

WELCOME

Contract management

IICA- 28.8.21

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What to expect today

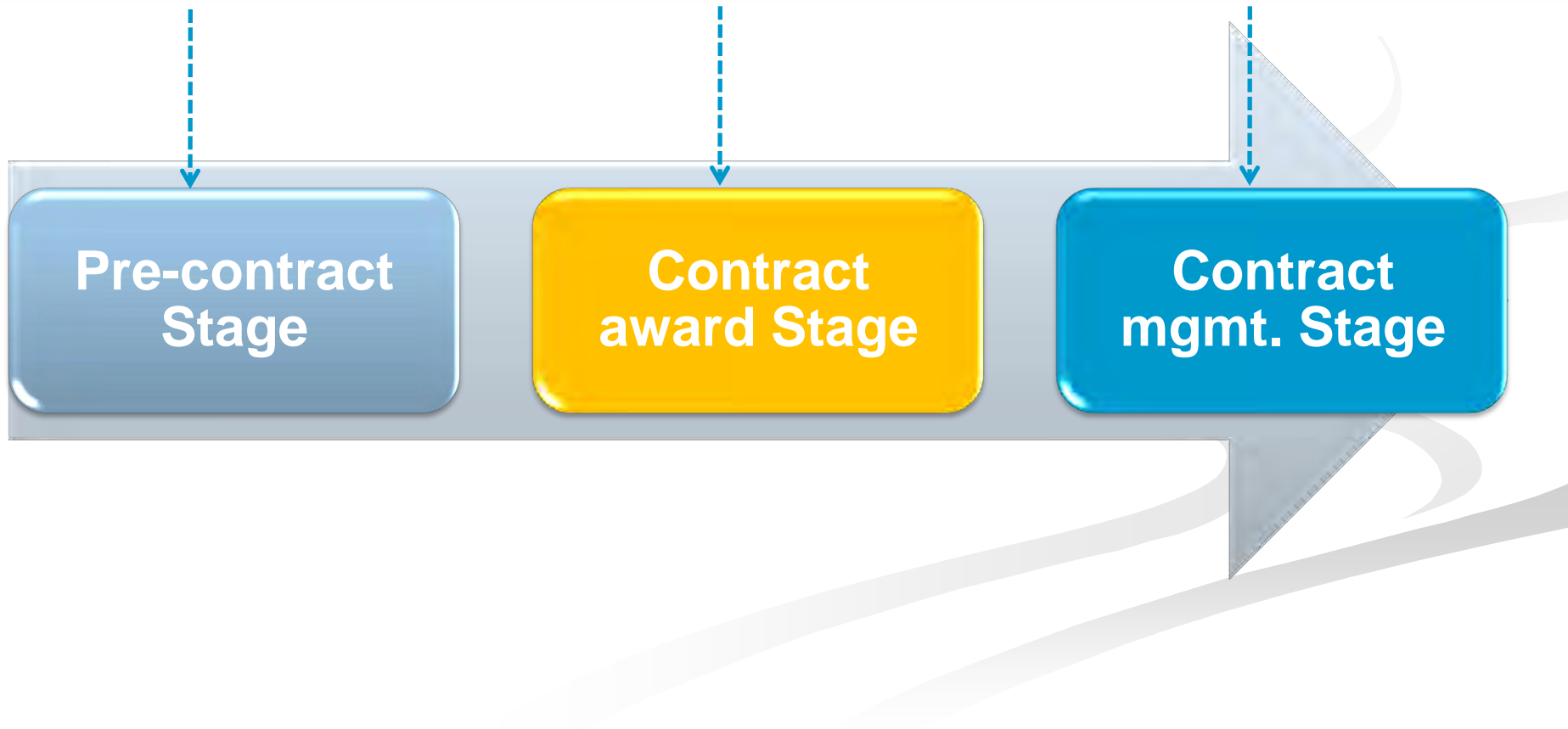
- Monitoring of contract, periodic review
- Contract management- D P extn, FM, Change Management, Amendment, Inspection, Installation, Testing, Commissioning, Payment, Release of performance security
- Delay analysis, LD claim
- Price variation as per PVC
- Termination of contract, remedy for breach of contract
- Dispute resolution- ADR methods
- Arbitration and Conciliation Act
- Steps taken by Govt for timely completion of arbitration

Public Procurement & Contract Management

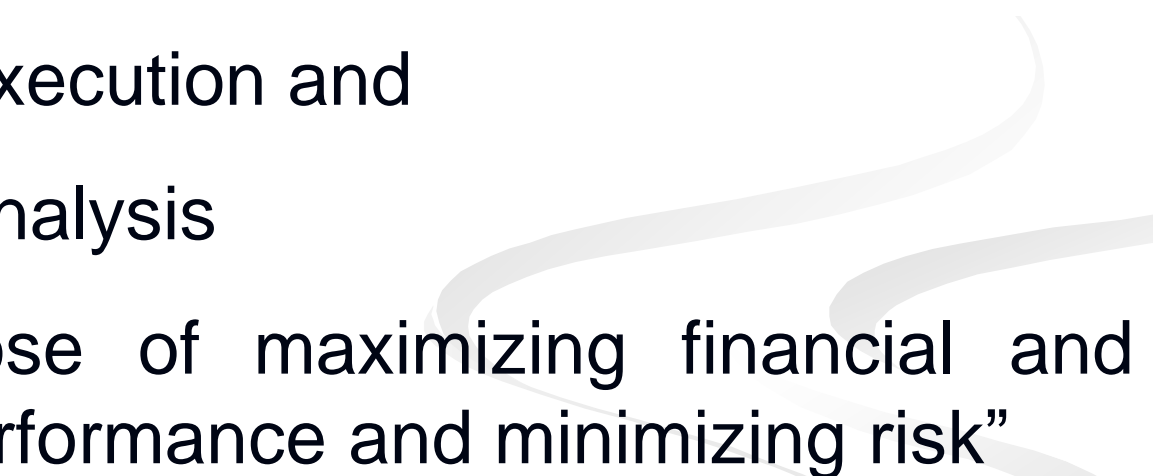
Assessment of need
Proc Planning
Tender invitation

