

State of Karnataka and Another Vs. R.N. Shetty and Co., Engineers and Contractors

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Court : Karnataka

Decided On : Jan-19-1990

Reported in : AIR1991Kant96; ILR1990KAR1309; 1990(1)KarLJ286

Judge : M. Rama Jois and;S. Rajendra Basu, JJ.

Acts : [Arbitration Act, 1940](#) - Sections 29 and 30; Interest Act, 1979 - Sections 3; [Code of Civil Procedure \(CPC\), 1908](#) - Sections 34

Appeal No. : M.F.A. No. 2478 of 1988 with Cross-objections

Appellant : State of Karnataka and Another

Respondent : R.N. Shetty and Co., Engineers and Contractors

Advocate for Def. : P. Vishwanatha Shetty, Adv.

Advocate for Pet/Ap. : Chandrasekharaiah, Govt. Pleader

Judgement :

ORDER

Rajendra Babu, J.

1. This appeal is filed under Section 39(1) of the Arbitration Act questioning the legality and correctness of the judgment and decree dated 18-4-1987 made by the learned Civil Judge, Yadgir, in Misc. No. 2/1987, on his file, making award Rule of the Court.

2. The essential facts, in brief, are as follow :

The construction work in repeat of Upper Krishan Project Narayanapur Left Bank Canal Reach No. 1 from Km 35.5 to Km 41 excluding Rajankollur Tunnel from Ch. 26.231 to 39.834, was granted to the respondent under an agreement dated 7-1-1980. The value of the contract was fixed at Rs. 115.12 lakhs with increases by 3.22 per cent above the estimated cost. The agreement dated 7-1-1980 stipulated that the contract was to be executed within thirty months fixing the date of completion of the contract on 23-7-1982. Disputes arose between the contractors and the appellants during the progress of the work which could not be settled between them. Clauses 71 and 72 of the agreement provided that in the event of disputes the matters in dispute could be arbitrated in the manner provided therein. Consequently, a panel of three arbitrators was appointed to go into the dispute.

3. Before the arbitrators the contractors filed their statement of claims and the appellants filed their counter statement. Neither party adduced any oral evidence, but wholly relied on documentary evidence. The arbitrators concluded the proceedings by making an award which was filed into Court and a decree in terms thereof was made by the Court. Before the trial Court the appellants raised several objections. The trial Court, however, did not find any substance in any of the objections, overruled them and made a decree in terms of the award. Aggrieved by the said award as affirmed by the decree of the civil Court the appellants have approached this Court in this appeal.

4. The appellant's grievance is confined to three claims of the contractors, which are as follows:

(i) Payment for excavation in over breakages and filling in cement concrete or uncoursed rubble masonry;

(ii) Payment of compensation for damages in respect of tendered items executed after the expiry of the original contract period; and

(iii) The award of interest made by the arbitrators.

5. The learned counsel for the appellants contended that there are errors apparent on the face of the record in that the conclusions reached by the arbitrators in regard to items referred to above are wholly unjustified and submitted that the arbitrators could not have granted claim No. 1 regarding excavation in over breakages and filling in cement concrete or uncoursed rubble masonry. Further, placing reliance on Clause 39 of the contract agreement which provides for satisfaction of the contractors regarding infrastructure and data of works and conditions of the work site, it was also submitted that no payment could have been made towards over breakages. Secondly, he contended that the arbitrators and the Court below could not have granted any compensation by way of damages for the work done in the extended period of contract. According to the learned counsel, what the arbitrators at best could have done is to award damages only at the rate as provided under Clauses 19A and 67 of the contract dated 7-1-1980. Lastly, the learned Government Advocate relying on decisions of the Supreme Court in Food Corporation of India v. M/s. Surendra Devendra and Mohendra Transport Co., : [1988]2SCR329 , Executive Engineer, Irrigation v. Abhaduta Jena, : [1988]1SCR253 . State of Orissa v. Construction India, : [1988]2SCR145 and State of Orissa v. Dandasi Sahu, : AIR 1988 SC1791 submitted that the arbitrators could not grant interest for period between commencement of reference and date of award or future interest.

6. The learned counsel for the respondent, per contra, submitted that :

(i) any enquiry into a matter of this nature falling u/s. 39 of the Indian [Arbitration Act, 1940](#) (hereinafter referred to as the Act) is very limited in that when once the parties enter into an arbitration of the dispute between them, the arbitrators decision is final and binding and it is not at all permissible for this Court sitting in appeal against a decree affirming that award to interfere with the same;

(ii) all matters that were referred for arbitration fell within the jurisdiction of the arbitrators and hence were free to exercise their jurisdiction in determining the damages in going Clause 19A of the contract;

(iii) Clause 19A is only a price adjustment clause and does not provide for damages for work done when there is breach of contract;

(iv) Clause 67 of the contract merely provides for saving the contract in case the work could not be done or commenced before the period stipulated in the contract and in case of extension of time there is no provision under the contract prohibiting claim for damages;

(v) in case where two opinions are possible in relation to whether there is breach of contract or not and if so at what rate the damages should be awarded, the opinion of the arbitrators should prevail; and

(vi) the award for over breakages and pen-dente life interest is validly made.

