Claim and Dispute Resolution in Construction Contracts

G.C. Kabi
Arbitrator Govt. of India

Abstract: India has an ambitious plan to revamp and create railways, inland waterways, ports, highways and smart cities. This paper examines the existing mechanisms of claim settlement and dispute resolution in construction contracts in India and its adequacy including proposed legislative reforms and suggestions.

Genesis of claims and disputes and types

Construction contracts being executory claims arise naturally as per terms of contract. Claims also arise on differing interpretation of express terms of contracts or terms implied on facts, obligation implied in law and allegation of breach of contract. Payment for work done and extension of time claims may be expressed in contract but handing over site and issue of drawings by employer (in certain contracts) and duty of ‘reasonable skill and care’ by the contractor are either expressed or implied on facts (goes without saying or as business necessity). If design is by contractor the implied obligation is not merely of reasonable skill and care but also of fit for purpose and liability is not restricted to negligence. Where language on variation is not clear a term can be implied depending on type of contract, employer requirement at the time of formation.
of contract and nature of variation for extra claim. Contract should be ad idem but parties differ on interpretation. Obligation of restitution is implied in law to prevent undue enrichment and failure to restore benefit enjoyed has consequences as in breach of contract though there is no contract. In breach of contract single cause may give multiple claims unless remote with remedy in contract or law. Unlike in restitution where the measure of compensation is benefit enjoyed (restoration is not possible when the work gets fixed at site to become property of employer and hence only compensation) damages in breach is for loss suffered putting the innocent party in a position if the contract would have been performed (thus also differ from tortious damages). Examples are non-delivery of work front, drawings, payments, and decisions etc by employer or delay or non-performance by contractor. On allegation of breach no pecuniary liability arises on the party alleged to have committed breach except a claim of damages by the innocent party till breach is proved by the innocent party and damages assessed in adjudication. In common law the primary remedy in breach of contract is claim of damages and not specific performance of contract. The damages in total breach resulting non-performance of contract are partly different from damages in partial breach when contract has to be performed by the innocent party. Claim of loss of profit is admissible in total breach and non-performance of contract there by but not in partial breach as the contract is to be performed with right to claim damages. In partial breach disruption and delay give rise to different types of claims. Disruptions may not cause delay in every case. Delay entitles to damages for fixed costs in addition whereas disruption for idle resources only. Acceleration cost claims are admissible in delay but not on mere disruption. Duty of mitigation of loss is applicable only for the secondary issue of assessment of damages when breach is established and it is the duty of the party in breach to prove so. This duty cannot be too exacting on behalf of the party who has committed breach. Loss should be real on evidence and not presumptive, but arbitrator in certain circumstances may base on guesswork for quantification once loss is evidenced. Claims on termination of contract are often hotly contested, both contractually and legally. Non-compliance of procedure in contract or requirement of law may make termination illegal even if justified and itself constitutes a breach of contract. Law does not allow frustration due to commercial hardship but parties are free for novation. Most claims in private contracts are settled but not in public sectors where disputes lead to arbitration. Public authorities can hardly settle claims of damages without adjudication. A claim asserted by one party and denied by the other becomes a dispute. Disputes cannot be prevented altogether but can certainly be managed. Adoption of balanced FIDIC documents in National Highway Authority of India has not reduced disputes as it is not enough to adopt good documents but to perform contracts.

Dispute Resolution Mechanisms

Court is the usual forum for justice, but courts cannot monitor contracts and hence only awards damages. Construction contracts need timely intervention for performance of contract. Arbirtation is preferred to court as a neutral forum when foreign parties are involved and courts only facilitate adjudication. The courts in India are burdened with huge pendence. Hence alternative dispute resolution (ADR) mechanisms like negotiation, mediation, expert opinion, dispute review or adjudication, mini-trial, conciliation, arbitration or a combination of these are used for settlement of claims and resolution of disputes outside the court.

