PETITIONER:
NATIONAL FERTILIZERS

Vs.

RESPONDENT:
PURAN CHAND NANGIA

DATE OF JUDGMENT: 17/10/2000

BENCH:
M.J.Rao, K.G.Balakrishnaan

JUDGMENT:
of 1995
L.....I.....T.....T.....T.....T.....T.....T..J

J U D G M E N T

M.JAGANNADHA RAO,J.

This appeal, which arises out of an award passed under the Indian Arbitration Act, 1940 concerns the interpretation of a 'variation' clause in the contract which allows the appellant, the National Fertilizers Ltd., to issue directions to the contractor varying the extent of the contract work, both upwards and downwards upto 25%. Question is whether ( as contended by the appellant) the said 25% is to be arrived at by taking into account the net overall increase in the work i.e. by adding up the increases in work and deducting therefrom the decreases in work or whether ( as contended for the respondent-contractor) the 25% was to be computed by adding up the total variations, both

involving the increase in the work and the decrease in the work. The importance of the point is that if the variations exceed 25% of the contract price, the contractor is not confined to the contract rates but can claim market rates.

The disputes were referred to arbitration and the arbitrator gave a non-speaking award. The arbitrator's award was set aside by the learned District Judge on the ground that the reference was bad. He, however, gave alternative findings accepting the conclusions in the award. As the learned District Judge held the reference was bad, he set aside the award. The contractor appealed to the High Court which by its judgment in Civil Misc.(First)Appeal No.211 of 1991 dated 18.10.94 held the reference was valid and allowed the appeal and directed the award be made Rule of Court. It is against the said judgment that this appeal is preferred.

The facts of the case are as follows. Quotations were called by the appellant for works amounting to Rs.3,39,88,000. It appears that the respondent submitted his quotation which was opened on 12.9.84. His tender was accepted. But, instead of giving him the entire contract, the appellant awarded only 48% of the work of Rs.3,39,88,000 amounting to Rs.1,52,94,235, by letter dated 5.11.84. Part I of the work was upto Rs.94,34,323 and Part II was upto Rs.94,34,323. Subsequently, letter of intent was issued on 5/6.11.84 and then a work order was issued on 22.1.85. The said

letter dated 22.1.85 of the appellant contained the + 25% clause which permitted rates higher than the contract rates to be paid, as an exception. It stated as follows:

"The contract price has been arrived at on the basis of your quoted rates in your tender and the enclosed schedule of quantities, your quoted rates shall hold good for a variation of+25% (plus/minus twenty five percent) of the contract price stated in this work order, beyond which your quoted rates will be suitably revised subject to mutual agreement."

It appears the site was not made available on time and there were lot of disputes between the parties. There was correspondence between the appellant and respondent. The appellant varied the works both upwards and downwards. As, according to the contractor, the sum total of variations went above 25% of the contract value, the contractor asked for higher rates in his letters dated 20.11.86, 8.12.86 and 9.12.86. The final bill was submitted by the contractor on 9.12.86 for Rs.85,98,705 as detailed in the Annexure A thereto.

This plea for extra rates was rejected on 31.1.286 by the appellant stating that the + 25% clause applied to the overall net increase. The letter stated:

".....no enhancement is justified unless the total contract value of the work has increased or decreased by 25%. Enhancement of rates is therefore not on account of any increase or decrease in the quantity of individual items.....on completion of the entire work, it is expected that there will not be any variation in the contract value within the limits of + 25%."

The letter also blamed the contractor for delay in the work.

It is not denied that the original date of

completion was 30.6.86 and was extended upto 30.10.86. The total value of work done upto 30.10.86, according to the appellant, was Rs.1,01,84,968.58. According to the appellant, the Contractor abandoned the work in November, 1986. According to the contractor, the appellant committed breach. Another contractor was appointed by the appellant for the balance work and in fact, a cross claim for compensation for Rs.7.64 lakhs was raised against the respondent.

On 26.12.86, the respondent claimed reference to arbitration. By consent, the District Court appointed Sri Dharwadkar, Ex. General Manager, Northern Railway, as sole arbitrator. It was stated that he was also connected with the appellant. He entered on the reference on 22.1.88. The arbitrator in his award accepted the plea of the contractor for higher rates upto the extended date. On the disputed claim No.4 he held as follows:

Payment of final bill, 50% of the revised including extra rates amount awarded. for increase & decrease Balance escalation in the quantities at on the original Rs.80,08,000(approx.) rate only may be Revised on 17.6.1986 as allowed upto Rs.70,98,852.67 30.10.86

In other words, the arbitrator awarded 50% of Rs.70,98,852.67 towards increase in rates. So far as the cross claim by the appellant for compensation for delay, the arbitrator negatived the same. That would mean that the breach was not by the contractor.