7. Before adverting to the various other contentions urged in this appeal, it is important to refer to the basic contention raised by the learned counsel for the respondent. The learned counsel for the respondent submitted that Clause 17 of the agreement in the present case provided for arbitration on all matters of claims and disputes and a reference having been made on disputes between the parties to the arbitration the decision of the arbitrators on such specific questions being final it is not open to the appellants to attack the award in these proceedings and backed up this argument with the decision of the Supreme Court in *Tarapore and Co. v. Cochin Shipyard Ltd.*, : [1984]3SCR118 .

8. In the decision referred to and relied upon by the learned counsel for the respondent, the points of dispute were specifically referred to the sole arbitrator and in that background the Supreme Court held that the parties having agreed to refer a specific question including the question as to whether the dispute raised was covered by the arbitration agreement, it becomes a specific question even if it involves the jurisdiction of the arbitrator and if it is so, a decision of the arbitrator on a specific question referred to him, even if it appears to be erroneous to the

Court, is binding on the parties. If a question of law is specifically referred and it becomes evident that the parties desire to have a decision on that specific question from the arbitrator rather than from the Court, the Court will not interfere with the award of the arbitrator on that question on the ground that there is an error of law apparent on the face of the record even if the view taken by the arbitrator does not accord with the view of the Court. However, the position is different in matters where disputes are generally referred to the arbitrator without specifying any question of law or fact and in such a case it is certainly open to the Court to find out whether the arbitrator had committed any error of law apparent on the face of the record.

9. The legal aspect of the matter has been pithily and succinctly summed up in Russell on Arbitration, 19th Edition, at page 441 thus:

'It is necessary here to distinguish cases in which a question of law is specifically referred, and cases in which a question of law merely arises (though necessarily so) in the course of a reference. The question is whether what is referred to the arbitrator is 'the general question, whether involving fact or law' or 'only some specific question of law in express terms as the separate question submitted, or in other words whether there is 'a reference in which the questions of construction arise as being material in the decision of the matter which has been referred to arbitration' or 'a reference in which a specific question of law was referred to the decision of the arbitrator as the sole tribunal. Only in the latter case will an apparent error in law be left unquestioned.' (underlining by us)

This position in law was restated by the Supreme Court in *Thawardas Pherumal v. Union of India*, : [1955]2SCR48 and again in *M/s. Alopri Prashad and Sons Ltd. v. Union of India*, : [1960]2SCR793 . Indeed, the matter was elaborately dealt with by the Supreme Court in *Union of India v. A. R. Rallia Ram*, : [1964]3SCR164 and the law on the point was again reiterated thus :

'Where the parties agreed as to particular issues which arise for decision in a dispute, they cannot be regarded as specifically referred to the arbitrator. The only permissible inference in such cases is that the parties agreed to have the dispute adjudicated on the issues raised, and not to submit the issues raised for

adjudication. Whether a question of law has been specifically referred to arbitration falls to be determined in each case on the terms of the particular submission. Ordinarily, the arbitration agreement would initially be in general terms, but actual reference would arise only after disputes crop up, which may comprise either specific questions of fact or law.'

10. In this case we have waded through the mass of material in the shape of pleadings and other documents placed before the arbitrators to ascertain whether specific questions of law as such had been referred to them or such questions of law arose incidentally as material in the decision of the dispute referred was in general terms. We could not discern any such specific question of reference on any question of law or fact on the material on record but, on the other hand, dispute has been referred in general terms. Therefore, the contention raised by the learned counsel for the respondent-contractors has no basis at all and the same is rejected.

