Dispute perspectives
Dispute Resolution Mechanism in Highway Contracts
<table>
<thead>
<tr>
<th>Contents</th>
</tr>
</thead>
<tbody>
<tr>
<td>Introduction</td>
</tr>
<tr>
<td>Dispute Resolution Mechanism under the NHAI</td>
</tr>
<tr>
<td>Calculation of Delay Claims</td>
</tr>
<tr>
<td>News Snippets</td>
</tr>
</tbody>
</table>
Dear Friends,

Welcome to our second issue of Dispute Perspectives – a monthly newsletter that will provide you with a focused analysis of ongoing trends in dispute resolution in India and update you with the ongoing events in this regard.

In this issue we will look at the dispute resolution mechanism under the much touted highway contracts under the National Highway Authority of India. Through this article we aim to gather a basic understanding of the existing dispute resolution mechanism and significance of expert assistance in calculation of delay claims.

We, of course, look forward to hearing from you. I believe that we should be able to assist you or at least guide you in your pursuit of finding the most efficient and effective way to resolve disputes.

Should you have any questions, concerns or suggestions for future topics, please feel free to write to us.

Warm Regards,

Vidya Rajarao
National Leader, Forensic Services

If you believe you have received this newsletter by mistake or if you wish not to receive our upcoming newsletters, you may please send a mail to divya.rishi@in.pwc.com to unsubscribe.


Introduction

India has one of the largest road networks in the world with 33.14 lakh kilometres consisting of national highways, state highways, major district roads and village roads.\(^1\) The eleventh five year plan envisaged a projected investment of USD 78.54 billion in building roads and bridges.\(^2\) The Government’s most ambitious National Highway Development Plan (NHDP) had two phases implemented through Engineering Procurement Construction (EPC) contracts, while the other phases are being implemented by way of the Built Operate Transfer (BOT) model. The likelihood of suffering significant losses under the EPC contracts is attracting contractors to switch their preference to BOT contracts, where the contractors/concessionaires have a much better control over some of the operational issues.\(^3\)

Interestingly, while the Government seems to be laying a lot of thrust on investment in road transport sector, the sector continues to be embroiled in critical issues like inefficient dispute resolution mechanism, governance and other operations issues.

In 2011, the National Highway Authority of India (NHAI) was facing INR 11,084 crore in arbitration claims in tribunals and various courts.\(^4\) Majority of these disputes were reported to be arising out of EPC projects. A significant amount locked up in disputes warrants our attention to this issue’s topic of dispute resolution mechanism in highway contracts. In this issue, we will endeavour to build a basic understanding of the existing dispute resolution mechanism and significance of expert assistance in calculation of damages. Last but not the least, we have tried to list certain prescriptive steps that may be taken by contractors, sub-contractors and employers to efficiently navigate the dispute resolution process.

---

Dispute Resolution Mechanism under the NHAI

Let us first look into why the likelihood of disputes is high in highway contracts. One of the key reasons leading to a dispute in a highway contract is non-availability of land. When the NHAI or the employer fails to provide land to the contractor, the project gets delayed. Most of the highway contracts include a liquidated damages clause and contractors and sub-contractors take recourse to extension of time to escape the payment of liquidated damages.

The dispute resolution process followed under the NHAI is represented graphically in Figure 1.\(^5\)

---

\(^5\) Faster Implementation of NHDP, Second Committee Report under the Chairmanship of Mr. B.K.Chaturvedi, February 2010. The dispute resolution mechanism classified disputes in three categories. Category A comprises of claim amount less than 10 crores or 5% of the contract price, whichever is lower. Category B comprises of claim amount between 10 to 100 crores and Category C comprises of claim amount more than 100 crores.
Even though this process of dispute resolution looks simple and straightforward, it is not very robust. One of the major claims by the contractor in any highway contract dispute is extension of time or overstay on site due to reasons not attributable to the contractor. Often contractors try to make this claim on their own but seldom do such claims sustain the rigour of the mediation or DRB process. On the other hand the employer (can be either NHAI or the contractor in case of sub-contractor) suffers from loss of revenue and loss reputation due to non-completion of the project. Therefore, the need of an expert arises who can provide an impartial advice to the employer, contractors or sub-contractors because they are independent to the dispute.

Experts can help with analysis of delays and consequent claims in the project. They can advise on various claims that may be claimed based on the provisions of the contract and also provide ammunition to the contractor or sub-contractor to fight possible wrongful levy of liquidated damages by the employer.