Tender evaluation
Negotiation
Cont award decision

Contract drafting
Contract Mgmt
Dispute resolution

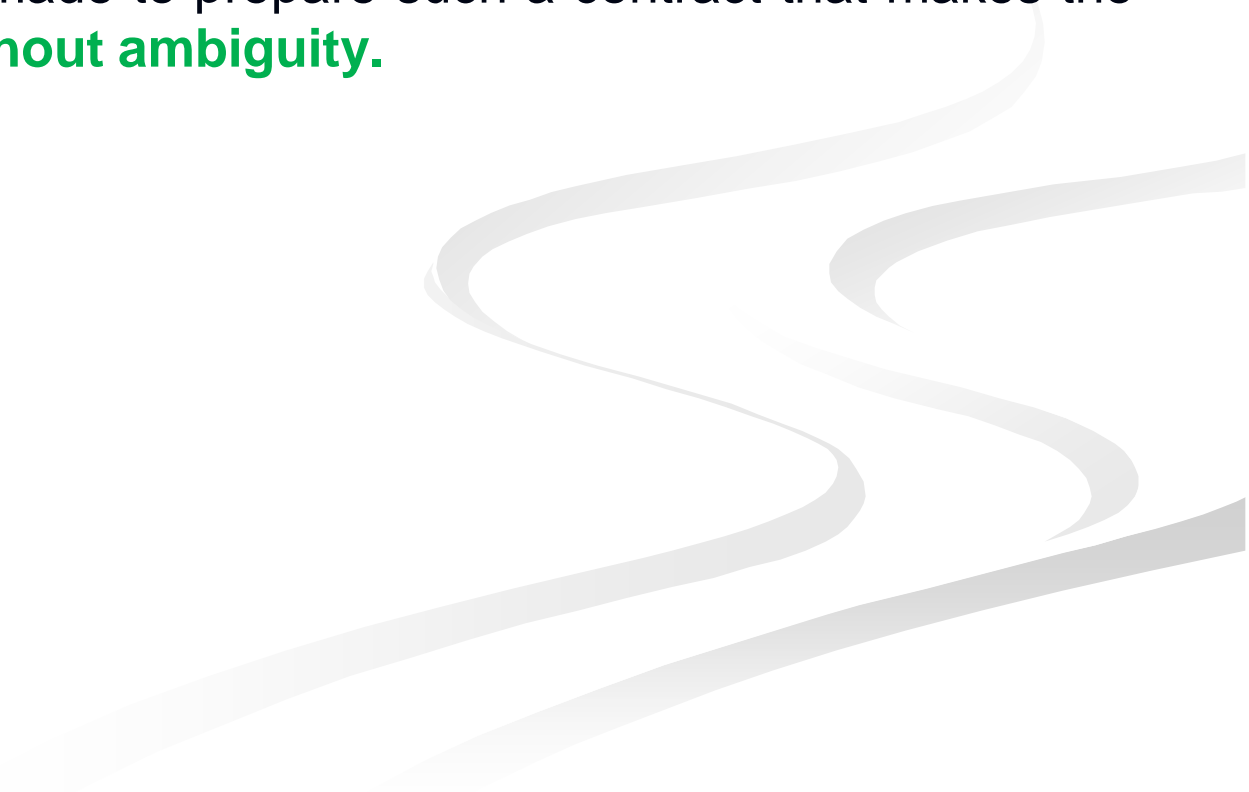


What is contract management

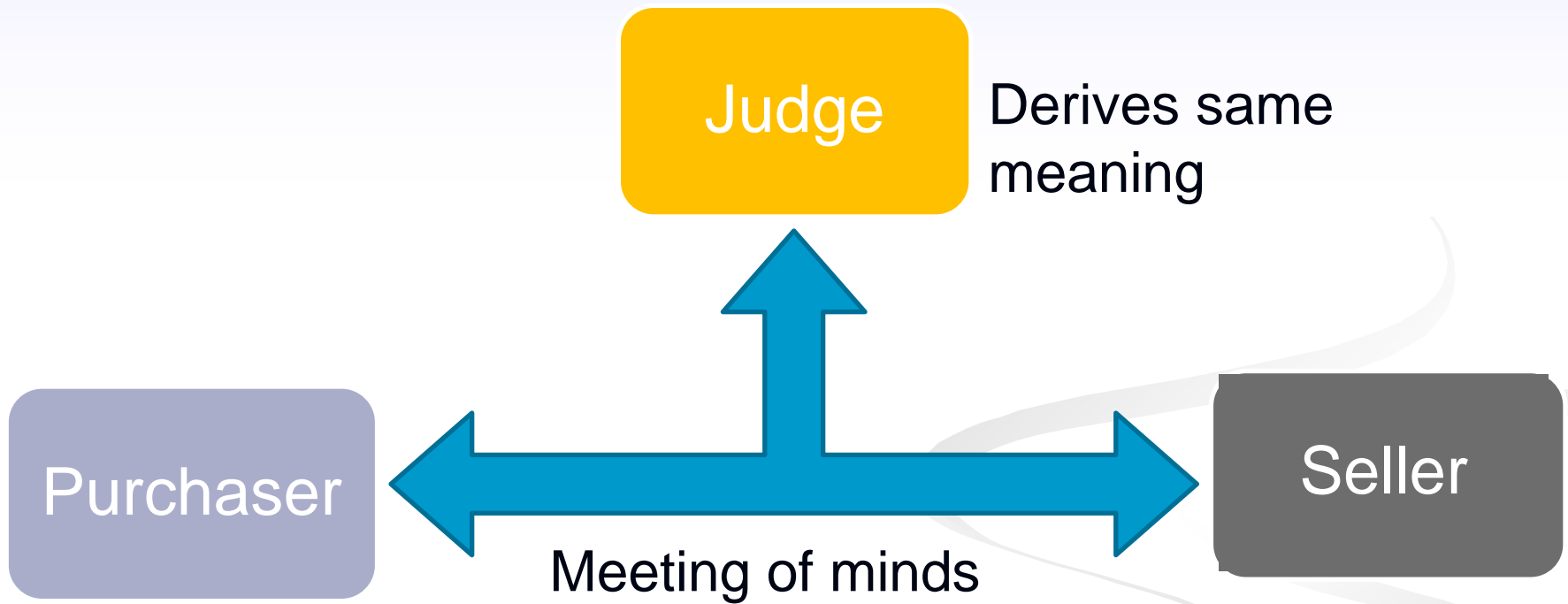
- “It is the process of systematically and efficiently managing
 - Contract creation,
 - Contract execution and
 - Contract analysis
 - for the purpose of maximizing financial and operational performance and minimizing risk”
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Contracts

How to make a good one?

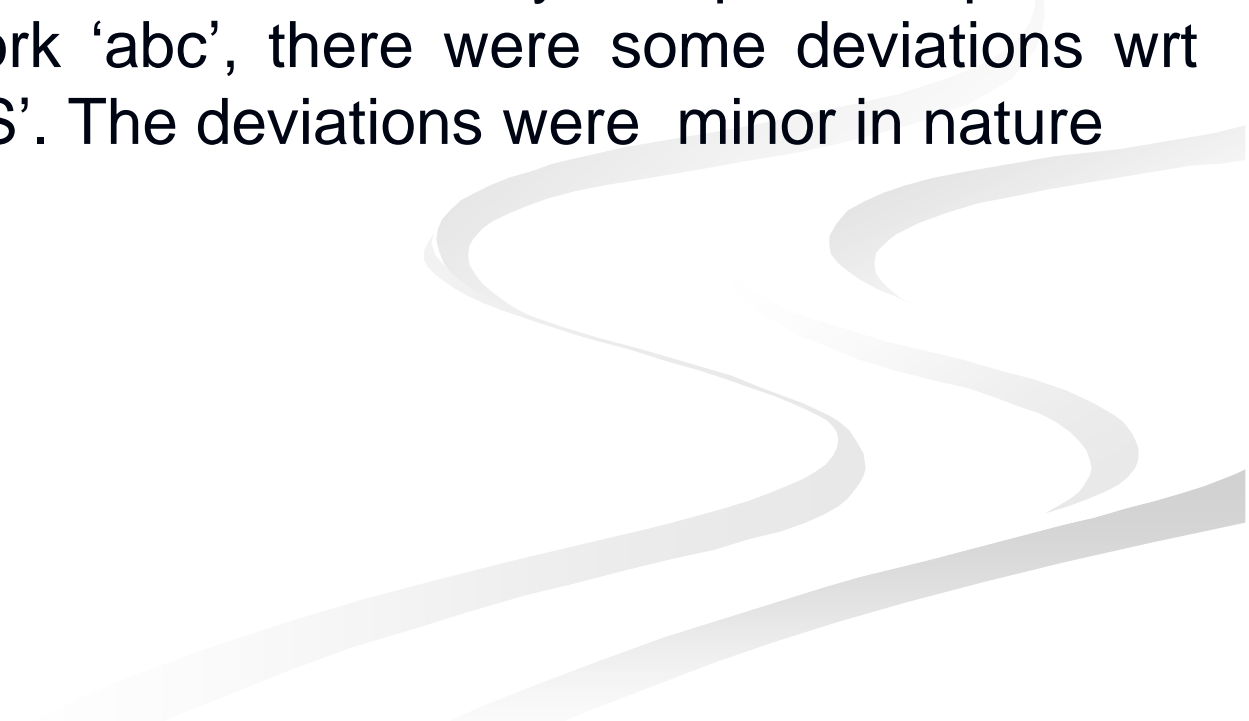
- To make a good contract:
 - **Legal aspects contract** must be kept in mind and
 - Efforts must be made to prepare such a contract that makes the **things clear without ambiguity.**
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Contract drafting



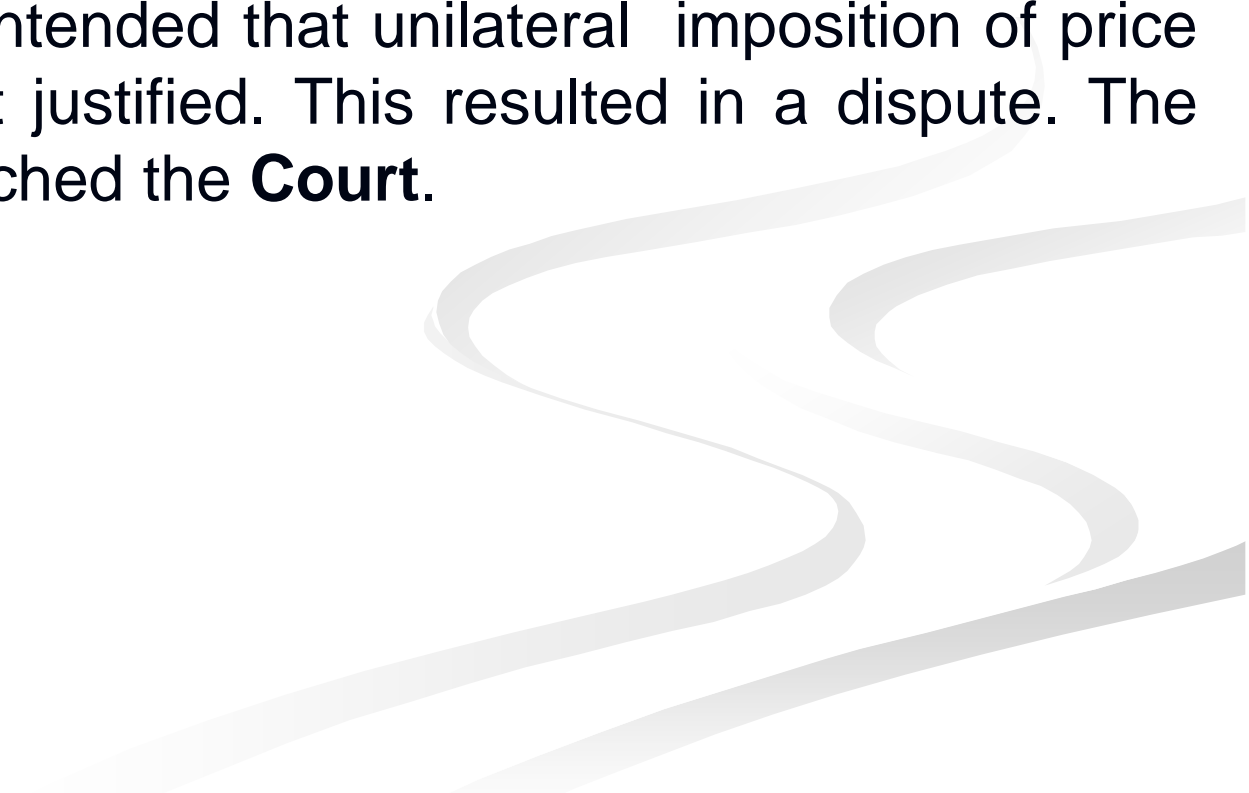
Case Study

Contract Specs

- A project contract specified that
 - “The contractor will perform the work ‘abc’ and the work ‘xyz’ in accordance with the specification S”.
 - The contractor performed the work ‘xyz’ as per the spec. But in the case of work ‘abc’, there were some deviations wrt the specification ‘S’. The deviations were minor in nature
- 

Case Study

Contract Specs

- The purchaser needed to open its office in the buildings urgently. While accepting the deviations, purchaser imposed a price reduction, which was not accepted by contractor.
 - The contractor contended that unilateral imposition of price reduction was not justified. This resulted in a dispute. The contractor approached the **Court**.
 - **You be the judge**
- 

Case Study

Contract price

- In a Project, the three acceptable tenderers offered their prices as follows:
- **L1**- Total civil works- Rs700 crs, Total electrical works- Rs300 crs, Grand total Rs**1000** crs. Discount **+2%**
- **L 2** - Total price-Rs **1025** crs (price after discount)
- **L 3** - Total price-Rs **1028** crs (price after discount)
- The purchaser placed the contract on L1 at Rs1020 crs ($1000+2\%$ ie 20 =1020).