11. The pleadings on the first claim relate to payment of excavation in over breakages and filling in cement concrete, which is in a sum of Rs. 23,04,775 with escalation charges. The contractors contended that due to adverse geological strata there had been over-breakages in excess of the specified limits and therefore these charges for over breakages and consequent filling with masonry or concrete had to be paid to them. They claimed that over breakages occurred in spite of due care and caution exercised by them. This claim has reference to the excavation item 1(b) and according to the specifications in para 1.8.6 payment for over breakages was permissible up to a maximum of 5 cms., limited to an average of 2.5 cms. They contended that extra overbreakage was apparent on a perusal of the actual measurements. In support of their contention the contractors relied upon clause 1.8.6 at page 79 of the agreement which is to the effect that the excavation done in excess of the specified limit either due to inadvertence of the contractors or due to their convenience shall not be measured and paid for and the contractor shall fill up the extra excavation at his own cost. They further contended that the excavation in this case was not due to any inadvertence on their part or for their convenience, but only due to adverse geological conditions not visualised at the time of estimation of work, which was beyond their control. In this regard they also

relied upon a report of the Geologist which stated that there was likelihood of breaking more than what is required according to approved cross sections of the canal. The contractors further contended that the work had been carried out under the very nose of the departmental officers and the claim as such had never been rejected, but on the other hand they recorded the measurements of the extra excavation done and consequent filling. This conduct, the contractors contend, is suggestive of acceptance of the claim but postponing fixation of rates to a later date. As regards the rates the claimants contended that most of the work having been done beyond the agreed date they are eligible for compensation in the shape of workable rates at the time of the execution of the work of various items in question and they pleaded for the acceptance of the rate analysis on the items of over breakages, masonry and the items of filling. The contractors contended further that the D.S. R. rates cannot be blindly applied, as such rates are not realistic and therefore they should be paid at the rate analysis filed by them. The appellant State contended, on the other hand, that the contractors themselves should be blamed for the extra breakages and they should have taken the necessary precautions after studying the nature of the soil strata. They also contested the correctness of the report given by the Geologist. Merely because the measurements were recorded that cannot by itself be taken as the acceptance of the work for the purpose of payment. They also further submitted that even if the contention raised by them on the merits of the matter is rejected, the rates that could be allowed to the contractors for the work done by them under this claim should be allowed on reasonable basis and that was only as per the D.S.R. rates and not as claimed by the contractors. They further pointed out that Clause 19A of the agreement and the clause at 1.8.6 at page 79 of the contract bars payment in regard to extra excavations. Therefore, in their opinion, the contractors were eligible for relief in respect of the increase in price only under Clause 19 A of the agreement. They also submitted that the claimants are presumed to be aware of the local conditions of the site before collecting rates for the work. Since the controversy revolves round the interpretation of Clause 1.8.6 we extract the same :

'1.8.6. Payment for excavation in soil shall be limited to the prescribed canal section plus 7.5 cm. cutting for lining. In the case of excavation of medium rock

and hard rock, the payment for overbreak or rock beyond the seating of bed and side lining will be limited to a maximum depth of 5 em. limited to an average of 2.5 cm. Excavation done in excess of the above, either due to inadvertence of the contract or or due to his convenience shall not be measured and paid for and contractor shall fill up the extra excavation at his own cost as specified in items 13 to 16 of schedule 'B' Part I and as directed by the Executive Engineer.'

What the above specifications provide is that the contractor would not be entitled for payment for extra breakages and their filling beyond the stipulated average depth of 2.5 cms. if the extra breakages are due either to inadvertence or carried out for the convenience of the contractor. The arbitrators found that the claim has been put in by the contractors in June, 19S1 while the work had commenced in January, 1980 and the departmental officers inspected the work on various occasions when the over breakages werebrought to their notice. The claim had not been rejected till the dispute was brought before the arbitrators. At no stage the department had informed that the over breakages in excavation was due to the inadvertence on the part of the contractors, but on the other hand they informed that the claim was under consideration of the department, even as late as 17-4-1985 when the Superintending Engineer held a meeting to decide the case. Again the Chief Engineer also inspected the work on 9-5-1984 and instructed the Superintending Engineer to regulate the payment of over breakages as per terms and conditions of the agreement. Therefore, they concluded that while the work was in progress all along at no time did the department warn or charge the contractors that they were not resorting to proper methods of blasting in the manner so as not to cause over breakages or that they had been careless or indiscriminate in blasting which resulted in breakages. Therefore, they concluded that the question of inadvertence or convenience never arose during the progress of the work and there was tacit acceptance of the respondent over the breakages. In fact the arbitrators were surprised at the stand of the department in refuting to stand by the report of the Geologist who was an officer of the Government and if for any reason the report was unacceptable for them they were in duty bound to inform the claimants within a reasonable time that their claim was untenable. The arbitrators held that Clause 39 of the agreement which requires the contractors to acquaint themselves of the site conditions before taking up the work does not

militate against their claim and that has no relevance at all to the issue. They also held that recording of the measurements in the measurements book was not merely for the purpose of accounts, but on the other hand discloses the tacit acceptance of the claim of the contractors. In the circumstances, they held that the over breakages occurred due to the peculiar geological strata and therefore rejected the contentions of the appellants and admitted the claim of the contractors. This discussion discloses that no error apparent on the face of the record can be spelt out inasmuch as the arbitrators have specifically referred to each one of the contentions of the appellants and the contractors and have considered the same with reference to the relevant clause and on examination of the facts arrived at the conclusion. Therefore, this aspect of the award cannot at all be attacked. At what rate the work should be paid also has been considered by them and that is dependent on their conclusion that the work could not be completed within the stipulated time. For reasons to be stated hereinafter we hold that the extension of time does not release the appellants from damages for breach of contract by delay caused by them and thereafter the rate analysis supplied by the contractors and accepted by the arbitrators should be adopted as the basis. Therefore the contractors would be entitled to the rates awarded by the arbitrators and hence on this ground also the appellants cannot assail the award.

