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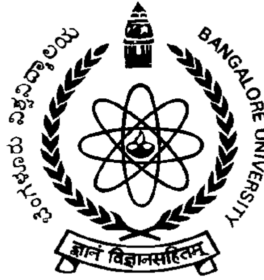

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A CRITICAL ANALYSIS OF PRICE VARIATION IN GOVERNMENT CONTRACTS

-Prof. (Dr.) Sairam Bhat* Aparna S** & Jaibatruka Mohanta**

Introduction

Price variation clauses are increasingly being incorporated in modern day contracts especially in long-term contracts. These contractual clauses relate to the expenditure, over and above the contractual price, that is incurred by a party in fulfilling his contractual obligations. Depending on the nature of goods or services involved in the contract, clauses related to contract price may assume different forms. It may be in the form of a fixed price contract where there is a supply of goods or services at a *pre-determined* price, which is unlikely to change as the scope of the work itself is bound to continue without many changes. It can also be in the form of a cost-plus contract where the scope of work and the costs involved are not definitive; accordingly, the contractor is paid the expenses incurred by him in an incremental manner once his obligations have been performed. Determination of contract price is a significant step in contract formation as a contractual breach typically entitles the aggrieved party to recover damages amounting to the difference between the contract price and market price of the commodity or service.[1]

The labour and materials in commercial contracts, including Government contracts, are usually procured at an estimated price.[2] Since the contracts usually seek to accomplish infrastructural or technological developments to existing systems, they involve the procurement of an enormous amount of material from the market. The prices of these materials are susceptible to fluctuations beyond the control of either party to the contract.[3] Therefore, it would be impractical to keep the contractual price fixed. If the supplier of labour or any other materials is compelled to continue with the supply at prices that formed a part of the contract without factoring in the surges in prices in the market. In that case, it will lead to a situation where the supplier would incur losses, and the procuring entity would stand to gain unfairly. Such a scenario would make it a case of 'unjust enrichment'

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[1] P.S.N.S Ambalavana Chettiar & Co Ltd. v. Express Newspapers Ltd., Bombay, AIR 1968 SC 741.

[2] Parth Rawal, *Can Arbitrator Award Escalation Charges in the Absence of any Clause for Escalation in the Contract?* 9 INDIAN LEGAL IMPETUS 4 (2018).

[3] *Id.*

where one party receives a benefit to the detriment of the other in a legally unjustifiable manner. This principle of unjust enrichment of one party at the expense of another is proscribed under the law of contracts, and the party who has unjustly enriched is liable to pay compensation to the other party.[4]

In this article, the authors delve into how variations in prices of labour and commodities are accommodated in Government contracts. The authors also encapsulate the possible remedies that can be availed of by a contractor when the Government contract contains no provision for factoring in the surges or decline of prices owing to market fluctuations. The authors argue that there is a pertinent need to make contractual prices flexible to ensure profitable performance in a scenario pervaded by market and price instability.

Price Escalation-Goods v/s Works Contract

In Government Contracts, the contract is usually awarded through the process of tendering to the lowest bidder. In such tender documents, price variation clauses play a significant role. Price variation clauses are generally incorporated in contracts as a precautionary measure so as to take into account the charges that would be payable by a party to the contract owing to fluctuation in the prices of raw materials necessary for the performance of his contractual obligations.[5] For instance, if there is an increase in the prices of building materials in the market, the incorporation of a price variation clause in the construction contract would ensure that the contractor would not have to incur losses by paying additional money out of his pocket. Such forms of price variation clauses may be generally referred to as price escalation clauses. However, it is pertinent to note here that in most Government tenders, there are explicit c that deny contractors any claim to price variations, even though the contractors are for goods, wherein the contractor ought to supply materials beyond 12 months, sometimes beyond 24 months as well. Further the Government tenders generally have stipulations for extension of such contracts, as well.

However, in Works Contract, it is important to note that an escalation in prices may also happen owing to a change in the scope of work during the contract, such as an alteration in the planned design or switching to a different construction material other than that agreed upon during the formation of the contract.[6] If the contract price increases due to this, it is also a cost escalation. Nonetheless, such cost escalations have been made due to the intention of either of the parties to a

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4 *See* GRAHAM VIRGO, THE PRINCIPLES OF THE LAW OF RESTITUTION 51-61 (2D ED., 2006).

5 *See* Ramachandran Maran, Senthil Rajendran & Satyanarayana Kalidindi, *Material Cost and Escalation Clauses in Indian Construction Costs,* 164 Proceedings of the Institution of Civil Engineers – Construction Materials (2015).