Case Study

Contract DP

- In a high value tender (Rs 100 crs approx), the supplier had offered a firm delivery period as per tender invitation (Global Tender).
- In the delivery clause of the contract , it was stipulated that “Supplies will be completed by May 31(year).” It was incorporated in the delivery clause itself that in case the supplier fails to adhere to this date, liquidated damages will be levied at the rate of 2% per month or part thereof of delayed period subject to a maximum of 10% of contract value.

Case Study

Contract DP

- The supplier failed to make any supply by May 31 (year). They did not make any request for extension to deliver period.
- The purchaser cancelled the contract in Aug (year) and claimed damages alleging breach of contract by the supplier.
- The matter was referred to arbitration.
- **Decide the matter as a Ld Arbitrator.**
- A BIG 'Thank YOU'

Delivery schedule

- Specify when and at what rate the goods are required to be delivered or services to be performed
- Specify the date of commencement and **completion**:
 - Delivery shall commence on Sept 1, 2021 and shall be completed within 4 months, ie by Dec 31, 2021. **Time is the essence of contract.**

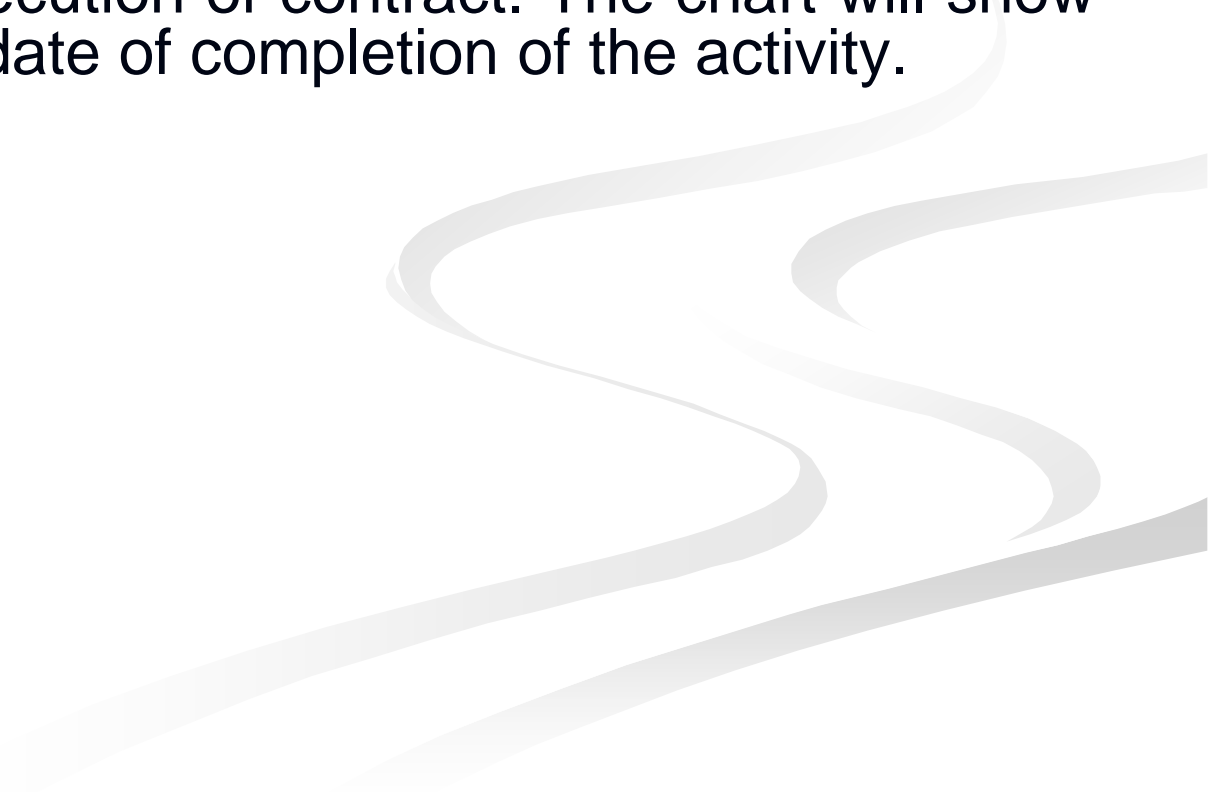
Performance Guarantee

- The contract specifies the amount of performance security and requires it to be submitted within 2/3 weeks.
- The contractors, usually, submit a Bank Guarantee (called Performance Bank Guarantee-PBG) towards performance security which is examined and accepted by the Purchaser if found in order.
- This step is usually linked to Advance Payment
- The Advance Payment as specified in the contract is made upon submission and acceptance of performance security

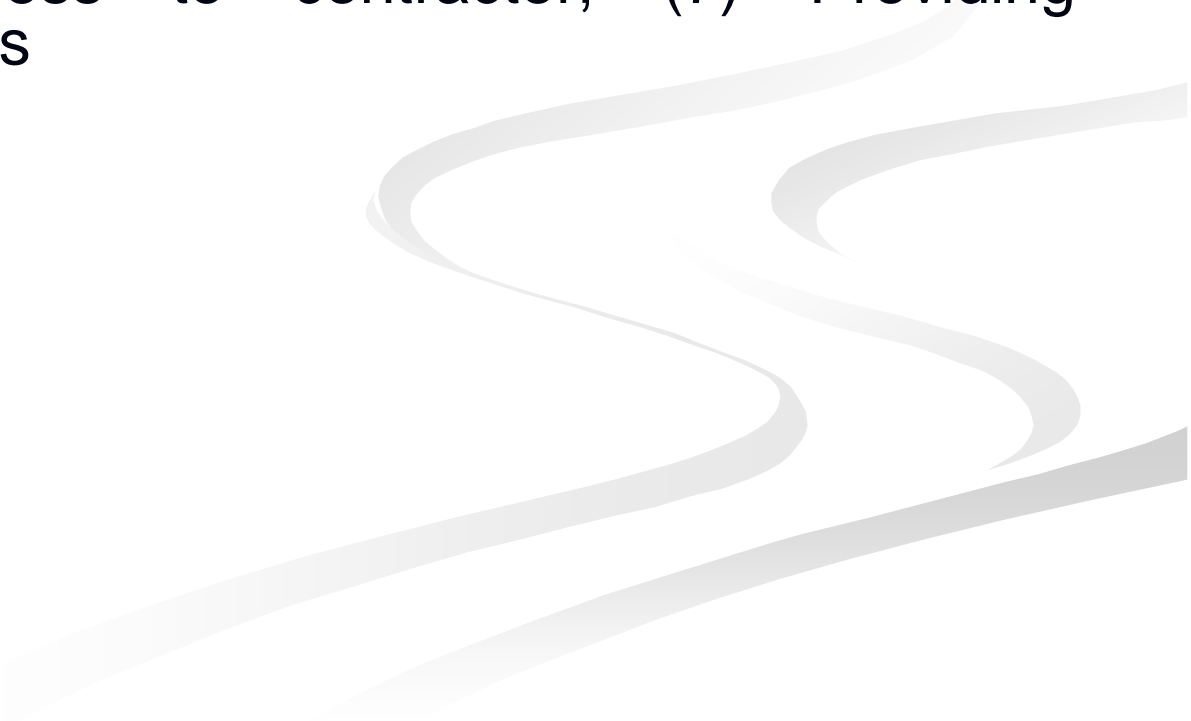
Release of Performance Security

- The Performance Bank Guarantee (PBG) submitted by the contractor towards performance security remains valid for
 - (a) The delivery period including erection & commissioning,
 - (b) The Warranty period and
 - (c) Two months additional period.
- On expiry of the aforesaid period, the PBG is released if the performance of the Equipment is satisfactory and the Purchaser has no Claim against the Contractor

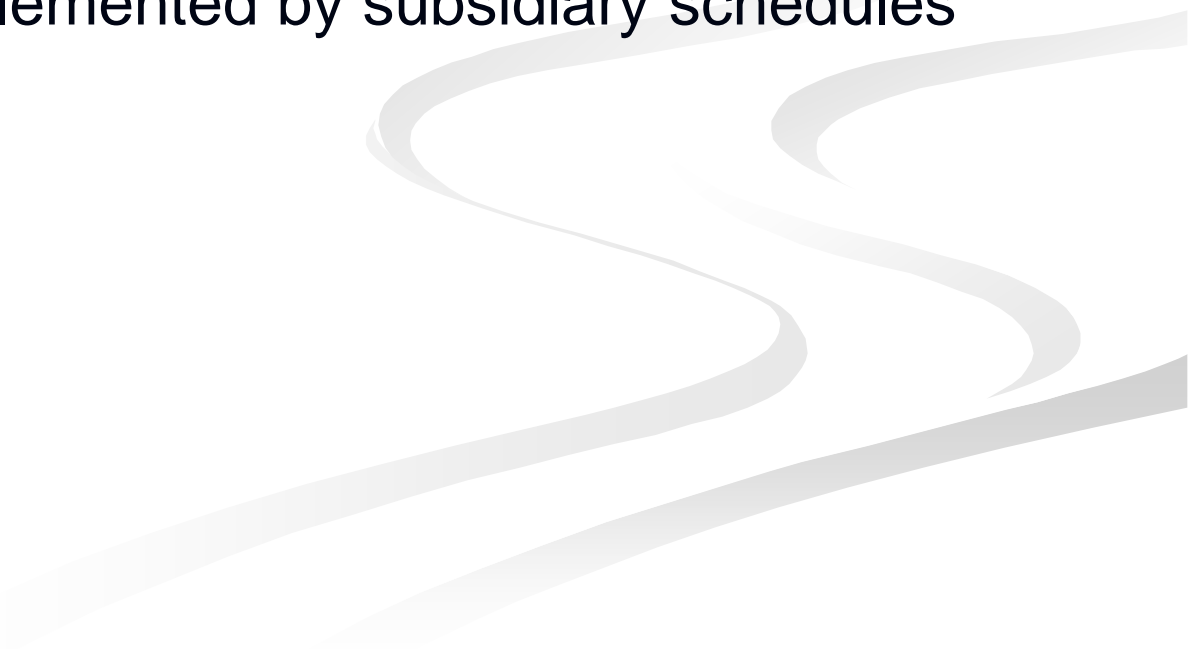
Contract Mgmt- Master Schedule

- Draw a Master Schedule of all the activities in their chronological sequence that have to be performed during the course of implementation of the contract.
 - This can be in the form of a chart to facilitate monitoring of activities for execution of contract. The chart will show the due date and date of completion of the activity.
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Contract Mgmt- Master Schedule