The appellant filed an appeal before the District Court for setting aside the award. (No appeal was

preferred so far as the rejection of the cross-claim)

The District Court, as already stated, set aside the award on the ground that the reference itself was bad. But, it gave alternative findings on merits. It held that, as the award was not a reasoned award, but was one made on consideration of all documents, the NIT, the tender papers, the offer, the acceptance and correspondence, it was not permissible to probe into the mind of the arbitrator. The District Court referred to Madan Lal vs. Hukum Chand [1967 (1) SCR 106], Hindustan Steel Works vs. Rajeswar Rao [1987 (4) SCC 93] and held that the award was not liable to be set aside on merits.

The District Court also found (para 38) that the value of variations in the work, both upwards and downwards exceeded 25% and was in fact more than 100%. It said:

"Because of modifications in quantities of items of work, which the respondent required the applicant to execute, the deviation difference was more than 100%, what to talk about 25%. Therefore, the arbitrator has not misconducted in awarding 50% of the claimed amount."

It is necessary to explain what the Arbitrator meant by 'Balance of escalation'. As pointed by the respondent in his counter filed in this Court, it appears that 75% of the escalation was released by the appellant and the balance 25% was not paid on the ground that the appellant slowed down. While the matter was pending before the arbitrator, the appellant prepared a final bill and the balance 25% was also allowed but only upto 30.11.85. The balance escalation was not allowed

upto 30.10.86, on the ground that the delay was attributable to the contractor. It was this balance that was allowed upto 50% by the arbitrator. (These facts are clear from the reply of the appellant on 18.3.88 filed before the arbitrator).

The High Court, as already stated, held that the reference was maintainable and it set aside the judgment of the learned District Judge and directed the award be made a Rule of Court.

In this appeal, it was contended by the learned senior counsel for the appellant Sri Bhaskar P.Gupta that the arbitrator acted without jurisdiction in granting extra amount or higher rates for the work done upto the extended date 30.10.86. This was prohibited by several clauses of the NIT, Special and general conditions and under annexure R attached to the work order dated 22.1.85. The variation limit of plus/minus 25% of the contract price was applicable on the 'total contract price' and not on any individual quantities or items. Any revision of rates would be permissible only after the total contract price stood increased or decreased beyond 25% on actual execution and completion of the contract project. In any event, the arbitrator could not have allowed a uniform increase of 50% for all items.

On the other hand, Sri S.Ganesh, learned counsel

for the respondent-contractor contended that the question was not one of increase or decrease in total contract value. If the sum total of the variations i.e. both plus and minus exceeded 25%, the contract rates were no longer binding and market rates had to be paid.

The learned District Judge had found, as a fact, that the sum total of the additions and deletions in the work exceeded 100%. A tabular statement in this behalf was also filed before us to show that the total variation, both upward and downwards in the work was of a value of more than 25% of the contract price, and in fact it was more than 100%.

On the above contentions, the following points arise for consideration.

(1) Whether, in view of the various clauses in the NIT, special and general conditions, schedules and Annexure R, the arbitrator acted without jurisdiction in revising the rates and in ignoring the contract rates which were to be "firm" upto date of extension of the contract?

(2) Whether, the case fell within the exception of escalation of "+25% of contract price". If so what was the meaning of that clause? Did it mean the overall net increase in contract price after deducting the value of the reduction in work from the value of the additional items of work (as contended by the appellant) or did it

mean that the plus and minus variations had to be added or pooled together (as contended by the contractor) to find out if they were together above 25% of the contract price?

(3) Was the arbitrator wrong in granting 50% out of the escalation claimed by the respondent?

Points 1 and 2:

It is true that there are various conditions in the NIT, the Tender Form and the Special and General Conditions that no extra amount or higher rates will be allowed under any circumstances whatsoever. These have been strongly relied upon by the appellant. We shall refer to them.