12. So far as the second contention is concerned, the claim arises in the following circumstances. The contractors contended that they were entitled to compensation for damages in respect of tendered items after the expiry of the original contract period by 23-7-1980 and relates to (1) excavation in medium rock; (2) extra load charges for conveying materials up to 1.5 km. load; (3) C. C. lining in M.100, 11.5 cm. thick for bed and side slopes of the canal; (4) random rubble masonry in CM 1:5 for templates and steps and (5) C.C. M. 100 for piers, abutments and wing walls etc. The contractors contended that the claim has arisen as a result of the breach of conditions on the part of the appellants inasmuch as the due date of completion had been extended up to 31-3-1985. The stipulated period of contract of 30 months had been extended by another 33 months and the tendered items had to be executed after 23-7-1982 on account of delays and defaults on the part of the appellants. They therefore claimed damages in the shape of workable rates as on 23-7-1982, that is, the date of completion as per agreement plus escalation

charges as per clause 19-A of the contract agreement considering the base Index T from the quarter commencing from 1-7-1982. They filed a rate analysis report before the arbitrators in support of their claim. The appellants contended that there was little or no delay on their part and no damages could be claimed in the circumstances. They further contended that (1) there is no power granted to the arbitrators under the contract to fix enhanced rates for the tendered items; (2) the claim itself being one based upon the rise in the market price for labour and materials fell outside the contract and as such is not arbitrable; (3) the procedure prescribed under Clause 49 of the agreement is only for the purpose of determination of rates for supplemental or extra items and not tendered items. When the specific procedure laid down in Clause 49(iii) has not been followed by the parties the arbitrators had no jurisdiction to adjudicate the claim on that basis. The arbitrators recorded a finding that there was delay in the execution of the work which was on account of non-fulfillment of the contract conditions for which the appellants were responsible and there were substantial changes in the working conditions and therefore the appellants were liable to pay damages/ compensation towards the quantities of items that remained incomplete on the stipulated date of completion namely 23-7-1982 and had to be completed thereafter. The arbitrators held that they have power to grant damages under the provisions of the Contract Act notwithstanding the terms of the contract and it was stated that this position was accepted by the appellants themselves. The arbitrators found that the claim of the contractors were justified and awarded damages calculated on the basis of prevailing rates of labour, machinery, spares and P.O.L. 30 months after the commencement of the work, that is, during the extended period of execution of the items in question. They also held that the claim made is not outside the contract. They proceeded on the basis that the tendered rates were not relevant for the work executed beyond the targeted date of completion of contract, that is, during the extended period and the question of deriving the rates from the tendered rates did not arise. In regard to items of work executed which do not correspond with any item in the agreement they held that the contractors were entitled to a mutually agreed rate after they undertook to carry out the same which cannot be anything other than equitable rate and such rate will not be accurate unless it is an equitable one which implies a fair rate prevailing on market price basis. They

concluded that the contractors had made claims for equitable rates for extra items and the appellants had not insisted upon compliance with Clause 49(ii) of the agreement and therefore it was not open to contend to the contrary. They also drew an inference that the appellants themselves offered rates for extra items based on schedule rates of the year of opening the tender, that is, 14% overhead charges and escalation which they considered as equitable and in the absence of any relevant data referred to in Clause 49(ii) the same could not be applied particularly when the parties had tacitly accepted the principle of payment of equitable rates without insisting on the procedure under Clause 49(ii), and therefore the appellants were estopped from objecting to the payment of damages on the basis of workable rates. They also added to it escalation as provided in Clause 19-A of the agreement. On that basis the arbitrators made an award for recovery of the sums mentioned in the award.

13. The contention raised by the appellants is that the finding recorded by the arbitrators is plainly contrary to law and does not arise out of the contract inasmuch as the delay in handing over the site as such will not result in any breach of contract.