The contractors, sub-contractor or employer can benefit from the report provided by these experts while making representation in front of the mediation panel or arbitration tribunal. The services of an expert do not stop with just the preparation of report containing the analysis and claims; they can go a step ahead and testify before the Arbitral Tribunal or the Court on behalf of their client, thereby assisting the Tribunal or the Court in arriving at a decision.
**Calculation of Delay Claims**

The phrase ‘Time is money’ can be best understood in any construction (highways, railways, ports, etc) dispute. When highway projects are delayed, the contractors and the employers not only lose profits waiting for the project’s completion but also the opportunity of commencing new projects. At the end of every dispute, each party is either interested in receiving or avoiding payment of money damages. This article would stand incomplete without discussing the calculation of delay claims.

Very often, it has been observed that calculation of damages is left to the parties’ accountants. A probable reason for this is that the attorneys are more comfortable with the legal implications of the contracts rather than going through the tedious process of gathering the financial evidence.

In highway contracts, it is rather a disastrous idea to leave the damage analysis to the in-house accountants of parties at dispute. Contractors and employers are not equipped with the necessary independence and skills to for analysis of construction damages. A detailed analysis of the source documents is needed rather than doing shorthand analysis of summary documents. A critical component of calculation of delay claim is construction schedules. A delay claim is typically calculated on the grounds of as-planned schedule and as-built schedule. The gap analysis helps build a case of where, why and how the delay occurred and whether it was addressed effectively. Addressing the delay effectively means whether appropriate documentation was maintained by the contractor or employer who encountered a delay in the project. Such calculation may additionally consider actual costs and as-bid costs.
As a part of calculation, following key items should be carefully looked at as they may significantly impact the calculation of the damages due to delay:

- Overhead costs incurred during the actual period and the extended period of the contract;
- Loss of productivity due to the delay;
- Material direct cost during the delay;
- Increased labour hours;
- Financing cost of working capital due to delay; and
- Escalation in prices of labour and materials.

Some of the essential points that parties involved in a highway project may consider to mitigate damages resulting due to delays are discussed below:

- Documentation plays a key role in delay claims. As mentioned earlier, the contractor or the employer needs to earmark the costs that are caused due to the delay. It helps in expediting the process of dispute resolution if documentation is managed efficiently;
- In case of loss of productivity, the Supervision Consultant must maintain a record explaining the reasons for the disruption. Here the Supervision consultant can either be a project management consultancy or engineers hired by the NHAI to oversee the contractor’s work or hired by a contractor to supervise the sub-contractor’s work.
- Very often the employers, contractors and sub-contractors do not recognise the delays unless it has taken its full course. The parties involved must predict the likelihood of delays and claims. The project performance report must be studied carefully and take corrective actions to stand a better chance to win a claim in a dispute;
- The project schedule is a powerful tool to identify the delay. Hence it must be maintained meticulously and monitored regularly during the project.
- It is difficult to avoid disputes in highway contracts owing to increasing complexity offered by the public private partnership (PPP) model and also sophistication adopted in EPC contracts. The party that will prevail in the dispute is the one who has accurate records of the delay and can substantiate delay claims with contemporaneous documentation.
**News Snippets**

**Word of Caution: Bilateral Investment Treaties**

A first of its kind, ruling from an international arbitration panel has held that the Government of India breached its obligations towards an Australian mining company, White Industries, under the India-Australia Bilateral Investment Treaty (BIT). The panel's reason was that the Indian judicial system did not provide White Industries an effective means of asserting claims and enforcing rights owing to delays inherent in the system.

At the time of enforcement of the International Council for Arbitration (ICC) award, the Government of India approached the Court to set aside the award triggering an investment dispute under the India-Australia BIT in July 2010. Typically under investor-to-state disputes, the measures that have been challenged include emergency laws put in place by governments, value-added taxes, land use regulations that impact an investor, divestment regulations that affect an investor's rights as a shareholder and so on. Failure of a government to enforce an award is rare and holds significance for a country's judicial system.

Related article was published in the Economic Times on 3 March 2012 under the heading “INDIA SHOULD BE CAUTIOUS ABOUT BILATERAL TRADE PACTS” accessed on 12 March 2012 on the following link: [http://articles.economictimes.indiatimes.com/2012-03-03/news/31119524_1_coal-india-arbitration-proceedings-settlement-of-investment-disputes](http://articles.economictimes.indiatimes.com/2012-03-03/news/31119524_1_coal-india-arbitration-proceedings-settlement-of-investment-disputes)
Does it lead to a bias when the Chief Engineer is selected to be the arbitrator?

