SUPREME COURT OF INDIA **REPORTABLE**

Bench: Justice Dipankar Datta and Justice S. Ravindra Bhat.

Date of Decision: 19 October 2023.

CIVIL APPELLATE JURISDICTION

CIVIL APPEAL NO……/2023
[ARISING OUT OF SLP (CIVIL) NO. 8791/2020]

M/S UNIBROS **…APPELLANT**

Versus

ALL INDIA RADIO **…RESPONDENT**

Section, Acts, Rules, and Articles:

Section 34, 37 of the Arbitration and Conciliation Act, 1996

Indian Contract Act, 1872

Subject: Challenge to an arbitral award regarding a delay in the execution of a construction contract and a claim for loss of profit due to the delay. The judgment primarily focuses on whether the second arbitral award was in conflict with the public policy of India.

Headnotes:

Civil Appeal – Challenge to arbitral award – Delay in execution of construction contract – Claim for loss of profit due to delay – Arbitrator awarded loss of profit – First award set aside by High Court – Second award for loss of profit maintained by Arbitrator – Challenge to second award – Whether the second award in conflict with the public policy of India – Public policy includes compliance with fundamental policy of Indian law and judicial precedents – Arbitrator ignored binding judicial decision in making second award – Second award in conflict with public policy. [Para 8-14]

Claim for Loss of Profit – Conditions for a claim of loss of profit to succeed – Delay in completion of contract not attributable to claimant – Claimant an established contractor handling substantial projects – Requirement of credible evidence to substantiate the claim of loss of profitability – Failure to establish loss of profit with evidence renders the claim unsustainable. [Para 19]

Arbitral Award – Requirement of evidence to substantiate claims – Award based on no evidence and outrightly perverse – In conflict with public policy as contemplated by Section 34(2)(b) of the Arbitration and Conciliation Act. [Para 20]

Dismissal of Appeal – Lack of merit in the appeal – Cost awarded by the learned Single Judge upheld. [Para 21]

Referred Cases:

- Associated Builders vs. Delhi Development Authority (2015) 3 SCC 49
- Bharat Cooking Coal Limited vs. L.K. Ahuja (2004) 5 SCC 109
- The Project Director, NHAI vs. M. Hakeem and Another (2021) 9 SCC 1
- M/s AT Brij Paul Singh & Ors. vs. State of Gujarat (1984) 4 SCC 59
- McDermott International Inc. vs. Burn Standard Co. Ltd. and Ors (2006) 11 SCC 181
- ONGC Ltd. vs. Saw Pipes Ltd (2003) 5 SCC 705

J U D G M E N T

DIPANKAR DATTA, J.

1. Leave granted.

2. This appeal, at the instance of M/s Unibros ("appellant", hereafter), registers a challenge to the judgment and order dated 9th December, 2019 in FAO (OS) 229/2010 passed by the High Court of Delhi ("High Court", hereafter) dismissing an appeal carried by the appellant under section 37 of the Arbitration and Conciliation Act, 1996 ("the Act", hereafter). *Vide* the impugned judgment, a Division Bench affirmed the judgment and order of a learned Single Judge dated 25th February, 2010 whereby an objection of the All India Radio ("respondent", hereafter) under section 34 of the Act was allowed resulting in setting aside of an arbitral Award dated 15th July, 2002 to the extent it awarded loss of profit to the appellant.

3. The relevant facts, discerned from the records, reveal that the appellant was awarded a work contract by the respondent to carry out construction of Delhi Doordarshan Bhawan, Mandi House, Phase-II, New Delhi. The work was scheduled to commence on 12th April, 1990 and reach completion on 11th April, 1991; however, it suffered a delay of roughly 42½ months and was finally completed on 30th October, 1994. Disputes and differences emerged between the parties owing to such delay, which were subsequently referred to an Arbitrator ("Arbitrator", hereafter) for resolution.