14. The contract in question was entered into on 7-5-1980 and the time limit stipulated was 30 months and the work was to be completed on 23-7-1982. Extension of time to perform the contract was granted under Clause 67 up to 31-3-1985. Therefore, the question that falls for consideration is whether there is any breach of the contract on the part of the appellants. Clause 67 of the agreement reads as follows :

'67. Liquidated Damages :

If the contractor fails to complete the works by the stipulated completion date he shall pay liquidated damages at one tenth of one per cent of contract value of the incomplete parts or reaches of the canal per day of delay in completion and handing over to the department. Delays in excess of 100 days will be the cause for termination of the contract and forfeiture of performance bond (bank guarantee) and other security deposits.

Time shall be considered as the essence of the contract. If, however, the failure of the contractor to complete the work as per the stipulated dates referred to above arises from delays on the part of the Govt. of Karnataka in supplying the materials or equipment, which it has undertaken to supply under the contract, or from delays in handing over sites, an extension of time to enable him to complete work shall be given by the Govt. of Karnataka.'

The first part of the clause provides that if there is any delay or failure on the part of the contractor to complete the works by the stipulated time he is liable to pay liquidated damages at one-tenth of the contract value and that delays in excess of 100 days would entitle the appellants to terminate the contract, forfeit the security deposit and the performance bond. The last clause is the most important for our purpose because the first two parts of the clause do not arise for consideration in this case and there is no allegation in this case that there has been a failure on the part of the contractor in completing the work within the stipulated time. The last part of the clause empowers the appellants to extend the period of contract and to fix a new time schedule as and when the time is extended. If, however, there has been any failure on the part of the appellants in the matter of supplying the materials or equipments, to enable the contractor to complete the work, Clause 53 provides for adjustment of the dates as regards completion of the work. The relevant portion of Clause 53 reads as follows :

'53. Programme of Works

The enclosed net works for all the reaches clearly indicates the programme for the completion of work for the canal which is to be adhered to. The date of commencement of the work will be the date on which the site (or premises) is handed over to the contractor in full or in parts. If for reasons, the sites are not made available on the stated dates, appropriate adjustment will be made in the completion dates. Irrigation department is prepared to consider any programme submitted by the contractor in lieu of the above programme provided the date of completion of work is not extended.'

(underlining by us)

The combined effect of Clause 67 which enables the Government to extend the period of contract and Clause 53 which states that the date of commencement of the contract will be on the date on which the site is handed over to the contractor is that the delay in handing over site though may result in breach of the contract, damages arising therefrom are mitigated by extending the period for performance of the obligation,

15. There is no specific clause in the agreement stipulating at what rates the contractor will have to be paid in the event there is delay in handing over the site, material or equipment. There is no clause in the agreement specifying that in the event the appellants delay in handing over the site or equipment or supplies, any extension of time granted will be in satisfaction of the claim for damages that may be claimed by the contractors.

16. The learned counsel for the contractors relying upon the decision of the Supreme Court in *M/s. Tarapore Company's case* : [1984]3SCR118 submitted that if the rates initially quoted by the contractors became irrelevant due to subsequent price escalation on account of the delay in completion of work because of the lapses on the part of the appellants, the agreement itself having become irrelevant by reason of passage of time, the agreement to that extent would become extinct and in such an event the claim for compensation for excess expenditure incurred due to the price rise could not be turned down just because there was no clause in the agreement regarding price rise. The learned counsel further submitted that a contractor has a claim for damages against the employer for latter's delay and extension of time does not in the absence of express words release such a claim.

The learned State counsel, however, submitted relying upon a decision of the Supreme Court in *Continental Construction Co. Ltd. v. State of M. P.*, : [1988]3SCR103 that the specific price escalation clause in the agreement would bar consideration of the claim made by the contractors and awarding of extra costs as in such an event, the delay in handing over the site would not entitle the contractors to claim such extra costs.

17. The effect of extension of time on damages claimed by the contractors has been exhaustively considered by several authors in several standard text books

and a few of them are Halsbury's Law of England 4th edition, para 1281, Keating on Building Contracts at para 161 and Hudson on Building and Engineering Contracts, 10th edition at page 647, which view is reiterated in Emdon on Building Contracts. All these text books are to the effect that when the time fixed by the contract ceases to be applicable on account of some act or default of the employer, a provision is generally inserted to extend the time. When the power to extend time has been properly exercised, the contractor will be liable to pay liquidated damages. In a true sense and on an examination of the matter in its proper perspective, what comes up for consideration in such a case is the determination of the question as to what are the rates applicable as a result of the extension of time granted and not awarding of damages as such. The enhancement in the rates itself will constitute the damages. When the contract itself does not bar such rates being given and the arbitrators in the case on hand on a consideration of the material on record, have arrived at the rate at which the contractors will be entitled for payment of extension of the contract time because of certain lapse on the part of the appellants and that rate being just and proper one, it cannot be said that the arbitrators have committed any error apparent on the face of the record calling for interference at the hands of this Court.