The Notice inviting tender (NIT) is dated 24.7.84. The instructions to the tenderer require 4 envelopes to be submitted. Envelope 1 related to earnest money deposit, envelope 2 to contain tenderer's conditions, envelope 3 to contain tender documents as filed. After envelopes 1 to 3 were opened and discussions were over, envelope 4 which contained papers relating to resultant modification, were opened. The Tender Form contained an undertaking to be signed by the contractor that he had seen the NIT, the instructions and the special conditions, the particular specifications and the general conditions of contract Schedules A, B and E and the drawings. Schedule A contained the rates of work

fixed by the appellant and Schedule E contained the time

stipulations. It also stated in para 11 which referred

to deviations/variations as follows:

"Para 11: Maximum limit +(plus/minus) 25 of deviation/ (twenty five) per- variation cent of the contract value"

That meant that the appellant's officers could entrust

work upto the said variations and the contractor would

have to execute the same without any extra payment or

higher rate.

In the Special conditions, it was stated in para

1.4 that the rates quoted would remain "firm" throughout

the pendency of contract; including the extended period

and "shall not be subject to any sort of escalation"

even if labour costs, material or petroleum oil and

lubricant (P.O.L.) prices increased. The rates were to

be quoted by the tenderer to the approximate Bill of

quantity. Para 4 dealt with 'additional works and

states that', if required, the contractor was to execute

works to the extent of an extra 25%. "No adjustment of

rates shall be made for the additional work ordered upto

this limit. Terms and conditions of the contract remain

unaltered.

The General Conditions of the contract defined

'contract value' in clause 3(e) to mean, in the case of

item rate contracts, the cost of works arrived at after

execution of the quantities shown in the schedule of quantities of the items rates quoted by the tenderer for variations. Para 11 of the general condition also required additional work to be carried and it permitted "alterations, omissions, additions" to the work, at the same price as agreed. Schedule A to the general conditions stated in para 1.00.02 that

"The total quantities of work may vary upto + 20% (later amended as 25%) on either side and nothing extra will be paid on this account."

Para 1.00.05 also stated that the quantities in the schedule were approximate and nothing extra would be paid above the quoted rates if there was any increase or decrease in quantities.

It will be noticed that the above clauses permitted increase or decrease in the work upto 25% of the contract price. As to what should happen if the value of the variations exceeded 25% of the contract price was stated in Annexure R attached to the letter of the appellant dated 22.1.85 by which the general and special conditions were modified. This clause in Annexure R has already been extracted and it permitted higher rates to be paid if the "variation is + 25% (plus/minus, twenty five percent) of the contract price".

The question therefore is as to what is the meaning of this clause. The arbitrator, as already stated, granted 50% of the extra rates obviously on the

basis that the case fell within the above exception. The District Court found that the total variations - both plus and minus - exceeded 100%.

The contention of the appellant is that the above exception is applicable only to the net difference between the increases and decreases and if it works out to more than 25% of the contract value, then rates can be revised. For example if the contract value is Rs. 50 lakhs, the increases are of a value of Rs. 15 lakhs and the reductions are of a value of Rs. 10 lakhs, the net difference according to the appellant, in the overall contract value is only Rs. 5 lakhs and being 10% of Rs. 50 lakhs, there can be no escalation in rates.

On the other hand, the respondent contends that one has to add up the total variations both plus and minus and hence, in the above example, the value of total variation, both plus and minus amounts to Rs.25 lakhs which works out to more than 25% ( in fact 50%) of the contract price and the enhanced rates will be applicable.

In our opinion, the construction put on this escalation clause by the learned counsel for the respondents, Sri S. Ganesh is the proper one. On that basis, this case would come within the exception and there was no error of jurisdiction on the part of the arbitrator.

The point raises certain important issues concerning integrity of the contract. The concept of

variation of the question of work is no doubt a common feature of works contracts. This is because in contracts relating to major works, the estimates of work at the time the tenders are invited can only be approximate. But, it was also realised that the power of the employer to vary the terms relating to the quantum of work cannot be unlimited. In Hudson's Building and Engineering Contracts (8th Ed.) (pp.294-296) it has been pointed out that this power

"although unlimited, is in fact limited to ordering extras upto a certain value."

McCardie, J. in Naylor, Benson & Co. vs. Krarinische Industrie Gessellschaft [1918 (1) KB 331] said that the words "even though general, must be limited to circumstances within the contemplation of the parties".

In Parkinson (Sir Lindsay) & Co. Ltd. vs. Commissioners of Works and Public Buildings [1949 (2) KB 632], Asquith, LJ. stated (at p.682) that the words enabling the employer to add extra work, though wide, have to be limited for otherwise it would amount to 'placing one party so completely at the mercy of the other'. Singleton, LJ. observed (p.673) that, to confer an unbridled power on the employer to vary the quantities of work would lead "to manifest absurdity and injustice as stated by Mathew, J. in Bush vs. Whitehaven Town & Harbour Trustees (I) (1888) 52 J.P. 392.