4. The trajectory of the case, leading to the present stage, is set out hereunder:

a) Arbitration proceedings having been initiated, the Arbitrator *vide* award dated 11th February, 1999 ("First Award", hereafter) decided various claims and counter-claims filed by the parties. Claim Nos. 10, 11, and 12 were collectively addressed under section 73 of the Indian Contract Act, 1872 ("Contract Act"), as they all centred around the issue of delay and the resultant losses.

Vide Claim No. 10, the appellant claimed a sum of Rs. 50,00,000.00 (Rupees fifty lakh) owing to the marked escalation in prices/rates for the work executed beyond the stipulated contract period. *Vide* Claim No. 11, the appellant

implored the Arbitrator to award Rs. 41,00,000.00 (Rupees forty-one lakh) to cover substantial expenses associated with the establishment, machinery, centring/shuttering, and other vital aspects of the project. Additionally, *vide* Claim No. 12, the appellant urged that a compensation of Rs. 2,00,00,000.00 (Rupees two crore) be granted as redress for the loss of profit endured due to the appellant's protracted retention on the contract without any corresponding increase in monetary benefits earned. Despite the Arbitrator's rejection of Claim Nos. 10 and 11, the appellant was awarded a sum of Rs. 1,44,83,830 (Rupees one crore, forty-four lakh, eighty-three thousand, eight hundred and thirty) towards

Claim No. 12, along with an interest of 18% per annum under Claim No. 13 from 12th May, 1997 to the date of actual payment. The Arbitrator supported this award based on the undisputed fact that the delay in completing the work beyond the stipulated contract period was caused by the respondent and against the stipulated contract period of 12 months, the appellant was retained by the respondent for the execution of the work for an additional period of 3½ years leading to loss of the appellant's profit earning capacity during the said extended period. The loss of profit was worked out based on a profit allowance of 7½% per year, which the Arbitrator held to be reasonable in a civil works contract. Applying Hudson's formula, the Arbitrator arrived at the final compensation for loss of profit, the computation of which is outlined below:

Period of delay	42.5 months
Contract value	Rs. 5,45,27,386.00
Contract period	12 months
Contractor's profit (7 ½ % per year)	Rs. 40,89,554.00
Contractor's expected profit per month	Rs. 3,40,796.00
The total amount of loss of profit	The total period of delay x Contractor's expected profit per month **Rs. 1,44,83,830.00**

b) Aggrieved by the aforesaid First Award, primarily to the extent it awarded Rs.1,44,83,830.00 towards loss of profit to the appellant, the respondent filed an objection under section 34 of the Act before the High Court impugning the decision pertaining to Claim Nos. 12 and 13. *Vide* judgment and order dated 20th May, 2002, the First Award was set aside and the aforesaid claims were

remitted to the Arbitrator for re-consideration and for passing a fresh award. The operative part of the judgment passed by the learned Single Judge reads thus:

"24. *** Except for placing on record the Hudson's formula and a passage from the book law (sic, Law) on Building and Engineering Contracts, no other evidence is placed on record by the respondent to show that the profit percentage as claimed towards loss of profit was a realistic one at that times and consequently there was no change in the market and also that the work of at least the same general level of profitability would have been available to the respondent at the end of the stipulated contract period. Therefore, evidence in respect of the said claim appears to be definitely not available on record. In absence of any credible evidence and when claims under Claim Nos. 10 & 11 were rejected on the ground that no sufficient evidence had been placed on record by the respondent indicating increase in the prices/rates for the work executed after the stipulated contract period and also on account of establishment, machinery, centering/shuttering etc., Claim No.12 was allowed by the arbitration (sic, arbitrator) without even considering whether the respondent has placed credible and reliable evidence as required to be proved. ***

25. *** Not only there was lack of credible and required evidence placed on record by the respondent in support of Claim No.12 as set out in the extracts from the book Law of Building and Engineering Contracts, and (sic) the arbitrator also took into consideration such factors which could not and should not be (sic, have) influenced his mind. Therefore, the award was passed by the arbitrator against the fundamental policy of Indian Law attracting the provisions of Section 34 (2)(b) (ii) of the Act. I set aside the award given by the arbitrator against Claim No.12 and remit the same for re-consideration by the arbitrator and to pass a fresh award in respect of the said claim without being in any manner influenced by such factors and on the basis of the evidence available on record. Since the award passed by the arbitrator is set aside to the aforesaid extent, the award of interest in Claim No. 13 in respect of the amount of Claim No. 12 also stands set aside and quashed and the same are remitted for reconsideration and decision. Subject to the aforesaid modifications in the award, the remaining part of the award is upheld."