6 *See* JG Perry, PA Thompson & Baxter, *Construction Finance and Cost Escalation,* 62 Proceedings of the Institution of Civil Engineers 623-642 (1977).

contract and hence, cannot be regarded as having been triggered due to an event that was outside their control. Such cases are not covered within the ambit of price variation clauses that are being discussed here. Only those forms of price escalations attributable to events outside the control of the parties to a contract, such as inflation, interruption in supply chains, etc., would be capable of being remedied with a price escalation clause. Further it is important to note that price change sought under a 'change in law' clause would also be interpreted significantly different that a merely price variation clause, both with the application of legal principles and the grounds under which it can be sought. This can be clearly understood in the case of *SEAMEC Ltd. v. Oil India Ltd.*,[7] wherein the Supreme Court noted that the tribunal had unstintingly interpreted the 'change in law clause,' i.e., even though the government circular which led to an increase in the price of HSD was not explicitly a law. Still, it does come under the *"force of law",* and therefore it falls under the purview of the change in law clause. Thus, the Apex court was of the view that the tribunal should have harmoniously constructed the contract as a whole and that the parties did not agree to the "broad interpretation" of "the change in law" clause envisaged in the contract. Further, the contract had come into force through a tender bid. According to the contract, the price was payable to the 'contractor' only after the full and proper completion of the contractual obligations. Thus, it was highlighted that according to clauses 14.7 and 14.11 of the contract –

"the rates, terms and conditions were to be in force until the completion or abandonment of the last well being drilled."

From the above-mentioned points, the Court ascertained that the parties did not agree to the broad interpretation of the clause and that the contract was based on a fixed price. From this case, it can be analyzed that the 'price variation' or "change in law" clauses are quite pertinent to the contracts. Therefore, they should be added to the contract while interpreting it as a whole to avoid superfluous clauses. Also, in the case of the *Energy Watchdog v. Central Electricity Regulatory Commission*[8], it was held that the 'change in law' clause cannot be invoked in cases where the change in price has occurred due to a change in statutory provisions of a foreign state.

Thus, while the variation in price will be permitted, there is always a restriction on the quantum of relief that can be provided under an expressed clause. However, this may be entirely different for Price variation sought under a 'Change in law' clause. But to a contractor, it may seem more practical to claim price variation, in the absence of such clauses in Government contract, for a statutory increase in material prices given that the drafting of this clause is always negative

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7 SEAMEC Ltd. v. Oil India Ltd., (2020) 5 SCC 164.

8 *Energy Watchdog v. Central Electricity Regulatory Commission, (*2017) 14 SCC 80.

towards the contractors than a Change in law clause.[9] It is pertinent to remember that price variation operate in a restricted manner, and courts, while adjudicating, consider multiple factors while allowing for their operation.

In view of the above, a price variation clause can also be invoked in situations where there is a decrease in the prices of the materials. For instance, a price variation clause would be extremely beneficial to the Government if there is a sharp decline in the prices of materials used for construction, though rarely, in which case, it is liable to pay the contractor only at proportionately reduced rates. A typical Price variation clause in a Government contract can be as given below –

"46A.5 *Components of various items in a contract on which variation in prices be admissible, shall be Material, Labour, Fuel, Explosives & Detonators, Steel, Cement, Concreting, Ferrous, Non-ferrous, Insulator, Zinc, Erection etc. However, for fixed components, no price variation shall be admissible.*"[10]

The allied provisions in a Price Variation clause would ideally elaborate the mechanism and formulae that would be used to compute the variations in prices that would be payable by the parties. But what happens in a situation where there is an absence of a Price Variation clause in a Government Tender agreement? How would either the Contractor or the Government substantiate the need to increase or decrease the quoted prices in response to fluctuations in the market when the contract contains a clause that forbids price variation on any account whatsoever?

The position of law, especially those as stated under Central Government procurements guidelines can be found under the General Financial Rules 2017. The Rules state that in relation to the general principle of contracts being definite and certain, price variation clauses are an exemption under the General Financial Rules.[11] The Rules mandate that price variation clauses can be provided only in long-term contracts, where the delivery period extends beyond 18 months.[12] They also require the price variation clause to stipulate the minimum percentage of variation of the contract price above which price variations would be admissible[13] and also provide that the clause should provide for a ceiling on price variations, especially where escalations are involved.[14] Additionally, the clause should also contain the mode and terms of payment of the price variation admissible.[15] Further,

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[9] Aishwarya Sathpathy, Seamec Ltd. v. Oil India Ltd.: A Case for Price Variation Clause Over Change in Law Clause, 8 INDIAN LEGAL IMPETUS (July 2020).