We may also state that under the general law of

Contracts, once the contract is entered into, any clause

giving absolute power to one party to override or modify

the terms of the contract at his sweet will or to cancel

the contract -even if the opposite party is not in

breach, - will amount to interfering with the integrity

of the contract (Per Rajamanner, CJ. in Maddali Thathiah

vs. Union of India AIR 1957 Mad.82). On appeal to this

Court, in that case, in Union of India vs. Maddali

Thathiah [ 1964(3) SCR 61 =AIR 1966 SC 1724] the

conclusion was upheld on other grounds. The said

judgment of the Madras High Court was considered again

in Central Bank of India Vs. H.F. Insurance Co. ( AIR

1965 SC 1288) but the principle enunciated by Rajamanner

CJ was not differed from. (See the discussion on this

aspect in Mulla's Contract Act, (10th Ed.) PP.371-372,

under Section 31 of the Indian Contract Act.)

There is thus good reason as to why, in modern

works contract, a limitation upto 20% (now 25%) has been

put on this power of alteration, both plus and minus.

(See Gajaria's Law Relating to Building and Engineering

Contracts in India, 3rd Ed., pp.410-412). Such a

limitation upto 20% or 25% is now imposed under clause

12A of the Standard Terms of CPWD Contracts.

These aspects were discussed in detail in

S.Harcharan Singh vs. Union of India [1990 (4) SCC 647]

by a three Judge Bench of this Court. That judgment

is

very much relevant to the present case both on principle

and on facts. It was held by S.C.Aggarwal, J. speaking

for the Court that the arbitrator could award higher

rates on the analogy of clause 12 A of CPWD contracts

for excess variations beyond 20%. The contract rate was

Rs.129 per thousand cft plus 2% but the contractor

claimed at Rs.200 per cubic ft in respect of the excess

over 20% extras. The arbitrator upheld part of the

enhancement claimed and that was upheld by this Court.

Clause 12A of the CPWD contract which permits

variations upto 20% again come up for consideration

recently in Himachal Pradesh State Electricity Board vs.

R.J.Shah & Co. [1999 (4) SCC 214]. In that case, the

arbitrator gave a non-speaking award on disputes 1, 2

and 4. Dispute 1 related to revision of rates. Dispute

2 was whether the quantities were payable at the

deviated rates, where quantities of individual items

exceeded the deviation limit. Dispute 4 was as to

whether the quantities to be considered for the purpose

of deviation limit. Under clause 3(2)(e) (ii)

deviations upto 20% were liable to be carried without

any extra. The contention of the department was that

the contract was an items rate contract and that it was

only those items which crossed the deviation limit that

were to be paid at revised rates. The rate for work in

excess of the deviation limit was to be fixed only as

per clause 12A. It was contended for the Board that the arbitrators acted beyond their jurisdiction and could not have revised the rates of items merely because the overall value of the contract which was executed exceeded 20%. On the other hand, it was contended for the contractor that the claim as to revised rates must be deemed to have been specifically referred to the arbitrator, the arbitration clause being wide, and that the construction put on the 20% clause by the arbitrator could not be held to be vitiated by any error apparent on the face of the word. Kirpal, J. after referring to a number of judgments dealing with the power of the arbitrator to interpret the terms of the contract, - including Hindustan Construction Co. Ltd. vs. State of J&K [1992 (4) SCC 217], K.R.Ravendranathan vs. State of Kerala [1998 (9) SCC 410],-held that the grant by the arbitrator at a rate higher than the contract rate could not be treated as outside his jurisdiction. It was observed:

"The construction placed on the contract by the contractor cannot be said to be an implausible one. Even if the arbitrators considered the terms of the contract incorrectly, it cannot be said that the award was in excess of jurisdiction."

It was, however, contended before us for the appellant that by a wrong construction of the clause permitting revised rates as stated in Annexure R, the arbitrator could not have clutched at jurisdiction he did not have. The question then is whether the arbitrator clutched at jurisdiction he did not have, by

an unreasonable construction of the clause "+ (25%)" for purposes of escalation.

We are of the view that the abovesaid clause "+25%" was understood by the arbitrator in a reasonable manner as being applicable to a case where the value of the sum total of the additions and deletions exceeded 25% of the contract price. That construction, in our view, cannot be said to be vitiated by any serious error of law. The following are our reasons.