- The right hand side of the chart may be used to denote the time taken by purchaser
 - Some of the activities are: (1) Acknowledgment, (2) Issue of A/L, (3) Arranging clearances/ CDE, (4) Furnishing of PBG, (5) Acceptance of PBG, (6) Providing data/ site access to contractor, (7) Providing equipments/ Utilities
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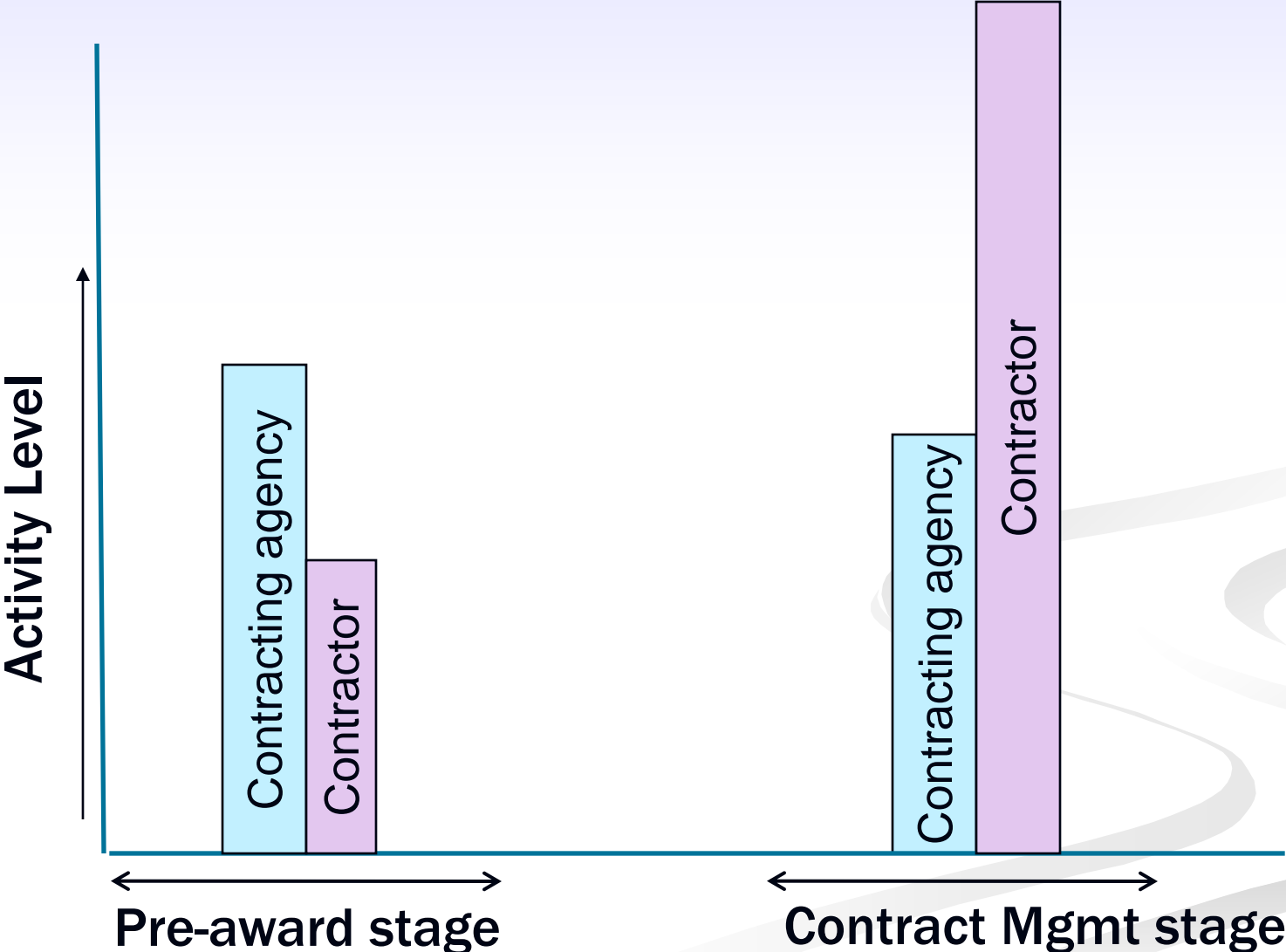
Contract Mgmt- Master Schedule

- (8) Furnishing BG for advance payment, (9) Release of Adv Payment, (10) Submission of Drgs, (11) Approval of Drgs, (12) Letter of credit, (13) Providing technical training, (14) Readiness for inspection, (15) Inspection, (16) Readiness for shipment, (17) nomination of Carrier, (18) Shipment, (19) Shipping docs (20) Port clearance
 - This could be supplemented by subsidiary schedules
- 

Periodic review of contract

- Check whether supplier's performance is as per contract schedule
 - Arrange site visit by your officers located nearer to the supplier's Plant
 - Hold meetings in your office/ at site to monitor progress
 - **Communicate with top management of supplier**
- 

Activities during procurement process




Purchaser's obligations include...

- Provide data
- Approve plans, drgs, design, advance sample
- Provide access to site for works contracts
- Arrange clearances
- Timely release of advance payment
- Provide materials, equipment, utilities
- Opening L/C
- Inspect goods / works
- Provide facilities for erection, commissioning, training
- Timely payment of contractor's invoices

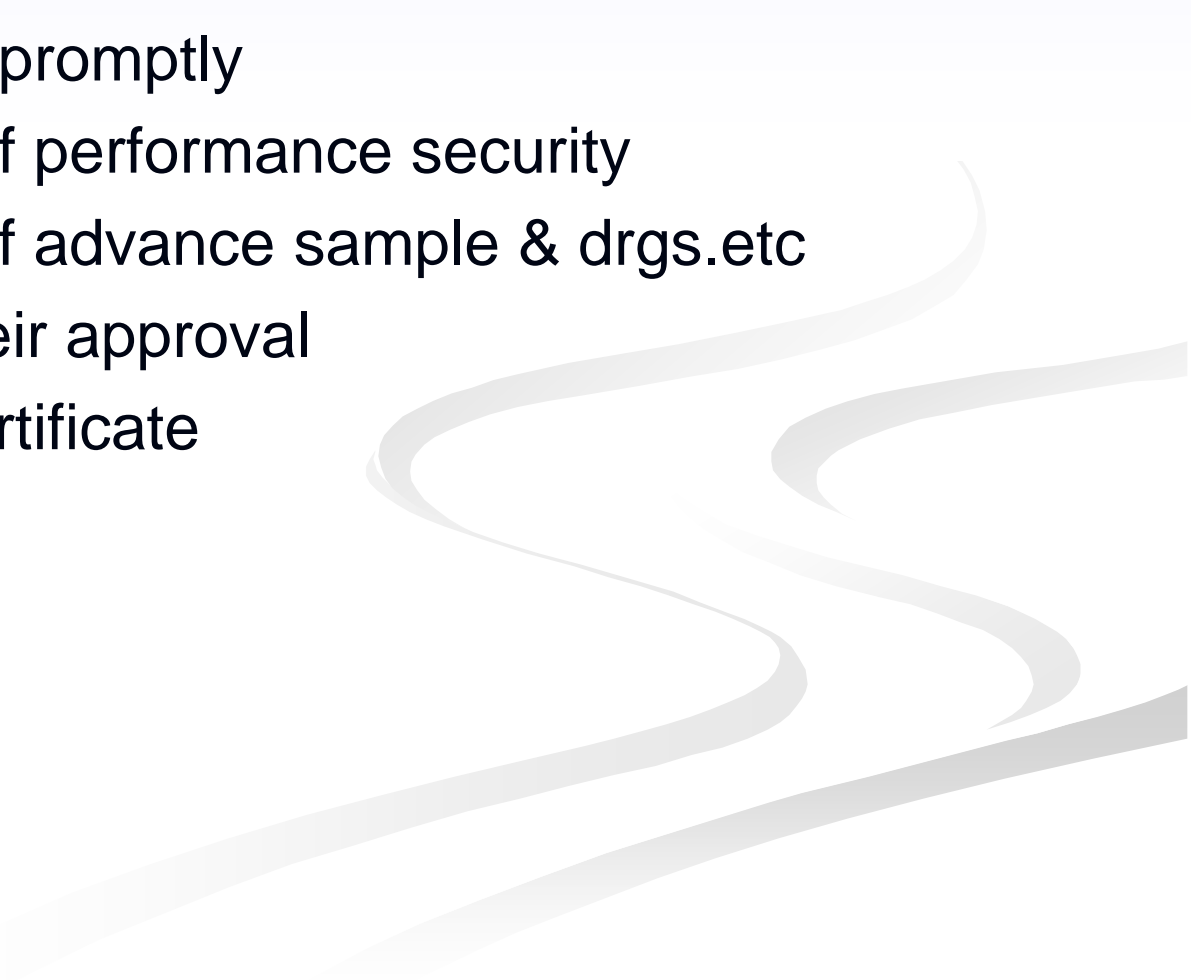
Contract Management

LOI

- Place LOI after settling all the terms.
 - Release promptly bid security of unsuccessful bidders.
 - Provide clarifications to unsuccessful bidders on request.
 - May hold meetings with unsuccessful bidders on request
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Contract Management