18. As stated earlier Clauses 67 and 53 provide that the date of commencement of the work will be the date on which the site is handed over to the contractor in full or part. If for any reasons the site is not made available on the stated dates appropriate adjustment will be made in the completion dates. In view of our conclusion on the question that extension of time does not absolve the appellants to pay damages resulting from inordinate delay in handing over the site, unless the contractor had agreed to accept the extension of the stipulated period for completion of the work itself is in satisfaction of his claim for damages. We have to reject the contention advanced on behalf of the appellants in that regard.

19. In the context of understanding the claim for damages against employer's delay and extension of time, it is necessary to examine when the right to damages exists. Claims by a contract or on account of defaults by an employer fall into two classes: (i) where there is a breach by the employer which goes to the root of the contract and the contractor elects not to proceed with the work and (ii) where the

contractor elects to treat the breach partial and continues with the work. In this case it is not the claim by the contractors that there is a breach by the employer which goes to the root of the contract and the contractors did not elect to proceed with the work. What we are concerned is only with the second category of damages. In this category when the contractor continues with work the most usual circumstance which gives rise to claims for damages is delay in giving possession of the site or supply of raw materials or suspension of work caused by the omission of the employer and consequent increase in the performance of the work and the contractor may be able to recover damages for delay caused by the employer notwithstanding such extension of time has been granted for such delay. But the learned Government Advocate contended that in cases where these damages are worked out, the liquidated damages claimable in respect thereof is in the shape of escalation as provided in the present contract is at Clause 19-A and suggested that proper course to be adopted in such cases is as provided in Clause 19-A which is to grant agreed damages. The learned counsel for appellants relied upon a decision in Metro Electric Company v. Delhi Development Authority. AIR 1980 Delhi 266. In that case the contractor had claimed damages in enhanced rates of 22% over the quoted rates. The Chief Engineer or the authority awarded 18% increase over the quoted rates by way of damages. The Delhi High Court declared that the grant of damages is an error apparent on the face of the record and set aside the grant in respect of that claim in view of a clause which provided for payment of 10% over and above the tendered price of the commodities used during the progress of the work for price of material or labour price. That was within the escalation clause pure and simple. But in the case on hand, what is set forth in Clause 19-A of the agreement is not mere escalation but a price adjustment clause. This is how the clause reads :

'19-A. Price Adjustment : The amounts paid to the contractor for the work done shall be adjusted for increase in the rate of labour and materials excepting those materials supplied by Government as per Schedule A.

Increase or decrease in the cost due to labour shall be calculated quarterly in accordance with the following formula

$$V1 = 0.75 P1/100 * R (i - io)/io$$

V1 = increase or decrease in the cost of work due to the labour during the quarter being adjusted.

R = The value of the work done in rupees during the quarter being adjusted.

io = the average consumer price index for industrial workers (wholesale prices) for the quarter in which the tenders were operated (as published in Karnataka Gazette).

i = the average consumer price index for industrial workers (wholesale prices) for the quarter being adjusted.

P1 = Percentage of labour components (specified in Schedule of the item.

The increase or decrease in cost of materials shall be calculated quarterly in accordance with the following formula

$$Vm = 0.75 Pm/100 * R (I - Io)/ Io$$

Vm = the increase or decrease in the cost of work due to materials during the quarter being adjusted.

R = the value of the work done in rupees during the quarter being adjusted.

Io = the average wholesale price index (all commodities) for the quarter in which tenders were opened (as published in appropriate Government publications).

I = the average wholesale price index (all commodities) for the quarter being adjusted,

Pm= percentage of material commodity (specified in schedule of the item.

Price escalation clause shall be applicable only for the work that is carried out within the stipulated time or extensions thereof as are not attributable to the contractor. No claims for price escalation other than those provided herein, shall be entertained.'

This clause when read with Clause 53 which provides for fixing the date for commencement of the work, states that if the sites are not made available proper adjustments will be made in the completion dates. It is not clear whether in the contract in aforesaid case which came up before the Delhi High Court there was a clause similar to the one with which we are concerned herein. In fact, in that agreement there was a specific clause in 10.C which provided that if during the progress of the work prices of any material or the labour charges increased as a direct result of any law coming into force and such increase exceeded 10% of the price there shall be enhancement in the rates. That was a price escalation clause pure and simple. But in the present case with which we are concerned, it clearly sets out the increase or decrease of the cost of labour which shall be calculated quarterly in accordance with certain formula which takes into consideration the cost of labour during each period and it also makes it clear that the price escalation clause is applicable for the work that is carried out within the stipulated time or extended time which is not attributable to the fault of the contractor.