(emphasis ours)

c) The Arbitrator passed a fresh award dated 15th July, 2002 ("Second Award", hereafter) maintaining the award for loss of profit and interest to the appellant *vide* First Award. By referring to the communications between the parties, the Arbitrator reiterated that the respondent had failed to provide the complete site and drawings within the stipulated contract period, leading to delays. As per established legal principles, the party responsible for the breach of the contract is liable for reasonably foreseeable losses. Considering the appellant's status as an established contractor, handling substantial projects,

the Arbitrator inferred that it was reasonable to assume earning of expected profits elsewhere by the appellant. Employing the doctrine that within a contract, gains prevented qualify as loss sustained, the Arbitrator observed that the appellant was not required to establish the exact amount of gain or loss with absolute certainty; instead, presenting fairly persuasive and the best available evidence under the particular circumstances of the case would suffice.

d) The respondent filed a petition under Section 34 of the Act, seeking to set aside the Second Award. The learned Single Judge of the High Court *vide* judgment and final order dated 25th February 2010 allowed the objection under Section 34 and rejected the appellant's claim under Claim No. 12 with an observation that there was no sufficient evidence presented by the appellant to establish the claimed loss of profit; the lack of records regarding the alleged utilization of men, material, machinery, overheads, and other resources in the contract performance that could have otherwise been used for other profitable contracts raised doubts about the legitimacy of the claimed losses under Claim No. 12. With an observation that the Union of India was forced into litigation due to the appellant's misconceived claim, the Single Judge awarded costs of Rs. 50,000.00 (Rupees fifty thousand) in favour of the respondent, payable within four weeks from the date of the final order and interest of 9% per annum in case of non-compliance. Findings returned by the learned Single Judge are extracted below:

"4. I have gone through the entire Award. The Award … as a loss under this Claim 12.

5. In this view of the … in the arbitration proceedings.

7. *** I accept the objections to the Award and the Award dated 15.7.2002 of the Arbitrator is set aside and the claim of the contractor under Claim 12 will accordingly stand dismissed. In the facts and circumstances of the case, I award costs of Rs.50,000/- in favour of the petitioner and against the

respondents… Accordingly, in the facts of the present case, I deem it fit to award interest on the costs."

e) Dissatisfied with the findings of the learned Single Judge, the appellant preferred an appeal before the Division Bench of the High Court under Section 37 of the Act. While dismissing the appeal *vide* the impugned judgment, the Division Bench was of the view that no evidence was produced on behalf of the appellant to support the plea of loss of profit during the period when the work was prolonged; findings returned by the Arbitrator are, therefore, contrary to law, more particularly the Contract Act which governs matters related to loss of profit. Having found no infirmity or illegality, the judgment of the learned Single Judge was confirmed, and the appeal was dismissed, being devoid of any merit.

SUBMISSIONS OF THE PARTIES

5. Taking exception to the decisions of the Single Judge as well as the Division Bench, Mr Sameer Rohatgi, learned counsel appearing on behalf of the appellant advanced the following submissions:

a) The learned Arbitrator had arrived at a just and reasoned conclusion after carefully perusing the materials and evidence on record and in the absence of any perversity or caprice, the courts cannot interfere with the award. Relying on ***Associated Builders vs. Delhi Development Authority*** [1], learned counsel submitted that the arbitrator is the sole judge of the quality and quantity of evidence and the High Court, under section 34 of the Act, cannot act as a first appellate or a revisional court by interfering with arbitral awards in the absence of perversity.