Acknowledgment

- Obtain acknowledgment
 - Issue required A / L promptly
 - Watch submission of performance security
 - Watch submission of advance sample & drgs.etc
 - Accord priority to their approval
 - Obtain C .D . E. certificate
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Contract Management

L. C.

- Arrange prompt opening of L . C.
- Ensure timely completion of civil works
- Request for monthly supply plan
- Initiate steps for TOT
- Monitor progress in compliance of provisions of offsets (plough back into India)

Contract Management

Inspection, Delivery, Installation

- Monitor progress in supply /performance
- Keep watch on DP
- Take prompt decision on request for DP extn.
- Extend DP with LD and denial clauses
- Inspect stores at mfr's works within DP
- Arrange prompt clearance at Port of entry
- Inspect stores / works at site
- Installation, testing, commissioning at site

Contract Management

LD, Payment, PV

- Issue CRC promptly to supplier
- Settle P V & LD claim quickly
- Ensure timely payments
- Release performance security in time
- Advise parties not to keep contract alive beyond DP/
extended DP
- Issue performance notice if contract is kept alive

Contract Management

Dealing with changes

- Ideally, no changes are permissible
- However in some cases changes in specs can be considered in the interest of expeditious supply / better performance of the equipment
- User should be consulted regarding any change in specification.
- Financial impact of the changes should be assessed and suitable price reduction should be obtained

Extension of delivery date

- Ideally, no extension of scheduled delivery or completion date should be granted
- Whenever such extension becomes unavoidable, approval of competent authority should be obtained and extension granted with reservation of right to levy **liquidated damages** for delay-Rule:204

Liquidated Damages clause in a contract

- **Damages generally means compensation for the loss**
- **Liquidated damages** is the loss estimated in advance and put in the contract itself
- The LD clause, usually, states that :
- (i) In the event of delay in performance under the contract, liquidated damages shall become leviable at the rate of $\frac{1}{2}$ % per week or part thereof of delay subject to a ceiling of 10% of the price of the equipment/goods or services of which the delivery or performance has been delayed.

Liquidated Damages clause in a contract

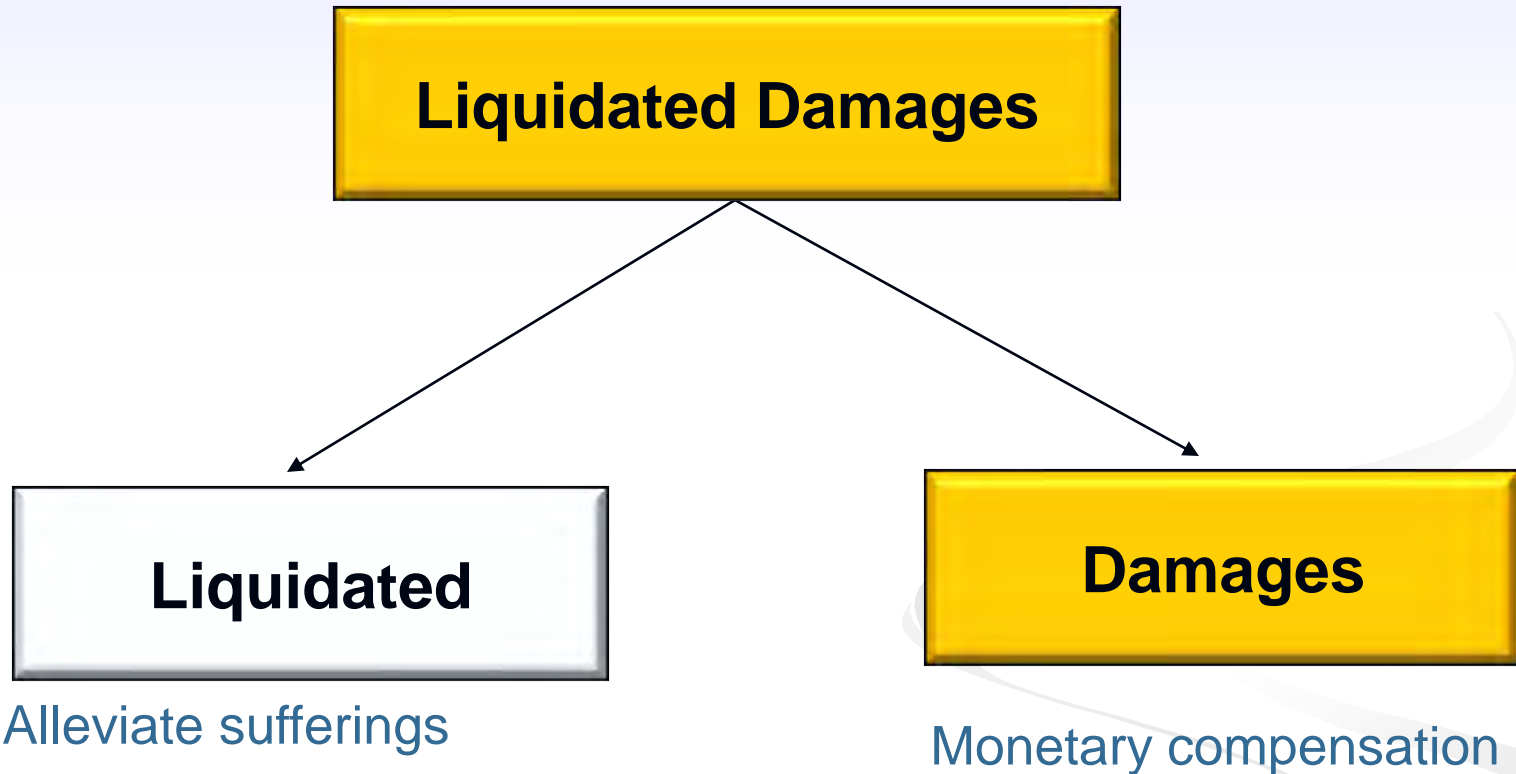
- (ii) In some cases, the rate of LD specified is 2% per month or part thereof of delay with a **ceiling of 10 %**.
- (iii) In some other cases, **no ceiling is stipulated**.
- The LD clause further states that the supplier shall remit the amount due to the purchaser within 30 days of receipt of demand from the purchaser. If the supplier fails to do so, the purchaser shall have the right to recover it from other payments due to the supplier

Liquidated Damages clause in a tender

Whether it has an impact on price?

- Purchaser 'A' has invited tenders with an LD clause that has a **ceiling of 10%** for levy of LD.
- Purchaser 'B' has invited tenders with an LD clause that has **no ceiling** for levy of LD.
- The goods are same, specs same, required delivery time-frame same and all other terms & conditions same
- **Who is likely to get lower price?**

What are Liquidated Damages (L/D)



- Where a party suffers due to breach of contract it has a right to claim damages thereof. S-73

Determination of Liquidated Damages

- Calculation of leviable L/D in the following cases, (a) Clause specifying the rate as $\frac{1}{2}$ % per week or part thereof of delay subject to a ceiling of 10%, (b) Clause specifying the rate as 2 % per month or part thereof of delay subject to a ceiling of 10% :
 - The contract price is Rs 1 Cr
 - The due date of delivery specified is 31.10. 2020
 - The above date was extended upto 31.12 2020
 - The actual date of delivery is 12.12.2020

What is 'Force Majeure'

- **'Force Majeure'** is a situation in which either of the parties is prevented, temporarily or permanently from performing its obligations under the contract due to circumstances **beyond its control**.
- The F M events can be classified into:
 - (i) Acts of God/ Nature- Earth quake, Tsunami
 - (ii) Acts of Sovereign Governments- Banning export
 - (iii) Acts individuals/ Groups- Acts of terrorism

The effect of incidence of F M events

Force Majeure

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graph TD; A[Force Majeure] --> B[Refixation of DP]; A --> C[Termination of contract];
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Refixation of DP