20. The learned Government Advocate for the appellants submitted that the damages to which the contractor is entitled to, for execution of the tendered item of work after the stipulated period, even on account of the delay in handing over the site, and supply of materials was only by way of extra payments over the tendered rates in accordance with Clause 19-A. But what the arbitrators have done in this case is to grant extra rates over the tendered items as if that was extra work done and also added escalation charges to it virtually amounting to double payment to the contractors.

21. However, the learned counsel for the contractors relied upon an unreported decision of this Court in M.F.A. No. 650/1984, disposed of on 16th January, 1985 and contended that the arbitrators in awarding the amounts covered by Clause 19-A towards escalation did not exceed in their power particularly when the arbitrators had adopted the equitable rates it was open to them to add escalation charges.

In the said decision the contention advanced was that the arbitrators in addition to the sum awarded towards excess and supplemental items awarded another sum under the head escalation charges under clause 19-A and according to the

counsel appearing for the State the arbitrators having determined equitable rates could not have gone further and granted additional sums by way of escalation under Clause 19-A virtually amounting to duplication. This Court in answering this contention held that the total amount awarded did not exceed the amount claimed by the contractors and in fixing the equitable rates adopted pertained to the work executed by the contractors in the years 1979-80, 1980-81 and 1981-82. The arbitrators therein adopted the equitable rates for the various items of work unitwise with reference to the first year 1979-80 which were taken as basal-rates. In respect of excess and supplemental work executed, those rates were applied and no escalation under Cl. 19 A was allowed. But for the years 1980-81 and 1981-82 alone the escalation clause was invoked and applied adopting the rates determined with reference to the basic year 1979-80. According to the concept of 'equitable rates' in respect of excess and supplemental works executed according to the method adopted by them would be equitable rates for the years only if read with escalation clause and that was the method adopted by the arbitrators and if that is properly understood there can be no complaint that there was double payment or duplication in making the payments. In the present case, the method adopted by the arbitrators is as under:

'Item Qnty. executed beyond 23-7-82 Rate applicable as on 23-7-82

(a) Excavation in medium rock 1,27,915 cum. Rs. 37-30 per cum. (b) Conveyance of excavated stuff 1,27,915 cum. Rs. 35-35 per cum. (c) Cement concrete lining in M 100' 11.5 cum. thick for bed and side slopes of the canal. 33,536 sq. m. Rs. 36-72 per sq. meter. (d) Random rubble masonry in CM 1 : 5 for templates and steps 213.90 cum. Rs. 187-60 per cum. (e) Cement concrete M 100 for piers, abutments wing walls etc. 708.387 cum. Rs. 393-70 per cum.'

In para 26-3-1 this is how the arbitrators concluded:--

'The rates as above in respect of the quantities of the items which have been executed after 23-7-1982 are considered just and fair towards payment of compensation. We also allow escalation charges to be paid in respect of the above items (a) to (e) for the quantities executed under each item on such rates as per contract condition with the only change that initial indices I, in the prescribed

formula for price adjustment as per Cl. 19 A of conditions of contract shall be for the quarter commencing 1st July 1982, instead of those for the month in which tenders were opened as per contract.'

These are the standards mentioned in the unreported decision of this Court referred to above and it appears to us that the arbitrators have added the escalation charges after having worked out the equitable rates for the relevant period.

22. In the present case, there is undoubtedly a price escalation clause as provided under Cl. 19A of the agreement. But that price escalation clause also specifies the base period with reference to which calculations have to be made. Here, the base period is the date of the contract while the work actually commenced much later as stated earlier and extension of time to perform the contract was granted under Cl. 67 of the agreement. Therefore, the relevant date for purposes of calculation of the base period would be that date. In the circumstances, what is to be seen is whether the rates that had been offered in the tenders could be taken as the basis for calculating the escalation or the rates that were prevalent as on the date of commencement of the work in terms of the contract should be taken note of. This is so, in the absence of any specific clause as to at what rate the contractors will have to be compensated in case there is delay on the part of the appellants in allowing the commencement of the work. A very careful perusal of the agreement will disclose that there are no specific clauses which bar consideration of the extra claims in the event of delay on the part of the appellants and price escalation resulting therefrom. Although the arbitrators have termed that damages have to be paid on account of the delay caused on the part of the appellants what really has happened is that the rates prevalent and accepted by the department have been adopted as per the rate analysis filed by them. They have made detailed calculations with reference to the rates worked out by the parties and thereafter arrived at their conclusions. They have adopted two standards; one for the work executed before 23-7-82 and the second for the work executed after 23-7-82. In respect of the latter they have indicated the rates which are just and fair towards payment of compensation to the contractors. To this they have added the price escalation that has taken place thereafter. In the circumstances, it cannot be

slated that the arbitrators have committed any illegality. In the case considered by the Supreme Court in Continental Construction Company (AIR 1988 SC 1116) there were specific clauses which barred payment of extra charges and no such specific clauses are available in the case on hand. Therefore, considering the agreement as a whole we have to negative the contentions raised on behalf of the appellants on this aspect of the matter.