[10] Ministry of Railways, Notification No. 2020/CE-I/CT/3E/GCC/ Policy, *Indian Railways Standard General Conditions of Contract*, Clause 46A, (2020), https://www.iricen.gov.in/iricen/Works_Manuals/GCC_July_2020.pdf.

[11] General Financial Rules, 2017, Rule 225(i).

[12] General Financial Rules, 2017, Rule 225 (viii)(a).

[13] General Financial Rules, 2017, Rule 225(viii)(e).

[14] General Financial Rules, 2017, Rule 225(viii)(d).

[15] General Financial Rules, 2017, Rule 225(viii)(k).

Rule 225 mentions that the clause should also specify the cut-off dates for material and labour as these make a difference.

Thus, primarily, to enable the calculation of the variation, under the GFR Rules, the agreed-upon price must specify *four parameters*- the minimum price fluctuation required to activate the variation clause, the maximum fluctuation which can be accommodated, the modalities of payment, and lastly, the time duration for which the clause operates. Along with this, the guidelines provide for estimating price using variables like the contract price at the base level, assigned percentage to the material and labour elements, and the base month.

To examine the above, if we suppose a supplier enters into a tender agreement with a State University to supply answer booklets to the latter. The letter of acceptance is issued, and the contract is valid for a period of two years. The contract stipulates that "*Prices quoted by the Tenderer shall be fixed during the Tenderer's performance of the Contract and not subject to variation on any account. A tender submitted with an adjustable price quotation will be treated as non-responsive and rejected,"* and "*The rates approved will be valid for two years, and no revision of rates will be permitted*." However, despite the above, the Contractor accepts the Purchase order and is supposed to perform the contract. Due to persistent inflation, the rate of paper has increased substantially by 50%-60% during this period. In such a scenario, can the Supplier claim price variation in response to the increase of cost in paper materials where there is no clear clause providing for price escalation? Can he claim compensation for the additional amount payable by him due to the increase in the cost of paper?

To answer the above, judicial precedent as was held by the supreme court in the case of *Bedi Construction Co. v. Delhi Development Authority,*[16] *stated that –*

*'that if the increase in prices of material purchased by the contractor or labour rate is more than 10% of the value of the contract, then the contractor can only make a claim in respect of increase in prices that also for the amount which goes **beyond 10%** of the contract value."*

Claim for Price Escalation

The Manual for Procurement of Works, 2019,[17] states that "*the contract price is subject to adjustment on account of price variation during the contract period as per a specified formula*." It also stipulates a ceiling of 10% (ten percent) of the contract price for catering to any changes in the scope of the project, the cost of which should be borne by the procuring entity.

The Manual further states that clauses providing for price variation can be incorporated in contracts whose period of completion is more than eighteen (18) months. Additionally, it also stipulates that if contractual provisions do not

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16 *Bedi Construction Co. v. Delhi Development Authority, ((2009) ILR Supp. 8 Del 52).*

17 Ministry of Finance, Manual for Procurement of Works (2019).

envisage compensating contractors for any rise or fall in costs that may be incurred by them, it shall be deemed that the unit rates and prices already incorporated are inclusive of such contingencies.

What essentially follows from this is that even if a fixed price has been expressly provided and there is an absence of a Price Variation clause for a tender that exceeds 18 months in duration, the rates and prices would be deemed to be catering to such contingencies as well. Simply put, for any procurement contract whose time period exceeds 18 months, price variation clauses are deemed mandatory and, in their absence, will be assumed by the court to be present in the contract. Therefore, in the illustration provided above, the Supplier can take recourse to this provision in the Manual to make his claim for price escalation corresponding to inflation in the market, even in the absence of an express price variation clause.

Claim for Compensation

Generally, the price variation clause is not a mandatory requirement in a contract or term and condition in the tender document. As the law of contracts would state; would in the absence of a price variation clause, the price variation needs to be construed in terms of equity? Notably, the Supreme Court and the various High Courts in India have extensively discussed the applicability of the law on price escalation and have culled out various principles, and enunciated laws of the contract to provide a remedy to an affected party who has suffered losses due to increases in prices or ensuing delays in the completion of work as a result of other party's actions. These judgments have demonstrated that a contractor even in the absence of a price escalation clause in the contract/tender may still seek remuneration at escalated rates from the Government agency.