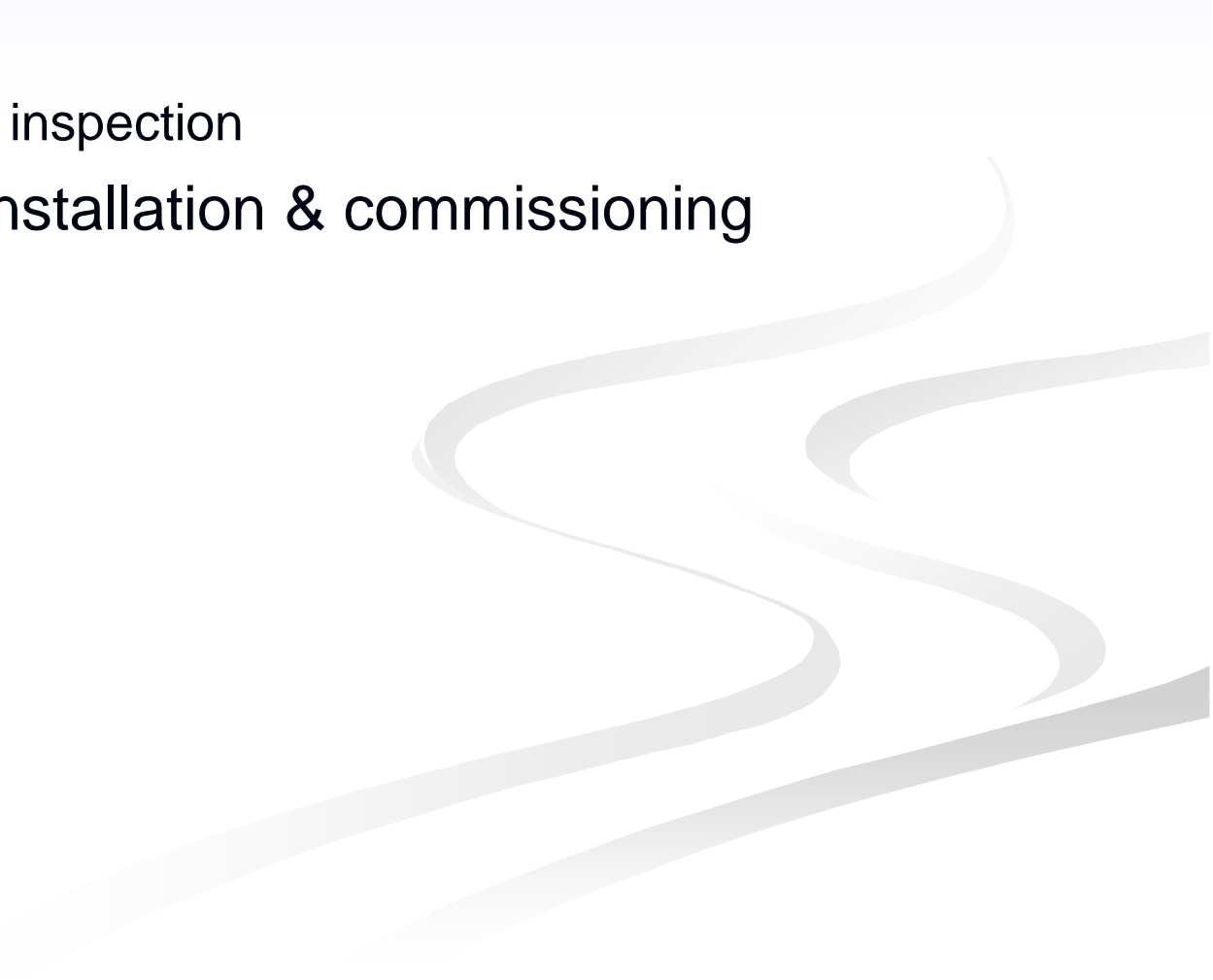
- Duration of Event plus set-up time

Termination of contract

- Termination without financial repercussions

How does buyer ensure quality?

Factory-end inspection and site inspection

- Inspection at the manufacturing-end
 - Stage inspection
 - Finished product inspection
 - Inspection after installation & commissioning
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Installation, Testing and Commissioning

- The responsibility for installation, testing and commissioning is usually entrusted to the contractor. The details of work to be done, the type of tests to be conducted and the performance parameters are specified in the contract
- The Testing and Commissioning is witnessed by the User and also by the Inspector concerned.
- Upon (i) Satisfactory completion of all the required tests, (ii) Demonstration performance and (iii) Satisfactory Trial Run, the equipment is taken over by the User

Advance payment

- Advance payment may be made in special cases
- While making any advance payment, a **Bank Guarantee** should be obtained-Rule:159
- In case any bank guarantee is furnished by a foreign bank, the same should be got duly **endorsed by a Public Sector Bank.**
- Advance payment to be restricted to 30% for private firms, 40% for PSUs and 50% for AMC

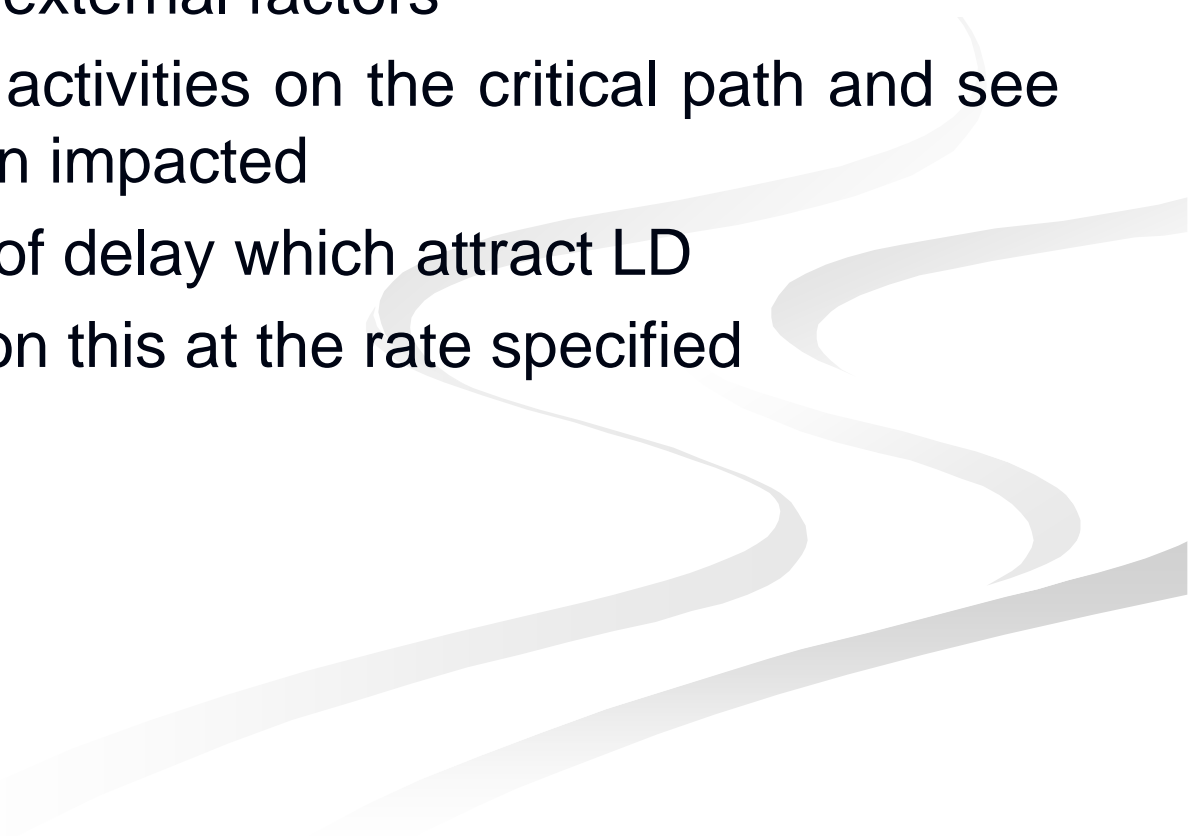
Stage/ Final payment

- Stage payments(95 or 90 or 80%) should be made after inspection and despatch in a **time-bound manner** as per terms of contract.
- Balance payment(5 or 10 or 20%) should be made on on acceptance of goods/ installation, testing and commissioning of Plant
- Claims of purchaser to be adjusted against final payment

Scrutiny of Seller's bills for payment

- Copy of inspection certificate
- Copy of delivery document (R/R, B/L, AWB)
- Manufacturer's test certificate
- Manufacturer's Warranty document
- Country of origin certificate
- Packing list
- Consignee's receipt certificate (CRC) for goods
- User's taking over (of Plant) certificate

Delay analysis

- Ascertain the extent of delay :
 - Attributable to the contractor
 - Attributable to the Project owner/ CA
 - Attributable to external factors
 - Take a look at the activities on the critical path and see how they have been impacted
 - Estimate quantum of delay which attract LD
 - Calculate leviabile on this at the rate specified
- 

Excusable delay

Delay attributable to Purchaser

- Extra works
- Changes in User's requirements
- Differing site conditions
- Delay in providing site access
- Delay in providing data, facilities, utilities
- Delay in approving design etc
- Hindrances due to other contractors engaged by you

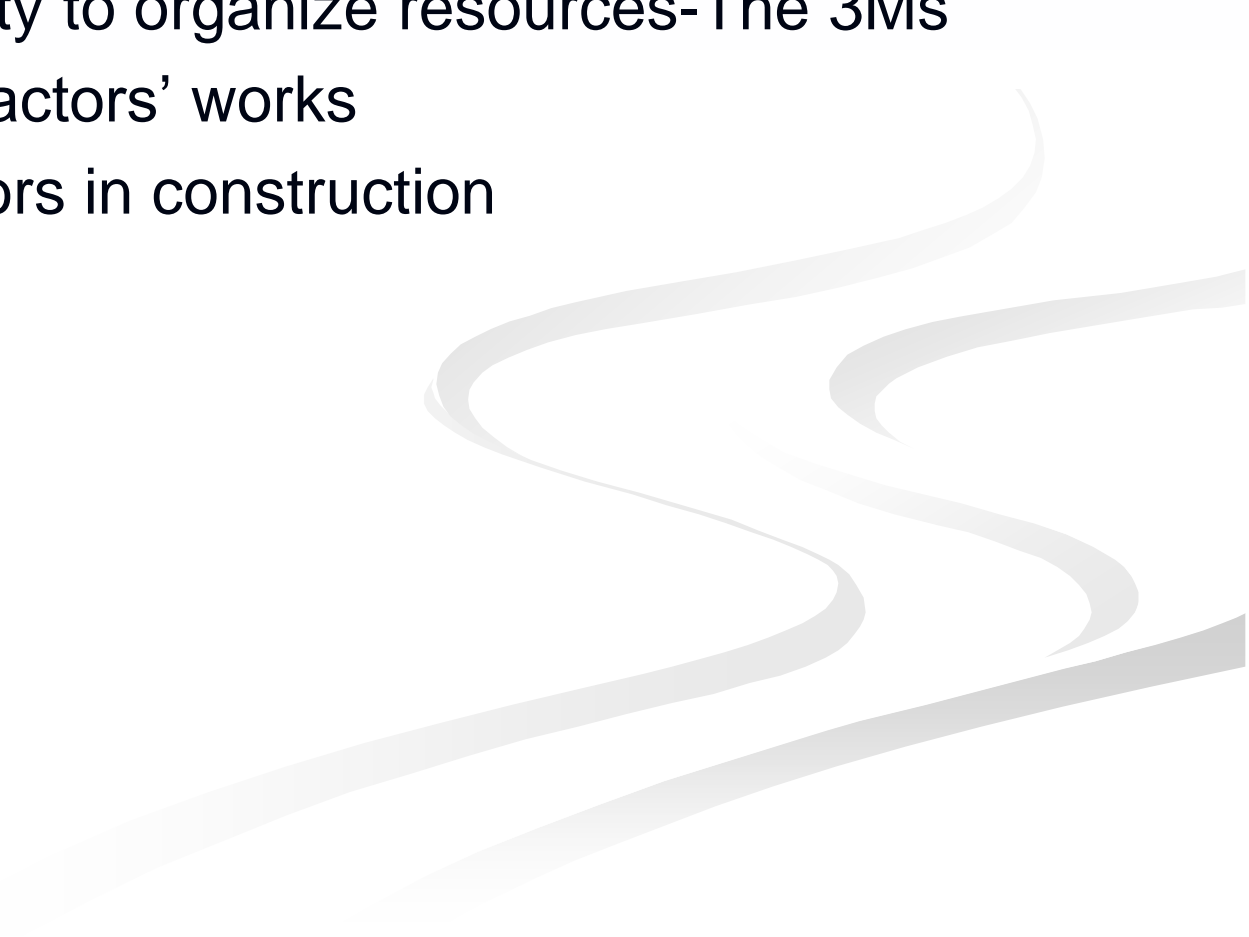
Excusable delay

Delay attributable to External Factors

- Force Majeure events
- Unusually severe weather
- Archaeological finds
- Third party issues – e.g. GAIL pipe line
- Suspension of work due to environmental restrictions etc-
e.g. To contain pollution in Delhi