[1] (2015) 3 SCC 49

b) ***Bharat Cooking Coal Limited vs. L.K. Ahuja***[2] was placed in support of the contention that the High Court has a limited scope of interference in awards passed by an arbitrator. Learned counsel placed reliance on the specific excerpt of this Court's decision, which is extracted below for facility of reference:

"11…When the arbitrator has applied his mind to the pleadings, the evidence adduced before him and the terms of the contract, there is no scope for the court to reappraise the matter as if this were an appeal and even if two views are possible, the view taken by the arbitrator would prevail. So long as an award made by an arbitrator can be said to be one by a reasonable person no interference is called for. However, in cases where an arbitrator exceeds the terms of the agreement or passes an award in the absence of any evidence, which is apparent on the face of the award, the same could be set aside."

c) According to Section 34, an award cannot be modified but can only be set aside under specific grounds outlined in the provision. Unlike the Arbitration Act of 1940, which explicitly allowed for modification, the Act of 1996, modelled on the UNCITRAL Model Law on International Commercial Arbitration 1985, does not grant the court the power to modify awards under Section 34. This aligns with the legislative intent of minimizing judicial intervention in arbitral awards. Reliance in support of the said contention was placed on ***The Project Director, NHAI vs. M. Hakeem and Another***[3];

d) ***M/s AT Brij Paul Singh & Ors. vs. State of Gujarat***[4] was relied upon to submit that a contractor is entitled to damages for loss of expected profit on the remaining work and only a broad evaluation is required to assess the amount of damages instead of going into minute details; and

e) Hudson's formula has received legal acceptance and is generally used by courts and other judicial bodies in awarding loss of profit. Learned counsel further submitted that Hudson's formula works on the numbers and figures contemplated in the contract as envisaged by the parties at the time of signing

[2] (2004) 5 SCC 109
[3] (2021) 9 SCC 1
[4] (1984) 4 SCC 59

of the contract rather than the actuals during the ongoing work. Therefore, the actual number of men, material and machinery allocated by the appellant for the work bears no relevance whatsoever in calculating the loss of profit incurred by the appellant due to the breach of contract by the respondent, else Hudson's formula would be rendered redundant. Reliance was placed on ***McDermott International Inc. vs. Burn Standard Co. Ltd. and Ors***[5] to draw support.

6. Mr. Sanjay Jain, learned Additional Solicitor General ("ASG", hereafter) appearing on behalf of the respondent submitted that the arbitral award was passed in an arbitrary and whimsical manner, and was rightly rejected both by the Single Bench and the Division Bench. Urging this Court to dismiss the appeal and confirm the decisions of the Division Bench as well as the Single Judge, the ASG advanced the following submissions:

a) The present case being that of delay simpliciter, Hudson's formula will have no application to award any amount for loss of profit without the aggrieved party leading any evidence as a *condition precedent* to the application of the said formula.

b) The application of Hudson's formula hinges upon three essential conditions:

i. Firstly, the profit awarded to the contractor must have been realistically attainable elsewhere had it been free to leave the contract at the appropriate time;

ii. Secondly, the contractor should not have consistently underestimated his costs during pricing, ensuring that the profit percentage was genuinely viable at that point;

iii. Thirdly, there should have been no subsequent changes in the market, such that work of a comparable level of profitability would

[5] (2006) 11 SCC 181

have been available to the contractor at the time of the conclusion of the contract.

c) It was further submitted that to fulfil the aforesaid conditions, satisfactory and cogent evidence is a *sine qua non* even if the loss is not of a remote or imaginary nature. In the absence of cogent evidence substantiating a genuine loss of profit or opportunity, it would be unjustifiable to permit the contractor to capitalize solely on the application of a formula.

d) In the present case, the ASG submitted, no evidence was led by the appellant, far less, any credible or cogent evidence, to prove that it was capable of earning such price elsewhere by way of any other contract that was available to it at that time, which it could not execute due to prolongation of the contract; such an award, being perverse, conflicts with the public policy of India under Section 34(2)(b)(ii) of the Act.