For instance, in *Tarapore and Company v. Cochin Shipyard Ltd,*[18] the Apex Court held that if the factual situation on the basis of which the agreement was entered into by the parties ceases to exist, the agreement would be otiose to that extent. Further, if rates that the contractor initially quoted become irrelevant as a result of subsequent price increases, the contractor's claim for compensation for the excess expenditure incurred as a result of price increases cannot be denied solely on the basis that the contract does not contain a price escalation clause. Similarly, in *P.M. Paul v. Union of India,*[19] the Supreme Court granted compensation to a contractor in respect of losses due to increases in material prices, labor costs and transportation costs during the lengthened time of the contract, in spite of the fact that the parties' contract lacked an escalation clause. It was further held that in the event of a price increase, the lack of a price escalation clause in a contract would not be conclusive if the completion deadline was delayed for reasons other than the contractor's fault.

[18] Tarapore and Company v. Cochin Shipyard Ltd., AIR 1984 SC 1072.

[19] P.M. Paul v. Union of India, AIR 1989 SC 1034.

Further, in *K.N. Sathyapalan (Dead) by Lrs. v. State of Kerala and Ors.,*[20] the Supreme Court reiterated these principles while dealing with an issue related to escalation for losses suffered by the contractor on account of price escalation of materials and observed that if one of the parties to the contract is unable to fulfill its obligations which has a direct bearing on the work to be executed by the other party, then the latter is entitled to be awarded compensation from the first party for its failure to discharge its obligations.

The rise in prices of commodities owing to severe inflation is a hard fact, which is reflected in the data shared by the office of the Economic Advisor of India. For instance, the Wholesale Price Index (WPI) of paper, as sourced from the office of the Economic Advisor of India, reveals that there has been a significant rise in inflation on paper. In January 2022, the WPI on paper for printing and writing was at 137.2; in September 2022, the WPI stood at 169.8, which clearly shows an upward inflation trajectory in this industry.[21] In addition, the cost of manufacturing paper and paper products has also escalated significantly. For instance, the WPI of manufacturing paper and paper products in 2018 – 19 was 123, and for the financial year 2021 – 22, it has significantly risen to 137.5, indicating an inflationary increase at a very high rate.[22] Applying the WPI as a marker to determine percentage of escalation to the example earlier stated in this article [supply of paper], an escalation may be claimed as compensation.

The Supreme Court has observed that escalation is a *'normal and routine incident'* and has accordingly allowed claims for price escalation.[23] In a recent case, *Raghunath Sahu v. State of Odisha*[24] the High Court of Odisha upheld the validity of a clause in the tender agreement which enabled a contractor to claim price escalation in the event of a surge in prices reflected in the Wholesale Price Index and Consumer Price Index (CPI). Thus, the WPI and CPI indices can be considered as furnishing authentic information regarding the increase of prices in response to inflation, and they can be relied upon to substantiate claims regarding the additional costs incurred as a result of the increase in prices of materials owing to inflation.

An Incentive for Courts to read in Price variation Clauses in the Absence of Contractual Clarity

Frustration of Contracts due to Force Majeure Events

When a contract does not contain a detailed price variation clause outlining reasonable price variations that the contractual agreement can accommodate, there

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20 K.N. Sathyapalan (Dead) by Lrs. v. State of Kerala, 2007 (5) SLT 17 (SC).

21 Department for Promotion of Industry and Internal Trade, *Wholesale Price Index* (2022), https://eaindustry.nic.in/display_data_201112.asp

22 *Id.*

23 Food Corporation of India v. A.M. Ahmed and Co., (2006) 13 SCC 779.

24 Raghunath Sahu v. State of Odisha, AIR 2022 Ori. 37.

are two alternative options that a performing party can resort to upon an unprecedented fluctuation in the cost of materials pertinent to contractual performance. As demonstrated above, especially in long-term government contracts where the performance occurs over the span of multiple years, continuing performance would prove financially catastrophic to the supplying party. In such cases, the party can either appeal to the court to read a price variation clause into the contract, thereby allowing it to claim compensation equivalent to the loss incurred by it from the government, or alternatively, the party is open to contend the frustration of the contract owing to the impossibility of performance in accordance with the initial terms. Simply put, the party can contend the occurrence of a *force majeure* event.

The legal basis for the second contention is Section 32 of the Indian Contract Act, which provides that when the performance of the contract becomes impossible owing to unprecedented circumstances, the party is no longer obliged to execute his contractual obligations. However, courts in India have been reluctant to allow the discharge of contractual liabilities in cases when a *force majeure* event has not been included in the contract and is used as a basis to argue for frustration. For instance, in *Satyabrata Ghose v. Mugneeram Bangur*, the Supreme Court held that when the contract specifically contemplated events that could justify non-performance, the case would fall under the ambit of Section 32 of the Indian Contract Act, as against Section 56.[25]

This would restrict the force majeure events to those mentioned explicitly in the contract. The court in *Alopi Parishad and Sons v. Union of India* has also held that "vague pleas of equity" will not allow parties to disregard the express provisions of the contract.[26] The court held that events ordinarily foreseeable by parties in the course of trade or business, like price fluctuations, are deemed to be in the contemplation of parties – therefore, being incapable of invoking the doctrine of frustration under Section 56. Thus, courts have often considered ordinary events like price fluctuation to be encompassed by the risks undertaken by the contracting party. Mere onerous conditions have been declared as falling outside the purview of Section 56 of the Indian Contract Act.

