

LOSS OF PROFIT CLAIMS AND ARBITRATION

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Normally two types of Loss of profit claims are made in the arbitration/ litigation matters arising out of breach of contract, namely, Loss of profits arising out of delays in the execution and loss of profits arising out of the illegal termination of contract. Loss of profit is one of the type of claims which are claimed by the contractors in infrastructure contracts against the employer, in case the project got delayed for the reasons attributable to the employer or when the contract is terminated and the contractor lost certain opportunities to earn profits by employing their resources in other projects. The endeavor of the author is to deal with the basic principles applied by Courts in granting and quantifying such loss of profit claims.

In these Loss of profit claim cases, the losses are estimated by the claimant, assuming that, if the contract was completed within the time, he would have got an opportunity to employ his resources and the money and might have earned additional profit within the delayed period. To substantiate these type of claims, parties should plead and prove that these delays happened due to the reasons attributable to the Employer. It is not unusual for the contractors to claim loss of profit arising out of diminution in turnover on account of delay in the matter of completion of work. What he should establish in such a situation is that had he received the amount due under the contract, he could have utilized the same for some other business in which he could have earned the profit. Unless such a plea is raised and established, claim for loss of profits could not have been granted.¹ The aspect of the recoverability of expected profits is considered the standard measure of contractual damages and has been known as “the expectation and interest”², which is in practice globally.

¹ Bharat Coking Coal Limited Vs L.K.Ahuja (2004) 5 SCC 109

² “The reliance Interest in Contract Damages” by Lon L Fuller and W.R. Perdue, 46 Yale Law Journal (1936) 52-92.

The main limitation to the above said loss of profit claims is remoteness and causation. Hence the claimant must be able to establish that the breach is not remote in nature and there is a strong association between the loss and the breach. Subject to rules on causation and remoteness, the contract breaker may be liable for the Claimant's loss of future profits from "repeat orders" from his previous customers' which loss was caused by the particular breach of contract³.

As stated above the Loss of profit is also claimed in the arbitrations/ litigations arising out of termination of contracts prior to completion of the execution of the project. When contract is illegally terminated before the completion of work, certainly the contractor is entitled to claim damages on the basis of expected profit from the unfinished work.

For evaluating the Quantum of losses there is no straight jacket formula, according to the facts, business practices and circumstances the Courts and Arbitrators apply different yard sticks. In Brij Paul Singh case⁴, Supreme Court of India held that when such a right is available to the contractor under law and the quantum fixed by the arbitrator is only 10% which according to the contract is reasonable compensation, the court cannot, set-aside the finding of the arbitrator as illegal or biased⁵. Damages can be claimed by contractor where the government is proved to have committed breach by improperly rescinding the contract and for estimating the amount of damages, the court should make a broader evaluation instead of going into minute details. Where in the works contract, the party entrusting the work committed breach of contract, the contractor is entitled to claim the damages for loss of profit, which he expected to earn by undertaking the works contract. Claim of expected profits is legally

³ Jackson Vs Bank of Scotland (2005) UKHL3, Para 26-137 of Chitty on Contracts Vol-I, 2015 Edn

⁴ Brij Paul Singh Vs State of Gujarat (1984) 4SCC 679

⁵ Dwarka Das Vs State of M.P. (1999) 3 SCC 500, Superintending Engineer TNUDP Madras Vs A.V. Rangaraju AIR 1994 Mad 217, Satyam Builders Vs Delhi Development Authority 1997 (2) Arb. LR26(Delhi)



admissible on proof of breach of contract by the erring party. What would be the measure of profit would depend upon the facts and circumstances of each case. But there shall be a reasonable expectation of profit is implicit in a works contract and its loss has to be compensated by way of damages, if the other party to the contract is guilty of breach of contract⁶.

In supply contracts the quantification was different from the works contracts. In Karsandas case⁷ Supreme Court of India held that if the buyer agreed to purchase scrap Iron, the buyer would not be entitled to damages beyond the difference between the contract price and the market price on the date of the breach. In Emil case⁸ it was held that if there is no market price the measure of damages is the difference between the resale price and the contract price. Breach of a contract in which parties knew that the goods were for supply to a third party under a sub-sale, would entitle the buyer the difference between the contract rate and sub-sale rate. The Delhi High Court in Delhi State Industrial & Infrastructure case rejected the requirement of proving the loss to make a loss of profit claim⁹. In the case of Mohamad Salmathullah¹⁰ Supreme Court refused to interfere in the lower court granting of 15% Loss of profit. Hence, the conclusion is that loss of profit claims is sustainable against the breaching party but the quantification of loss of profit differs from case to case and same formulae cannot be used.

⁶ MSK Projects INDIA (JV) Limited Vs State of Rajasthan and Another (2011) 10 SCC 573, A.T.

⁷ Karsandas H Thacker Vs Saran Engg Co.Limited AIR 1965 SC1981

⁸ Emil Adolph Zippel Vs KD Kapur & Co AIR 1932, Sind 9, 139IC,114

⁹ Delhi State Industrial Infrastructure Development Corporation Limited Vs M/S. Rama Construction Company 2014 SCC Online Del 3470

¹⁰ Mohamad Salmathullah Vs Government of Andhra Pradesh AIR 1977 SC 1481