e) The Arbitrator's actions present a perplexing situation: while dismissing Claim Nos. 10 (compensation for increased prices/rates after the contract period) and 11 (compensation for the establishment, machinery, centring/shuttering, etc.) due to the absence of credible evidence, the Arbitrator, on the other hand, proceeded to grant damages for loss of profit under Claim No. 12. This prompts a crucial question: If there was insufficient evidence to support Claim Nos. 10 and 11, what other evidence could possibly justify awarding loss of profit under Claim No. 12?

f) Mechanical application of Hudson’s formula would serve no purpose and burden the exchequer was the ASG’s concluding submission.

ANALYSIS AND FINDINGS

7. We have considered the submissions advanced by learned counsel for the parties and also perused the materials on record.

8. The appeal is directed towards dismissal of the appellant's claim for compensation relating to loss of profits (Claim No. 12). It is undeniably established that the appellant's claim for loss of profit stems from the delay attributed to the respondent in completing the project. It is further evident that the loss of profit sought in the present case is primarily based on the grounds that the appellant, having been retained longer than the period stipulated in the contract and its resources being blocked for execution of the work relatable to the contract in question, it could have taken up any other work order and earned profit elsewhere.

9. The contentions advanced on behalf of the appellant tasks us to resolve a recurring issue which, while not unprecedented, has consistently confronted the courts leading it to navigate various circumstances under which a claim for loss of profit may be allowed in cases of delay simpliciter in the execution of a contract.

10. However, the contentions so raised, need not detain us for too long. Quite apart from the appeal raising the question as to whether a claim on account of loss of profit is liable to succeed merely on the ground that there has been delay in the execution of the construction contract, attributable to the employer, the question that first needs to be answered on facts and in the circumstances is whether the Second Award is in conflict with the public policy of

India (as held by the learned Single Judge, since affirmed by the Division Bench) .

11. What would constitute "public policy of India" has been lucidly explained by this Court in ***ONGC Ltd. vs. Saw Pipes Ltd***[6]:

> "31…, the phrase 'public policy of India' used in Section 34 in context is required to be given a wider meaning. It can be stated that the concept of public policy connotes some matter which concerns public good and the public interest. What is for public good or in public interest or what would be injurious or harmful to the public good or public interest has varied from time to time. However, the award which is, on the face of it, patently in violation of statutory provisions cannot be said to be in public interest. Such award/judgment/decision is likely to adversely affect the administration of justice."

12. Subsequent decisions of this Court have interpreted "public policy of India" to include, among others, compliance with fundamental policy of Indian law, statutes and judicial precedents, need for judicial approach, compliance with natural justice, Wednesbury unreasonableness and patent illegality. We may refer to the decision in ***Associated Builders*** *(supra)* in this behalf.

13. Having read the Second Award, we have no hesitation to hold that it fares no better than the First Award, for, it is equally in conflict with the public policy of India. We have noticed from the order dated 20th May, 2002 of the learned Single Judge that while remitting Claim No.12 for reconsideration, the Arbitrator was warned not to be influenced by the factors that weighed in his mind while making the First Award. The Arbitrator was also required to proceed only on the basis of the evidence on record. Yet, regrettably, what we find is that the Arbitrator went on to ignore the judicial decision of the High Court with impunity. He once again emphasized on delay caused by the respondent in completion of the works entrusted to the appellant by not providing complete site and drawings within the stipulated contract period and that non-

[6] (2003) 5 SCC 705

handing over of site certainly constituted fundamental breach of contract vitiating the entire contract. He then referred to Hudson's espousal of fundamental breach of contract which, according to him, was the standard text in all engineering and building contracts. It is, therefore, apparent that the factors which weighed in the Arbitrator's mind in the first round and the second round are one and the same. To avoid any charge of being branded as a mirror image of the First Award insofar as Claim No.12 is concerned, the Second Award appears to have been expressed in language and form different from the earlier one without, however, there being any change in substance.