However, the courts have been more sympathetic in instances where contractual performance becomes incapable of discharge owing to extraneous circumstances which *radically alter the very basis of the contract*.[27] A clear principle can be distilled from the case of *Taylor v. Caldwell*.[28] Here, the court held that any condition which could 'defeat the purpose of the contract' could frustrate

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25 Satyabrata Ghose v Mugneeram Bangur, 1954 SCR 310.

26 Alopi Parishad and Sons v Union of India, 1960 SCR (2) 793.

27 This principle was first adopted by the UKHL in Davis Contractors Ltd v Fareham Urban District Council.

28 Taylor v Caldwell 22 ER 309.

it, however in contemporary times whether price escalation beyond the sense of reasonability would defeat the purpose of the contract is debatable. The jurisprudence that economic hardship[29] cannot be argued as frustration, is clearly and firmly laid down by judicial precedence.

This principle is extremely relevant in government tenders. Government tenders are usually given to the lowest-bidding party. In such cases, the contractual price forms the very basis of the tender agreement between the supplier and the government. This demonstrates the keen commercial sensitivity of the participants. In government contracts purported to be executed over long courses of time, drastic price fluctuations are capable of exceeding the original price significantly, thereby bearing the potential to frustrate the very basis of the contract itself. In *Easun Engineering v. Fertilizers and Chemicals Travancore*, the Court has also observed that an abnormal price increase could be considered as 'frustrating the very basis of the contract.'[30] As evidenced by such reasoning, price fluctuations can be adopted as an adequate basis for frustrating the tender agreement. In such cases, the supplier is free to depart from his contractual obligations. It is significant that economic hardship caused due to price escalation be admitted as a ground for compensation atleast, if not for complete and absolutely avoidance of performance under the doctrine of frustration.

Price Fluctuation Clauses – An Effective Alternative to Frustration

The above method of frustration poses a significant problem. Through tenders, the state usually seeks to accomplish important objectives, like providing commercial and infrastructural facilities to the people. Frustrating contracts would stall the process, causing inconvenience to citizens, who are the ultimate stakeholders. Floating another tender would be a protracted and time-consuming process, thereby affecting the citizenry detrimentally. In such cases, instead of allowing for the frustration of contracts, courts can adopt the first approach – that is, reading a price variation clause into the contract. The court can then *deem* the contract to be *flexible and accommodative* to price fluctuations. With such clauses, performance would no longer be intractable since the supplier would be enabled to demand the excess amount from the government. The Government would be spared the hassle of floating another tender, and the contract would be executed in a time-bound manner.

Abusing this process would also be impossible within the framework provided by the General Financial Rules. As demonstrated above, the Rules impose a cap on the estimated price fluctuation, which the supplier can demand from the government. This would mitigate losses and also ensure a continuation of contractual obligations. This argument postulates a pertinent reason for courts to

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[29] *See e.g., Energy Watchdog v. Central Electricity Regulatory Commission, (*2017) 14 SCC 80; Tsakiroglou & Co. Ltd. v. Noblee Thorl GmbH, 1961 (2) E.R. 179.

[30] Easun Engineering v Fertilizers and Chemicals Travancore, AIR 1991 Mad 158.

read price variation clauses into contracts that lack clarity regarding the same. The frustration of the tender is a real possibility, which can be avoided satisfactorily through this approach.

Claiming Price Variation when there is a statutory escalation of Minimum Wages

Contractors are under an obligation to pay minimum wages to the labourers hired by them according to the mandates of the Minimum Wages Act, 1948. It is routine for the State Governments to issue revised rates of minimum wages that would be payable to labourers in a periodical manner. In this context, it is worthwhile to examine whether contractors would be able to claim price variation in Government contracts as and when there is an escalation of labour costs owing to the statutory revision of minimum wages. This has been a point of contention for decades, and the position of law emerging from the judgments pronounced by various Courts needs to be appraised.

In *Associated Engineering Co v. Government of Andhra Pradesh,*[31] the issue of eligibility of contractors for being awarded compensation on account of statutory revision of minimum wages was considered by the Supreme Court. In this case, the arbitrator had allowed the claim of compensation by the contractor and proceeded to lay down the formula for escalated prices that would be payable to the contractor, which was different from the price variation formula existing in the contract. The Supreme Court observed that the arbitrator could have awarded the price escalation only according to the formula present in the contract and that he exceeded his authority by framing a revised formula. Even though the arbitrator's decision was struck down owing to his lack of authority, what can be surmised from the Supreme Court's judgment is that price variation can be claimed when there is an increase in labour costs attributable to an increase in minimum wages.