Negotiation is by the parties themselves without involving third party. Parties are in control of process and outcome. This is unsuccessful in public sectors due to rule based rigid position undertaken and risk aversion particularly in claim of damages in breach of contract.

Mediation is assisted negotiation; assistance provided by third party the mediator, to reach a negotiated settlement by the parties. S.89 of CPC as well as s.30 of the Arbitration and Conciliation Act, 1996 refers to mediation, but there is no statutory procedure prescribed for mediation. In court referred mediation rules are to be framed by the court. Mediation is hardly used in construction contract claims and disputes involving public sectors.

Conciliation is reaching settlement authenticated by conciliator and thus differs from mediation having a statutory procedure. As per Supreme Court in conciliation substantial compliance of s.73 of the Arbitration and Conciliation Act, 1996 is not sufficient and complete compliance is necessary. There is no challenge or appeal to conciliation as it results in settlement. An arbitrator can act as conciliator in the proceedings but despite the legislative intent, conciliation has not been used in construction sector in India.

Contractual decision of senior officers and appeal to such decisions provided in some contracts are not conciliation as many presume, as in conciliation the parties only agree and decide and there is no third party decision.

The processes are represented under

| A D R (Alternative Dispute Resolution) v Court NEGOTIATION MEDIATION CONCILIATION ARBITRATION COURT OF LAW OR COMBINATIONS |
| INFORMAL | FORMAL |
| (FORMALITY LINE) | |
| CONSENSUAL | BY IMPOSITION |
| GREATER CONTROL | DIMINISHING CONTROL |
| (LINE OF CONTROL) | |
| By Parties | By 3rd Party |
| NON LITIGATIVE | LITIGATIVE |
| NON BINDING | BINDING |
| Equity Based | Justice Based |

Dispute Resolution / Adjudication Board / Committee are provided in many contracts, which are to be exhausted before seeking arbitration unless waived. In India the unsuccessful party invariably goes to arbitration and decisions of DAB though contractually binding in the interim till arbitral award, are disregarded. India has no statutory interim adjudication as Construction Industry Payment & Adjudication Act 2012 Kulailumpur. The proposed Public Contracts [Resolution of Disputes] Bill, with Tribunal having judicial composition to partly adjudicate and refer to arbitration” or “adjudicate fully”, in its current format is unworkable and conflicts treaty obligations under New York Convention for international commercial arbitration as adjudication has to be in arbitration and not in municipal public forum.

If the remedy is only to claim damages in arbitration for breach of contract for non compliance of interim binding decision of adjudication the intended purpose of such adjudication is lost. In an interesting decision in serial adjudication in Interserve Industrial Services Ltd. vs. Cleveland Bridge UK Ltd. (2006) EWHC 741 (TCC), the Court Wrote:
"Where the parties to a construction contract engage in successive adjudications, each focused upon the parties’ current rights and remedies, in my view the correct approach is as follows. At the end of each adjudication, absent special circumstances, the losing party must comply with the adjudicator’s decision. He cannot withhold payment on the ground of his anticipated recovery in a future adjudication based upon different issues.”

This was followed in YCMS Ltd v Grabiner[2009] EWHC 127 (TCC).

Arbitration is the most used mechanism for resolution of construction contract disputes in public contracts primarily because its decision is final and binding and it follows a judicial process. Despite the Arbitration and Conciliation Act 1996 being a progressive legislation on the line of UNCITRAL modal law dispute resolution has not been satisfactory in arbitration in India. The reasons, proposed legislative reforms and suggestions are as under:

Issues and legislative reforms

Lack of institutional and professional arbitration without regulation has created trust deficit prompting courts to interfere and setting judicial precedents making arbitration nugatory. Adhoc arbitration with multiple short hearings conducted leisurely in offf-time with excessive oral evidence and then routine challenge of arbitral awards makes it an eternal process instead of resolving any disputes. Huge amounts are locked in dispute blocking projects. The proposed amendment to the Arbitration Act approved by the Cabinet reportedly provides statutory time line and regulates cost with accountability on arbitrator and parties. Internationally such aspects are regulated by institutional rules and not by legislation. Also arbitral awards are made enforceable even if challenged unless stay granted specifically on recorded reasons. It fixes timeline to dispose cases by courts and gives narrow interpretation to public policy so as courts not to re-appreciate facts or go on merits or erroneous application of principle of law as ground for challenge to undo the unintended consequences of ONGC v Saw Pipes Ltd.[2003] 5 SCC 705 and reverse the ratio of the recent decision of Supreme Court in ONGC v Western GECO (2014)9 SCC 263 which created further new sub heads of public policy under fundamental principles of Indian Law. Similarly in Bhatia International v Bulk Trading S.A.[2002]4 SCC 105 PART I of the Act was applied to give interim relief in foreign seated arbitration, but the subsequent judgments interfered with foreign awards allowing challenge in India keeping the requirement of bar of implied exclusion of PART I in foreign seated arbitration very high. In Bharat Aluminiurum v Kaiser Aluminium Service dated 06.09.2012 the Supreme Court reversed this ratio re-stating the law. The proposed Act recognizes the same and tries to fill the existing gaps. Employee Arbitrators are barred to act as arbitrator. Powers of arbitrator on jurisdiction partially lost on judicial pronouncements are restored. Tribunal is given more power on interim measures.

Suggestions

i. No doubt the proposed legislative reform would fix major issues of delay and enforcement of awards making arbitrator and parties accountable so far legislative framework is concerned, but quality of arbitration cannot improve without ad-

equate pool of competent professionals to handle arbitration. We need world-class arbitral institutions and techno-legal professionals which cannot be developed overnight. Legal education must be liberalized. Masters Courses in Construction law should be introduced in top law universities with doors open to engineering graduates. Education must liberate and reform itself first.

ii. Fast track arbitration and emergency arbitration are necessary in construction contract disputes to provide early resolution of disputes and interim enforceable decisions respectively to avoid delay in projects. This is possible through institutional rules and parties adopting the same, with legislative support. Also rules for multiparty arbitration should be adopted on the line of recent UNCITRAL rules 2010.

iii. The Commercial Division of HIGH Court Bill is pending since long and without its implementation the disposal cannot be as envisaged.

iv. India ranks 186 out of 189 counties in enforcement of contracts as per World Bank. Disputes are but natural as contracts are not respected in India. Perception of unfair outcome in arbitration is partly due to misunderstanding contracts and consequences of ignorant actions. Contractual actions on justified grounds should not be vitiated on procedurally illegality. Decisions in disputes are governed by substantive law and terms of contract; fairness and natural justice which are for rules of conduct of arbitration. Law should permit arbitration to be inquisitorial rather than adversarial to be more fair and quick. People in government and public sectors handling contracts must learn the basic concepts of contract law. It is a massive task considering the complacency, lack of knowledge and skill and the number of organizations involved. It is not out of place to state that many handle large contracts without the required knowledge and the outcome is often disastrous.

v. Since the decision in White Industries case in 2011 India has awakened to a new reality of foreign parties invoking treaty obligations. In that case delay in higher judiciary consequent to a foreign award was the cause of investment treaty arbitration. Such delay was held to be a failure of Indian State to provide ‘effective means of assertion of claims and enforcement of contracts’ as per treaty obligation. Since then in a series of cases international commercial arbitration has been invoked by foreign players forcing India reconsider our bilateral investment treaties. India has to accept global practices by respecting contracts and developing its institutions rather taking protective measures against international arbitration if order to attract foreign investment.

vi. The opt-repeated slogan of India becoming a hub of international commercial arbitration is a day-dream. When India debates and discusses amending arbitration law for one-and-half decade Singapore has already established an International Court of Arbitration with foreign nationals as judges both from civil and common law countries. Nowhere in the world like in London or now in Singapore world class arbitration hub is possible without active support of judiciary. This cannot be expected unless India develops professional institutional arbitration. It is time to act...