14. It is elementary, though it has to be restated, that a judicial decision of a superior court, which is binding on an inferior court, has to be accepted with grace by the inferior court notwithstanding that the decision of the superior court may not be palatable to the inferior court. This principle, *ex proprio vigore*, would be applicable to an arbitrator and a multi-member arbitral tribunal as well, particularly when it is faced with a judicial decision (either under section 34 or section 37 of the Act) ordering a limited remand. In the wake of authority of judicial determination made by the Courts of law, any award of an arbitrator or a tribunal that seeks to overreach a binding judicial decision, in our opinion, does conflict with the fundamental public policy and cannot, therefore, sustain.

15. Considering the aforesaid reasons, even though little else remains to be decided, we would like to briefly address the appellant's claim of loss of profit. In ***Bharat Cooking Coal*** *(supra)*, this Court reaffirmed the principle that a claim for such loss of profit will only be considered when supported by adequate evidence. It was observed:

"24. ... 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 the work. What he should establish in such a situation is that had he received the amount due under the contract, he could have utilised the same for some other business in which he could have earned profit. Unless such a plea is raised and established, claim for loss of profits could not have been granted. In this case, no such material is available on record. In the absence of any evidence, the arbitrator could not have awarded the same."

(emphasis ours)

16. To support a claim for loss of profit arising from a delayed contract or missed opportunities from other available contracts that the appellant could have earned elsewhere by taking up any, it becomes imperative for the claimant to substantiate the presence of a viable opportunity through compelling evidence. This evidence should convincingly demonstrate that had the contract been executed promptly, the contractor could have secured supplementary profits utilizing its existing resources elsewhere.

17. One might ask, what would be the nature and quality of such evidence? In our opinion, it will be contingent upon the facts and circumstances of each case. However, it may generally include independent contemporaneous evidence such as other potential projects that the contractor had in the pipeline that could have been undertaken if not for the delays, the total number of tendering opportunities that the contractor received and declined owing to the prolongation of the contract, financial statements, or any clauses in the contract related to delays, extensions of time, and compensation for loss of profit. While this list is not exhaustive and may include any other piece of evidence that the court may find relevant, what is cut and dried is that in adjudging a claim towards loss of profits, the court may not make a guess in the dark; the

credibility of the evidence, therefore, is the evidence of the credibility of such claim.

18. Hudson's formula, while attained acceptability and is well understood in trade, does not, however, apply in a vacuum. Hudson's formula, as well as other methods used to calculate claims for loss of off-site overheads and profit, do not directly measure the contractor's exact costs. Instead, they provide an estimate of the losses the contractor may have suffered. While these formulae are helpful when needed, they alone cannot prove the contractor's loss of profit. They are useful in assessing losses, but only if the contractor has shown with evidence the loss of profits and opportunities it suffered owing to the prolongation.

19. The law, as it should stand thus, is that for claims related to loss of profit, profitability or opportunities to succeed, one would be required to establish the following conditions: first, there was a delay in the completion of the contract; second, such delay is not attributable to the claimant; third, the claimant's status as an established contractor, handling substantial projects; and fourth, credible evidence to substantiate the claim of loss of profitability. On perusal of the records, we are satisfied that the fourth condition, namely, the evidence to substantiate the claim of loss of profitability remains unfulfilled in the present case.

20. The First Award was interfered with by the High Court for the reasons noted above. The Arbitrator, in view of such previous determination made by the High Court, could have granted damages to the appellant based on the evidence on record. There was, so to say, none which on proof could have translated into an

award for damages towards loss of profit. A claim for damages, whether general or special, cannot as a matter of course result in an award without proof of the claimant having suffered injury. The arbitral award in question, in our opinion, is patently illegal in that it is based on no evidence and is, thus, outrightly perverse; therefore, again, it is in conflict with the “public policy of India” as contemplated by section 34(2)(b) of the Act.

21. For the reasons aforesaid, we find no merit in this appeal. The same stands dismissed. However, cost awarded by the learned Single Judge is

made easy.