Further, in *Hindustan Construction Co. v. Union of India,*[32] a similar case was decided by the High Court of Bombay wherein the contractor's claim for recovering compensation due to the revision of minimum wages by the State Government was allowed by the arbitrator. The Court struck down the arbitrator's decision as the terms of the arbitration agreement had clearly made this an excepted matter. Here also, the decision seemed to have been unfavourable to the contractor only because the arbitrator exceeded his authority and not because such an escalation could not have been claimed.

The position seems to be clearly expounded by the High Court of Bombay in *A2Z Infraservice Ltd. v. Union of India.*[33] In this case, the contract had a clause providing for price variation in the event of an increase in CPI. The claim before the Court was whether the price variation computed according to this clause would

[31] Associated Engineering Co v. Government of Andhra Pradesh, AIR 1992 SC 232.
[32] Hindustan Construction Co. v. Union of India, 2007 (1) MhLJ 673.
[33] A2Z Infraservice Ltd v. Union of India, MANU/MH/1014/2018.

be sufficient even in the case of an increase in minimum wages since it is also a step taken in furtherance of an increase in CPI. However, the Court categorically expounded that compensation payable to contractors cannot be computed according to the already existing price variation clause and that it should incorporate the increased minimum wages. Further, in *AG Enviro Infra Projects Pvt Ltd. v. State of Maharashtra,*[34] the Court reiterated the position that when there is a statutory revision of minimum wages, the contractor would be entitled to recover a compensation amounting to the additional expenses incurred due to the increased minimum wages.

However, the Supreme Court's decision in *Union of India v. Varindera Constructions Ltd.*[35] paves the way for a new trend. In this case, the special conditions enumerated in a construction contract between the parties clearly had a clause barring recovery of reimbursement or price escalation owing to an increase in labour wages during the subsistence of the contract. There was also an additional clause that contractors would not be entitled to claim compensation for expenses incurred in paying wages in excess of the statutorily prescribed minimum wages. The Supreme Court held that in light of these clear provisions incorporated in the contract, no claims for reimbursement or compensation for wages paid owing to statutory revision of minimum wages could be entertained. With this decision, the Court has ushered in a possibility where Government can do away with paying contractors if a specific clause barring contractors from claiming a reimbursement in the event of price escalation attributable to statutory revision of minimum wages is incorporated in the contract. However, the authors believe that this is not entirely a 'just' principle of contract law. Government usually in the party which decides and pre determines the terms and condition in Tendering contracts. Undue advantage to exclude price variation for minimum wage would violate the essential spirit of labor welfare and social security legislations and may lead to laxity in labor law compliances. Not to forget the loss caused in this labour market driven transaction.

Recently, in *NTPC Ltd. v. Larsen and Toubro Ltd.,*[36] the High Court of Delhi observed that the contractors would be entitled to recover additional amounts on account of an increase in the Basic Minimum Wage rate as the price variation clause in the contract covered only 'Variable Dearness Allowance' within its ambit. However, the case was ultimately decided against the contractors as they could not establish the price variation in terms of actual payments instead of notional terms. The position of law seems to be clear as in a similar case, *Tata Projects Ltd. v. NTPC,*[37] the Court affirmed that contractors were entitled to be

[34] AG Enviro Infra Projects Pvt Ltd. v. State of Maharashtra, MANU/MH/2968/2018.
[35] Union of India v. Varindera Constructions Ltd., (2018) 7 SCC 794.
[36] NTPC Ltd. v. Larsen and Toubro Ltd., MANU/DE/3249/2021.
[37] Tata Projects Ltd. v. NTPC, MANU/DE/3426/2021.

compensated for additional expenditure incurred by them due to increase in basic minimum wage rate.

It is also worthwhile to note that in a 2012 decision *N.J Devani Builders Private Ltd. v. Indian Farmers Fertilizer Cooperative Ltd.,*[38] the High Court of Delhi had decided that if there was a ceiling limit imposed in the contract on the amount recoverable as compensation owing to escalation, then the contractor would not be eligible to obtain amounts beyond the said ceiling. This position seems to be at odds with the jurisprudence that has emerged later. The decisions subsequent to this, which have been surveyed here seem to indicate the Court's inclination to award contractors compensation for increased rates of minimum wages over and above the increase in labour costs that have been already provided in the price variation clause in the contract.