Non-excusable delay

Delay attributable to contractor

- Delay in site mobilization
 - Contractor's inability to organize resources-The 3Ms
 - Delay in sub-contractors' works
 - Rework due to errors in construction
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Warranty

- **Warranty:** A period after delivery during which the seller has express or implied liability to the buyer for defects in the goods.
- The seller gives assurance regarding proper design, materials, Manufacturing and Workmanship and promises to rectify/ replace the equipment free of cost if the equipment does not function properly.
- The period of warranty, normally, ranges between 1 to 5 years

Contract of Indemnity

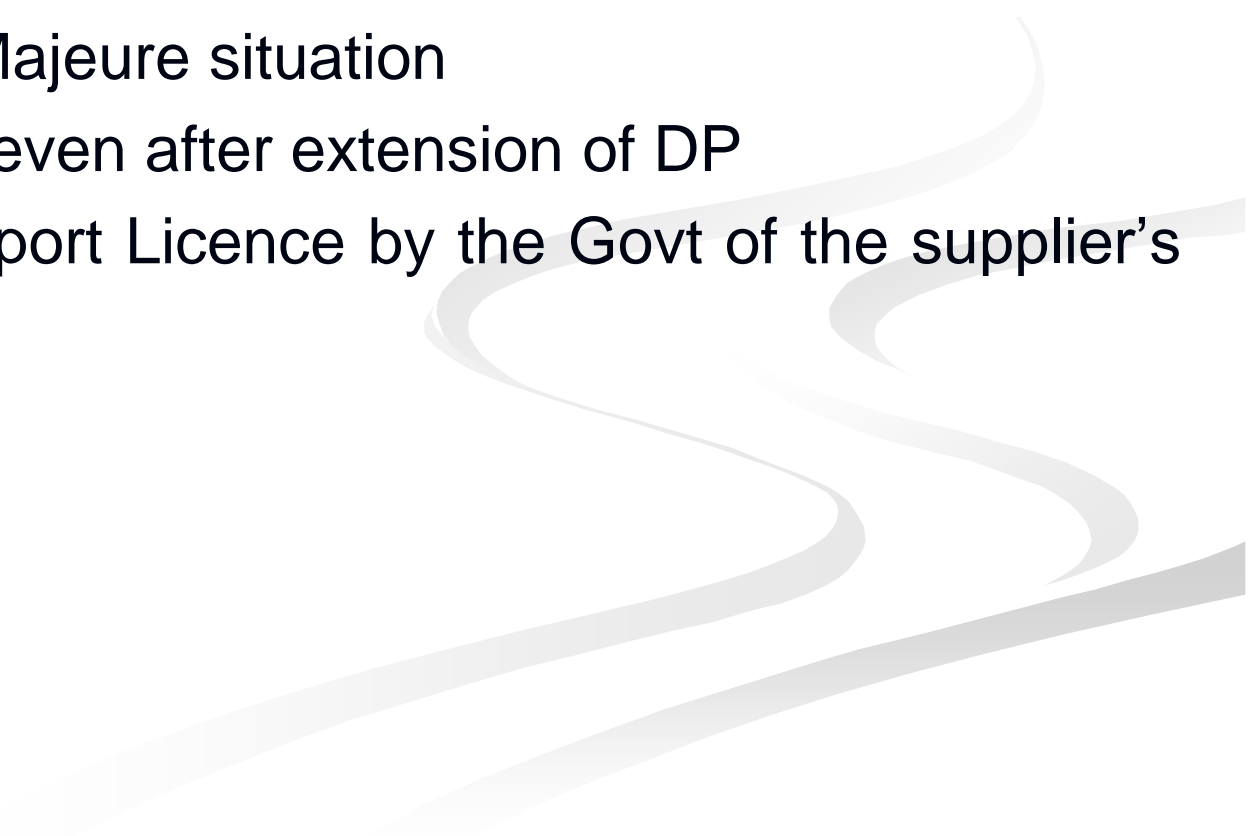
Protection against loss

- A contract of indemnity is a contract whereby one party promises to save the other from loss caused to him by the conduct of promiser himself or by the conduct of any other patty. S124


Notices

- During the course of execution of a contract, it becomes necessary for the parties to issue communications to each other from time to time. – Notice of occurrence / cessation of FM events; Notice of readiness of equipments for inspection/ shipment; Notice of default
- The contract clause relating to ‘Notices’, furnishes full address of the parties to which such communications have to be sent

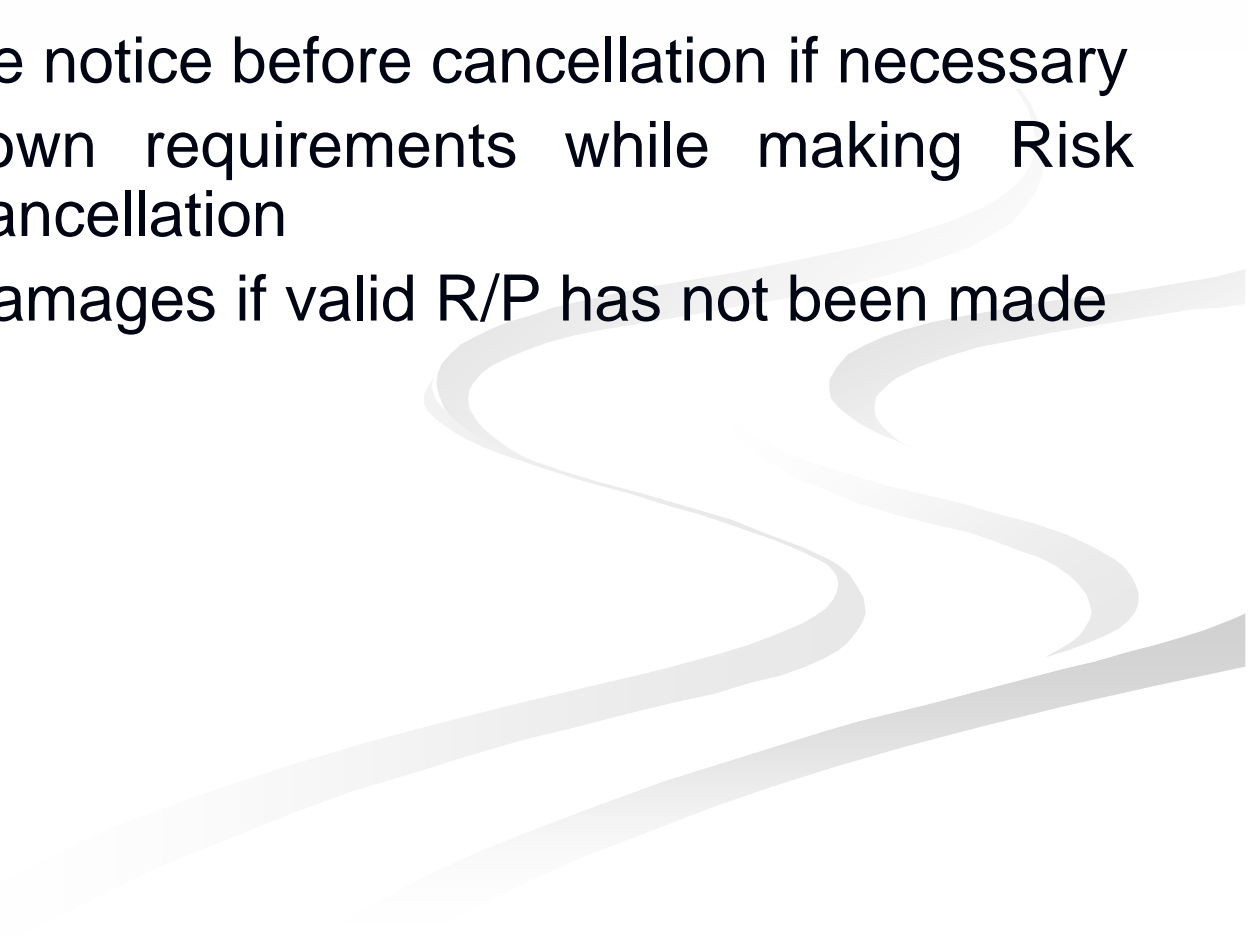
Termination of Contract

- During the implementation of a contract, there are normally the following three events which may lead to termination of contract:
 - Prolonged Force Majeure situation
 - Prolonged default even after extension of DP
 - Cancellation of Export Licence by the Govt of the supplier's country
- 