When a contractor bids in a contract, he has to offer reasonable rates for the works which are both difficult to perform and other works which are not that difficult to perform. Every contractor tries to balance his rates in such a manner that the employer may consider his offer reasonable. In that process the contractor tries to get a reasonable margin of profit by balancing the more difficult (and less profitable items) and the less difficult (and more profitable items). His bid is, normally, a package. If the employer is permitted in law to make variations upwards and downwards - even if it be upto a limit beyond which market rates become payable - then the interpretation of the clause must be one which balances the rights of both parties. For example, if the plus and minus variations go beyond 25% and are made in a manner increasing the less profitable items and decreasing the more

profitable

items, and if the net result of the contract is to be the basis, as contended by the appellant, then it may work out that the contractor could be made to perform a substantially new contract on the same contracted rates.

In fact, if the said reasoning of the appellant is accepted and if, in a given case, the value of the increases in unprofitable items is 50% of the contract value and the value of the reductions of the remaining more profitable items is 50% of the contract value, it could still be contended for the appellant that the net variation was nil, even though that was a situation where the contract had been substantially modified and was almost a different contract from the one stipulated.

Such an unreasonable construction is to be avoided and was rightly avoided by the arbitrator.

The additions and decreases in work are, in our opinion, therefore both independent for the purpose of finding out the + 25% variation and have to be pooled together. The arbitrator was right in thinking that the case fell within the exception. Obviously, he must have felt that the plus and minus variations are more than 25% and that the contract rates are no longer binding. His construction of the clause appears to be rational and just and cannot be said to be unreasonable.

In the result, the interpretation put on the clause by the arbitrator appears to us to be quite reasonable and very plausible and it cannot therefore

be

said that the award is vitiated by any error of law affecting his jurisdiction. In fact, the learned District Judge found that the total variation - both upwards and downwards was more than 100% of the contract price. For the aforesaid reasons, we are of the view that Points 1 and 2 should be answered in favour of the respondent-contractor.

Point 3:

This concerns the question whether the arbitrator could have awarded at a flat rate of 50% of the extra claim or at 50% of the difference between the market prices and the contract rates. Both on law and on facts, the case of the appellant cannot be accepted.

There is material on record that the appellant had, during the pendency of the arbitration proceedings, not seriously disputed that market rates were payable because the plus and minus variations exceeded 25% of the contract price. As pointed out in the respondent's counter filed in this Court, the appellant had, in a reply dated 18.3.88 filed before the arbitrator conceded having paid 75% of the additional work at the revised rates though not upto the extended date. Now the award by the arbitrator was for the 'balance' and upto 30.10.86. That is also an indication that, on facts, the arbitrator's construction of the "+ 25%" clause was correct.

In the appellant's defence to the respondent's claim before the arbitrator, there was no specific denial of the contractor's right to the market rates. The appellant was relying more on its general plea that the + 25% clause was not attracted at all as the contract value as a whole or the net increase was to be taken into consideration. In fact, there were favourable recommendations of the departmental officers for payment at higher rates. In S.Harcharan Singh's case to which we have referred earlier, there were similar recommendations of the officers. The arbitrator cannot, therefore, be said to have acted illegally on facts for he has not in fact granted at the full market rate claimed by the contractor but has only granted at 50% of the claim.

In law also, the appellant has no case. In the case of a non-speaking award, it is not permissible for the Court to probe into the mental process of the arbitrator [ See Hindustan Steel Works Vs. Rajeswar Rao ( 1987(4) SCC 93)] when he rejected 50% of the claim in favour of the appellant and accepted 50% of the claim in favour of the contractor. In two decided cases of non-speaking awards when a flat increase of 20% or 25% for permissible items of additional work was granted by the arbitrator, this Court accepted the same as not being illegal. See P.M.Paul vs. Union of India [1989 Suppl.

(1) SCC 368] and Himachal Pradesh Nagar Vikas Pradhikaran vs. M/s Aggarwal & Co. [AIR 1997 SC 1027].

Therefore, merely because the increase was at a flat rate, we cannot find fault with the award. The arbitrator was appointed by consent and he was a former General Manager in the Railways and was also associated with the appellant corporation. We do not therefore find any error apparent on the face of the record in the award of 50% of the escalation claimed and in the claim upto the extended date, 30.10.86.

For the aforesaid reasons, the appeal is dismissed. The interim orders passed by this Court stand vacated. No costs.