In a certain dispute, referred to arbitration, it was argued in the court of law that the arbitrator who is a Chief Engineer and also the arbitrator in the case was biased. However, the Supreme Court’s ruling stated that the parties who select the Chief Engineer as the arbitrator despite knowing his role, authority and power are bound by their choice. The Court also held that only on a valid legal ground can the parties challenge his exclusion.

The parties in construction projects must meticulously draft their agreement especially on significant points of language, choice of arbitrator(s) and seat of arbitration.

Related article was published in the Business Standard on 5 March 2012 under the heading “BIAS OF ARBITRATOR NOT PROVED” accessed on 12 March 2012 on the following link: http://www.business-standard.com/india/news/biasarbitrator-not-proved/466719/

Arbitration as an effective dispute settlement mechanism, says expert

Nowadays, we can see that up to 60 to 70 per cent of cases pending in courts arise out of commercial contracts. This has led to a backlog of cases in the Indian courts. It should be understood that the Courts are there mainly to safeguard constitutional issues, criminal issues and special issues.

In the construction sector, for instance, the building of a major hotel project might involve multiple contracts. They can cover an entire gamut of issues ranging from recruitment, trainees, procurement, engineering and design to land acquisition. In case there is some trouble with the project, all these could end up in court.

These cases deal with highly technical and domain-specific contractual agreements. If all of them were to end up in court, how fast can courts proceed and pronounce a judgment? But if there is an arbitration clause built in, one can engage a retired or senior civil engineer or structural engineer with mutual consent of the parties involved to settle the matter.

Related article was published in the Business Line on 27 February 2012 under the heading “ARBITRATION MAY HELP COURTS DEAL WITH PILING UP OF COURT CASES” accessed on 12 March 2012 on the following link: http://www.thehindubusinessline.com/industry-and-economy/economy/article2938509.ece?homepage=true&ref=wl_home
Supreme Court Judges suggest Mediation to be effective in disposal of pending cases.

In a conference organised by the UP State Legal Services Authority, it was extensively discussed that mediation could be an effective means to help the disposal of pending cases.

Several authorities and institutions around the country are spreading awareness on varied dispute resolution mechanisms to avoid litigation. This can be a step towards helping the Courts to effectively manage cases. The effectiveness of a mechanism largely depends on the nature of a dispute and the demand for sophistication in the proceedings.

Related article was published in Times of India on 26 February 2012 under the heading "MEDIATION EFFECTIVE IN REDUCING CASES’ PENDENCY," accessed on 12 March 2012 on the following link: http://articles.timesofindia.indiatimes.com/2012-02-26/lucknow/31101395_1_mediation-dispute-resolution-subordinate-courts

UK’s Ministry of Justice pushes for compulsory mediation

On 9 February 2012, The Ministry of Justice in the UK introduced its plan to for mandatory mediation provisions for small value payments. The new regime aims to compel parties in disputes with claim values of up to GBP 100,000 to seek mediation or other forms of ADR deemed acceptable such as arbitration, conciliation or a settlement conference.

This step by the Ministry of Justice is aimed to give a significant boost to mediation as a form of ADR.

Related article was published in Times of India on 22 February 2012 under the heading “UK UPS ANTE ON COMPULSORY MEDIATION DESPITE CITY OPPOSITION,” accessed on 12 March 2012 on the following link: http://www.cdr-news.com/arbitration-and-adr/112-articles/1883-uk-ups-ante-on-compulsory-mediation-despite-citys-opposition
About PwC

PwC firms help organizations and individuals create the value they're looking for. We’re a network of firms in 158 countries with close to 169,000 people who are committed to delivering quality in assurance, tax and advisory services. Tell us what matters to you and find out more by visiting us at www.pwc.com.

In India, PwC (www.pwc.com/India) offers a comprehensive portfolio of Advisory and Tax & Regulatory services; each, in turn, presents a basket of finely defined deliverables. Network firms of PwC in India also provide services in Assurance as per the relevant rules and regulations in India.

Providing organizations with the advice they need, wherever they may be located, our highly qualified, experienced professionals, who have sound knowledge of the Indian business environment, listen to different points of view to help organizations solve their business issues and identify and maximise the opportunities they seek. Our industry specialization allows us to help co-create solutions with our clients for their sector of interest.

We are located in these cities: Ahmedabad, Bangalore, Bhubaneshwar, Chennai, Delhi NCR, Hyderabad, Kolkata, Mumbai and Pune.