Therefore, it is evident that contractual price variations can be pegged to a statutory enactment like the Minimum Wage Act. Such statutory enactments provide definitive bases upon which the contractual price can fluctuate. Such pegging would also be consonant with principles of public policy by ensuring that workers are paid the statutorily mandated minimum wage amount.

Position in other Jurisdictions

Price variation clauses are a common phenomenon across the globe. The current unanticipated war in Ukraine has had further far-reaching repercussions, with major implications for the industry. The construction industry has been preparing for price increases to continue as COVID-19[39] and other factors have caused global shortages in materials and labour. In this background, it is necessary to examine the variations in price-variation clauses adopted by countries across the world to respond to the arbitrarily fluctuating market. The authors will examine two jurisdictions- the United Kingdom and Germany.

Position in the UK

Categorically, 'lump sum' or fixed price contracts, which include methods for modifying the contract price but typically not for price inflation, make up the majority of agreements in the construction business in the UK.[40] In essence, the contractor gives the employer or client a price for the task and assumes the risk of

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[38] N.J Devani Builders v. Indian Farmers Fertilizers Cooperative Ltd., MANU/DE/5771/2012.

[39] For the Indian Position see Standard Retail Pvt. Ltd. v. M/s G.S. Global Corp., O.M.P (I) (COMM) & I.A. 3697/2020.

[40] *Pricing Structures in Construction Contracts,* LEXIS NEXIS, https://www.lexisnexis.co.uk/legal/guidance/pricing-structures-in-construction-contracts (last visited Feb. 09, 2023).

fluctuating costs.[41] But owing to the huge inflation, the contractual terms have undergone a slight change.

Therefore, to combat the price rises, parties to construction contracts are increasingly employing '*provisional sums*.' These amounts are the estimated costs of works that cannot be fully defined at the time of contracting or works that the employer or customer may decide not to complete, which are included in contract specifications. Further, when performing the work, the contractor typically has the right to amend the provisional sum. The employer or client then has the choice of either ordering an increase in the contract sum to reflect the provisional sum's increase or hiring a different contractor to complete the specific works that were associated with the provisional sum.

The second provision used to deal with the fluctuation in prices in the UK is by way of incorporating a '*fluctuation provision'* as a compensatory clause in a construction contract that allows the price to be adjusted to account for variations in the price of labour or materials during the term of the contract. Cost-plus contracts are also being employed to address major increases in material prices. In this case, the contractor receives payment for the real expenses of the project's plant, materials, and labour, plus an additional sum to cover the contractor's overhead and profit.[42] Therefore, the contractor might charge the client or employer any price increases.

Position in Germany

The German legal system has historically been reluctant to adjust contract prices, evident from its hesitancy following the oil crisis of the 1970s.[43] The Federal Budget Act now recognizes that it is possible that current events could significantly alter the common assumptions to the point where maintaining the agreed prices would be intolerable, giving the contractor the right to request a price adjustment.[44] In the present scenario, it largely depends on the specific circumstances. The Act states that a price adjustment is permissible without the contractor's impending insolvency resulting from the execution of the contract, but it is not sufficient if the higher material prices only consume the calculated profit. As a result, the field is open and the contractor is fully exposed to the risk of

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[41] Hendrickson Chris, *Construction, Pricing, and Contracting Project Management for Construction* (2008), https://www.cmu.edu/cee/projects/PMbook/.

[42] Cardenas Emanuel, *Cost plus free contracts in the era of CoVID-19*, DLA Piper (Nov. 30, 2020), https://www.dlapiper.com/en/uk/insights/publications/2020/11/pgi-issue-4/cost-plus-fee-contracts/.

[43] Cesaratto, Sergio & Antonella Stirati *Germany and the European and Global Crises*, 39 INT'L J. POL. ECO., 56-58 (2010).

[44] Stahl, Harald, *Price Adjustment in German Manufacturing: Evidence from Two Merged Surveys*, 31 MANAGERIAL AND DECISION ECONOMICS, 67–92 (2010).

contract termination if the price adjustment is unable to resolve the issue at hand or is rejected by the client.[45]

Further, German budgetary law entitles the contracting authorities to agree to changes in contract provisions under certain conditions. According to Section 58 of the Federal Budget Act, the contracting authority may agree to a contract modification if such an amendment will not cause the Federal Republic of Germany any economic disadvantage or if the contractor would suffer unreasonable hardship. This has to be evaluated by the authority on a case-by-case basis.[46]

The analysis of the legal remedies in these two jurisdictions demonstrates the increasing adaptation of contracts to include different variations of price escalation clauses. The legal developments from these areas could be used to inform Indian jurisprudence on the same.

