

Extension of Time clauses in a contract, destroy the sustainability of Liquidated Damages – Supreme Court of India

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The Hon'ble Supreme Court of India Bench consisting of Justice Mr NV Ramana and Justice Surya Kant brought in a lot of clarity to the connection between Liquidated Damages and the concept of '*Time is the essence of the contract*' by a very well written Judgment (written by Hon'ble Chief Justice N V Ramana) in the matter of Welspun Specialty Solutions case¹. Even though the law relating to sustainability of Liquidated damages in contracts where time cannot be said to be the essence has consistently developed from Maula Baux case², the above said Judgment settles the law finally. The short question that arose for the consideration of the Hon'ble Supreme Court of India is whether the impugned High Court Judgment was correct in setting aside the Arbitration award which was in favour of ONGC.

The short facts are that Remi Metals was the successful bidder in a global tender issued by ONGC for the purchase of aggregate quantity of 3,93,297 meters of seamless steel casing pipes. It was mentioned in the Purchase orders that the delivery period will commence within 16 weeks and will be completed in 40 weeks, or earlier, from the date of the purchase order. The following were the important conditions mentioned in the purchase orders, (i) The time and delivery is the essence of the supply order and delivery be completed not later than the date specified therein. (ii) It must be noted that delayed supplies even delivery and/or accepted by the purchaser will be treated as supplied/ effected after schedule period without prejudice to failure & termination clause. (iii) Even if extension of delivery period is granted, such acceptance of extension as the case may be will be without prejudice to claim damages under failure & Termination clause unless purchaser clearly waives his right in writing to recover such damages with the approval of competent authority.

More over Clause 10 of GCC titled as FAILURE AND TERMINATION CLAUSE/LIQUIDATED DAMAGES provided for the following conditions after terming the contract as the contract in which time is the essence:

- (a) Recover from the contractor as agreed liquidated damages and not penalty, a sum equivalent to ½% (half percent of the contract price) of unit per week for such delay or part thereof (this is an agreed, genuine pre-estimate of damage duly agreed between the parties) which the contractor has failed to deliver within the period fixed for delivery in the schedule, where delivery thereof is accepted after expiry of the aforesaid period. It may be noted that such recovery of liquidated damages may be

¹ Welspun Specialty Solutions Limited Vs Oil and Natural Gas Corporation Ltd., 2021 SCC Online SC1053

² Maula Bux case (1969)2 SCC 554

upto 5% of the contract price of whole unit of stores which contractor has failed to deliver within the period fixed for delivery. (or)

- (b) It may further be noted that the clause (a) above provides for recovery of liquidated damages on the cost of contract price of delayed supplies whole unit at the rate of ½% of the contract price of the whole unit per week for such delay or part thereof upto a ceiling of 5% of the contract price of delayed supplies (whole unit).....

During the execution of the contract, there were delays in meeting the obligation as required under the contract. In this context various extensions were given by the ONGC to fulfil their obligation. Two of the extensions were granted without LD and five extensions were given with LD. Remi accepted those extensions and satisfied the contract.

The Arbitral tribunal held that liquidated damages, which are pre-estimated damages, cannot be granted as there was no breach of contract due to the fact that time was not the essence of the contract. Accordingly, arbitral tribunal went ahead to determine the actual damages based on the evidence furnished. The arbitral tribunal held that damage for losses incurred during the extended period of delivery where LD were expressly waived and upheld the rest of the claim of Rs.1,09,28,838 was accepted. Hence ONGC filed a petition under S.34 of the Act. The District Judge upheld the award and modified the costs. Both the parties appealed against the order of the District Judge under S.37 of the Act. The High Court held that the Arbitral Tribunal erred in construction of the contract with respect to whether the time was the essence of the contract and in its conclusion that ONGC has to prove loss suffered before recovering damages. Hence, the matter went to the Supreme Court of India.

The Hon'ble Supreme Court of India after hearing the parties came to the following conclusion:

- (a) The Arbitral tribunal's interpretation of contractual clauses having extension procedures and imposition of liquidated damages, are good indicators that 'time was not the essence of the contract'.
- (b) The Arbitral tribunal's view to impose damages accrued on actual loss basis could be sustained in view of the waiver of liquidated damages and absence of precise language which allows for reimposition of liquidated damages. Such imposition is in line with the 2nd para of Section 55 of the Indian Contract Act.

From the above it could be understood that all the contracts that are providing for extension of time cannot be contracts, where time is the essence and hence arbitrator cannot impose liquidated damages. This finding gives a lot of clarity to the above said issue.