23. The next point raised in this appeal is in relation to the award of interest by the arbitrators. The arbitrators granted simple interest at 12% p. a, in respect of claims Nos. 1 and 2 from the date of entering upon the reference, that is, on 29-5-1985 to the date of decree or the date of payment whichever is earlier. The award of interest by the arbitrators pursuant to an arbitration in exercise of their powers under the Arbitration Act is a serious and vexed question. The power to award interest on the amount awarded by them from the date of award to the date of realisation or till the date of decree as the case may be has been subject matter of various decisions of High Courts and the Supreme Court. In our view the question of awarding interest by the arbitrators may relate to three periods, namely, (i) the period prior to the date of reference to the arbitrators; (ii) the period during which the dispute was pending before the arbitrators; and (iii) the period subsequent to the date of arbitrators' award.

24. So far as the period prior to the reference is concerned, the matter appears to be governed by the Interest Act, 1979, which has replaced the 1939 Act. Under the old Act 'arbitrator' was not included in the definition, of the word 'Court' but in the 1979 Act, which came into force from 19-8-1981 the term 'arbitrator' has been included within the definition 'Court'. Accordingly, an arbitrator can now award interest in such cases in which the Interest Act is applicable. Besides the Interest Act, if there are any statutory provisions for award of interest the arbitrator can award interest thereunder. Here, what the arbitrators have awarded is from the date of entering upon the reference to the date of award and thereafter. That is not a period in respect of which the arbitrators could have made an award at all as S. 3 of the Interest Act, 1979 authorises payment of interest up to the date of institution of proceedings. They had no jurisdiction to make an award granting interest in respect of a period subsequent to the institution of the proceedings. The

only period in respect of which the arbitrators can award interest is the one prior to the reference. This aspect of the matter has been considered by the Supreme Court in Food Corporation of India case : [1988]2SCR329 , Executive Engineer, Irrigation, State of Orissav. Abhaduta Jena : [1988]1SCR253 , State of Orissa v. Construction India : [1988]2SCR145 , State of Orissa v. Dandasi Sahu : AIR 1988 SC1791 and in Gujarat Water Supply and Sewerage Board v. Unique Erectors (Gujarat) (P) Ltd. : [1989]1SCR318 . In Dandasi Sahu's case the Supreme Court summed up the position in law thus : AIR 1988 SC1791 :

'It is now well settled that the interest pendente lite is not a matter within the jurisdiction of the arbitrator. In this connection reference may be made to the observations of this Court in Executive Engineer, Irrigation, Balimela v. Abhaduta Jena, : [1988]1SCR253 where this Court held that the arbitrator could not grant interest pendente lite. In the aforesaid view of the matter this direction in the award for payment of such interest must be deleted from the award. So, we delete the following portion from the award -- 'The award amount shall bear interest at 10% per annum from 9-9-1975 till the date of decree or payment whichever is earlier'. The order of the High Court is modified to the extent that the award is confirmed subject to deletion of the interest as aforesaid. We make it Clear that in the facts of this case interest for the period from 26-9-81 to 18-3-83, the date of the award be deleted. The High Court has, however, granted interest from the date of the decree. That is sustained.'

25. Again in Secretary, Government of Orissa v. Sarbeskar Rout, : AIR 1989 SC2259 the Supreme Court held that award of interest after the arbitrator called upon the parties to file statement of claim (that is the date of institution of proceedings) was without jurisdiction and must be excluded.

It is clear that the power of the Court to grant pendente lite interest arises only under S. 34 of Code of Civil Procedure and such powers are not vested with arbitrators even after the amendment to the Interest Act, 1979. Therefore, the direction given by the arbitrators to pay interest pendente lite has got to be deleted in its entirety.

26. The contractors have filed cross objections regarding reduction of the rate of interest payable, from 17.5% to 12%. The dispute in relation to award of interest subsequent to entering upon reference has been rejected by us and thus the claim of the contractors in this regard in the cross objections lose relevance and stand dismissed.

27. To sum-up the position, the appellants succeed only to the extent of grant of interest pendente lite by the arbitrators and to that extent this appeal is allowed and the award made by the arbitrators stands set aside. In all other respects, the award as decreed by the learned Civil Judge shall stand undisturbed.

28. Appeal is partly allowed and cross objections dismissed as indicated above.

29. Appeal partly allowed.

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