Additional Legal Remedies available

The principle of 'Quantum Meruit' which describes the extent of liability in a contract implied by law can be relied upon. According to the legal principle of Quantum Meruit, no one should be forced to pay more than the worth of the goods or services transferred, nor should anybody else be permitted to obtain more than that amount. [47] It shares a close connection with the equitable notion of unjust enrichment. Furthermore, under the law of contracts, a party is believed to have received an 'unjust enrichment' if he has received a benefit or an advantage at the benefit of another. In this case, the Courts can compel the party who has unjustly enriched to make restitution of the benefit to the person to whose detriment it has been made. These principles are reflected in Section 70 of the Indian Contract Act, 1872 which provides that if a party to a contract, who has done additional work for another, not intending to do it gratuitously and the other party has obtained benefit therefrom, the former is entitled to compensation for the additional work covered by the contract. Under this Section, payment can also be claimed for work done beyond the terms of the contract, when the benefit of the work has been availed by the other party.

If these two principles- *Unjust Enrichment* and *Quantum Meruit*- are applied in the hypothetical scenario enlisted above, the Supplier would be entitled to be

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[45] Essen Michelle, *Construction contracts: drafting for price inflation – views from the UK and Germany*, Womble Bond Dickson (May 19, 2022), https://www.womblebonddickinson.com/uk/insights/articles-and-briefings/rebuild-construction-contracts-drafting-price-inflation.

[46] Dr. Scherer Christian, *CMS Expert Guide on Rising Raw Material Prices in Germany*, CMS (April 12, 2022), https://cms.law/en/int/expert-guides/cms-expert-guide-on-rising-raw-material-prices/germany.

[47] *See* H O Hunter & J W Carter, *Quantum Meruit and Building Contracts,* 2 J. CONTRACT L. 95-114 (1989).

compensated in lieu of the additional charges that it has incurred while meeting the terms of the contractual obligation in lieu of the law stipulated in Section 70. This case can be presented one of unjust enrichment in as much as the Government reaped in monetary benefits by procuring paper from the Supplier for the same rates even though there was a surge of 50-60 % in the market prices. However, it is important that parties continues their respective business obligations and resolution of the difference on price variation is allowed on the principles of 'reasonability' and 'justice' to the affected party. Cases law on quantum meruit needs more jurisprudential applicability so as to decide substantial performance and not necessarily award the same as remedies for breach of contract.

Conclusion

Incorporation of a Price Variation clause is highly advisable so as to ensure that parties do not suffer losses owing to fluctuation in the market prices of a commodity. However, in Government contracts in India, this is highly unlikely. This is often justified on the ground that it is likely to hand over discretionary power to the tender accepting authority and provide undue favor to the contractor. However, an absence of a Price Variation clause or a stipulation to the effect that prices shall remain fixed throughout the duration of the contract would not leave parties without any remedy. Courts have also taken a proactive stance towards the tenderers in Government Contracts and have enabled them to claim price escalation or recover compensation in lieu of the additional amount of money levied from them owing to an increase in market prices. Interpretations like these are also favourable for the Government as it would also be in a position to take advantage of a decrease in prices of commodities and save public funds by paying proportionately revised rates to contractors, especially in Public Private Partnership contracts and long term contracts, which is currently is the trend in tendering.

The authors in this paper have outlined several remedies to rectify the problems associated with fluctuating market prices of commodities. One of them is pegging the contractual price to an index or statutory enactment. This would encompass daily fluctuations and would mitigate loss almost entirely. The authors have also argued that price variation clauses are more feasible alternatives to the frustration of contracts, as they prevent widespread loss to the Government. Further, the legal framework imposed by the General Financial Rules has been summarized. The status of price variation clauses in foreign jurisdictions, namely Germany and the United Kingdom has also been examined briefly. Finally, the authors have discussed a few alternative legal remedies available to suppliers.

This analysis has also brought us to an understanding that price variation clauses are always amenable to judicial review. There is no straight-jacket formula to determine whether a particular clause is ousted from the jurisdiction of the inns of the Court of law. Therefore, a dispute that springs from a price variation clause shall primarily be adjudicated based on the facts of the case and not solely upon the precedents as laid down in law. Thus, uncertainty is the biggest factor that governs

such clauses, where the parties have almost negligible influence over them owing to external control exerted by market forces. The position of law that emerges is that the matter of price variation in Government contracts is mostly adjudicated on the basis of facts and, therefore may be subject to different interpretations in varied circumstances. During such adjudication, courts should acknowledge the myriad factors and stakeholders- primarily the citizens- involved in the issue. This will allow the courts to be perceptive to matters of governance.