauses, a three-factor test must be satisfied in cases where there is delay in performance by the employer:

(a) the contractor must have sought extension of time for performance of the contract;

(b) the contractor must have been granted such extension of time by the government undertaking without any change in conditions applicable to such performance; and

(c) the contractor must have performed the Contract in such extended time period.

If the above three facts exists, any claim raised by the contractor for delay in performance by the employer would fall outside the jurisdiction, and authority, of the arbitral tribunal.

CONCEPT OF "CAPPING" OF DAMAGES

If the contractor has also been granted escalation on the prices quoted by it, then that becomes another factor against the contractor. In the opinion of the authors, such escalation could be termed as the "cap" on the liability of the employer in case of delay, and be covered by the principle of law enunciated by a Constitution Bench of the Hon'ble Supreme Court in the case of Chunilal

Mehta And Sons, Ltd. v. The Century Spinning and Manufacturing, reported at AIR 1962 SC 1314.

APPLICABILITY OF THE PRINCIPLE OF CONTRA PROFERENTUM

Having said this, in the opinion of the authors, such clauses should not come into operation in certain situations which do not strictly fall within the four corners of such exclusionary clauses. For example, if the contract exonerates liability of the employer in cases where there is delay in handing over land to the contractor progressively, then the employer ought to be held liable to pay damages if it fails to provide any land to the contractor at the beginning of the contract. In such a case, the principle of contra proferentum should be brought into play to construe such exclusionary clause strictly against the employer, given that typically such clauses are part of standard form contracts drafted by the employer.

CLAIM FOR LOST PROFITS IN CASES OF DELAY

In view of the above, the authors opine that contractors need to understand when to "pull the plug" on the contract that is being plagued by delay, and claim such delay to be a fundamental breach of the contract. Adopting such course of action, and proving fatal delay on the part of the contractor could entitle the contractor to claim lost profits on the unexecuted portion of the contract in terms of the judgment of the Hon'ble Supreme Court in the case, titled A.T. Brij Paul Singh v. State of Gujarat, reported at (1984) 4 SCC 59.

OUTCOME OF CHALLENGE TO VALIDITY OF EXCLUSIONARY CLAUSES BY THE HON'BLE SUPREME COURT

It would also be interesting to see whether such clauses are tested on the anvil of Section 23 of the Contract Act before the Hon'ble Supreme Court, something that has not yet happened. There are some compelling arguments, which could be made regarding the very legality of clauses that exclude, and not just limit, the liability of the employer in such one-sided "take-it-or-leave-it" contracts.

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