Termination of Contract

- In these cases, the final remedy provided to the Purchaser is a right to terminate the contract.
 - This clause gives the purchaser, through a written notice sent to the supplier, a right to terminate the contract in whole or in part.
- 

Do's for Contract termination

- Cancel contract only when breach/anticipatory breach occurs
 - Give performance notice before cancellation if necessary
 - Fulfill all laid-down requirements while making Risk Purchase after cancellation
 - Claim General Damages if valid R/P has not been made
- 

Requirements for valid Risk Purchase

- Specs must be same as was adopted initially
- Mode of procurement same or ATE
- Risk purchase contract must be concluded within a reasonable time which is normally 6 months from the date of breach
- Lowest acceptable offer should not be ignored while placing the risk purchase contract
- If it is ignored, risk purchase loss will not be legally recoverable

Price Variation clause

$$P_1 = P_0 \left(F + a \frac{M_1}{M_0} + b \frac{L_1}{L_0} \right) - P_0$$

- Where P_1 is the adjustment amount payable
- P_0 is the Contract Price at the base level
- F is the Fixed element
- a is the assigned percentage to the material element
- b is the assigned percentage to the labour element
- L_0 and L_1 are the wage indices at the base month and year and at the month and year as stipulated in the contract
- M_0 and M_1 are the material indices at the base month and year and at the month and year as stipulated in the contract

Price variation as per PVC

- The PVC incorporates a fixed component-'F' which is usually 15%. No price variation is applicable to this.
- Now come to Labour and Material components.
- The base indices of Labour and Material are shown in the contract itself.
- Data regarding final indices of Labour and Material are usually provided by Contractor with documentary evidence. This is checked by the Purchaser, who determines the amount of price variation.

Determination of Price variation as per PVC

- Calculation Price Variation in the following cases:
 - The contract price is Rs 1 Cr
 - The Fixed component 'F' is 0.15
 - The base indices of Labour and Material shown in the contract are 100 for both
 - The final indices of Labour and Material are 110 and 120 respectively
 - The factor for Labour ie 'b' is 0.30 and the factor for material ie 'a' is 0.55

Calculation of Price Variation

$$P_1 = P_0 \left(F + a \frac{M_1}{M_0} + b \frac{L_1}{L_0} \right) - P_0$$

- P_1 is the adjustment amount payable to be calculated
- $P_0 = \text{Rs } 1 \text{ Cr}$
- Fixed component, $F = 0.15$
- Materials factor, $a = 0.55$
- Labour factor, $b = 0.30$
- Labour indices, $L_0 = 100$; $L_1 = 110$
- Material indices, $M_0 = 100$; $M_1 = 120$

Calculation of Price variation

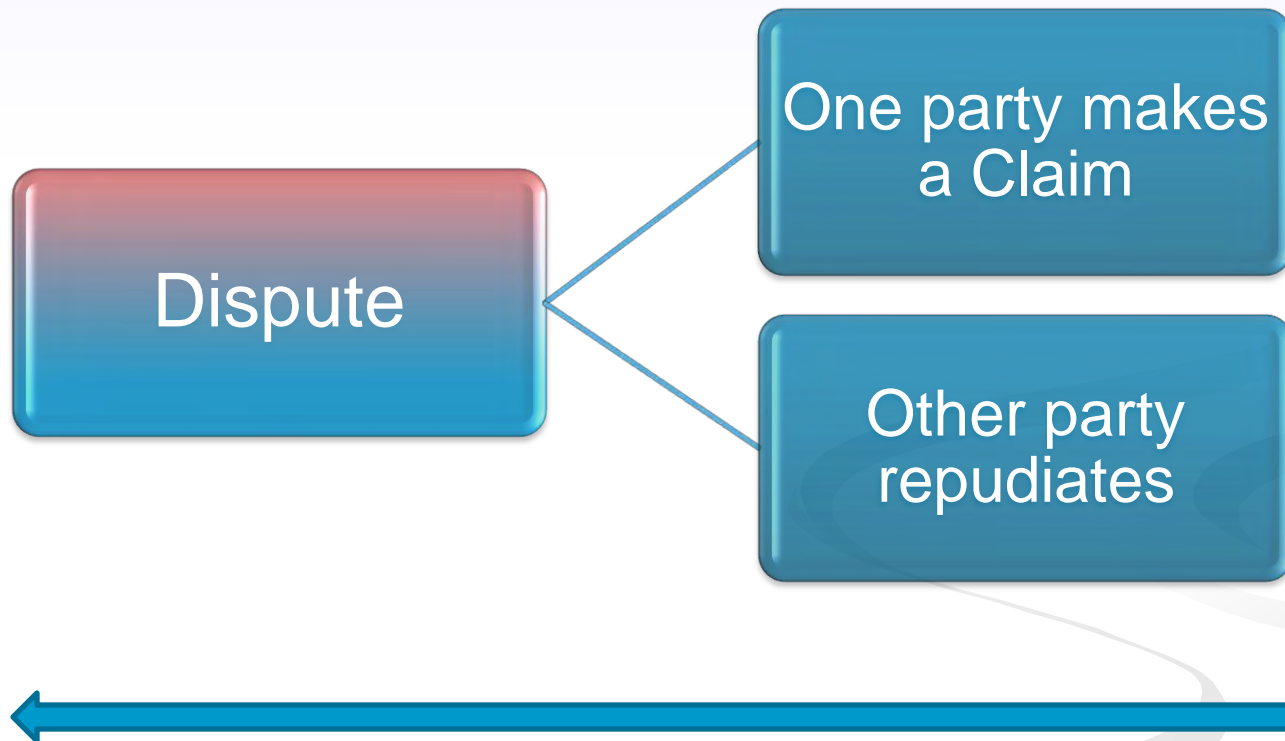
- The Materials: Rs 1 Cr x 0.55 = Rs 55 Lakhs
- Increase due to materials: Rs 55 L X 120/100 = 11 L
- The Labour: Rs 1 Cr x 0.30 = Rs 30 Lakhs
- Increase due to labour: Rs 30 L X 110/100 = 3 L
- Total increase as per PVC: Rs 11 L + Rs 3 L = Rs 14 L

Remedies for breach of contract

(Rights of aggrieved party)

- Rescission of contract- Cancellation of contract
- Claim damages- Damages for compensation of loss
- Suit upon quantum merit – Suit for getting of as much as earned for the quantum of work done by the seller
- Suit for specific performance- Court orders performance
- Suit for injunction- Court restrains performance

How does a dispute arise



Contract Dispute resolution

Strategy for dealing with disputes

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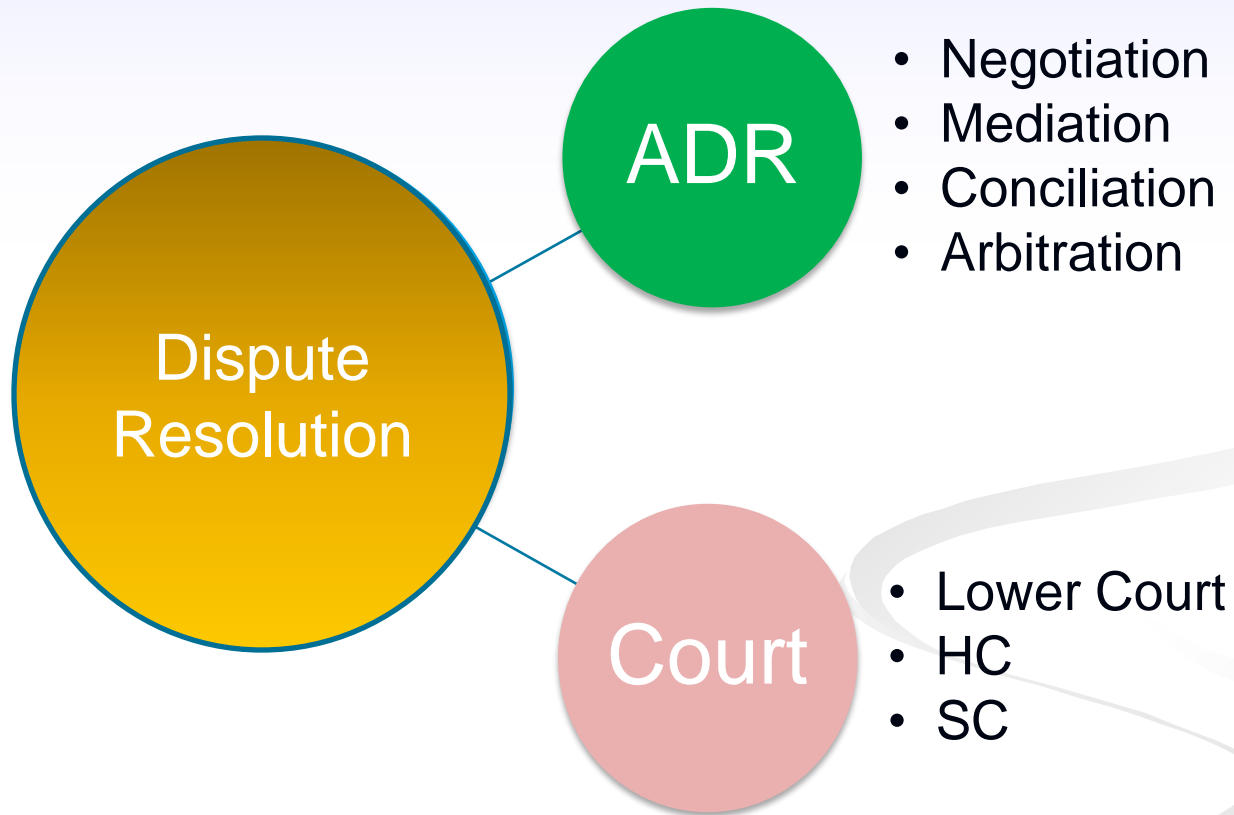
Prevention of disputes

- Drafting of contract
- Contract Mgmt
- DRB

Settlement of disputes

- ADR
- Court

Dispute resolution



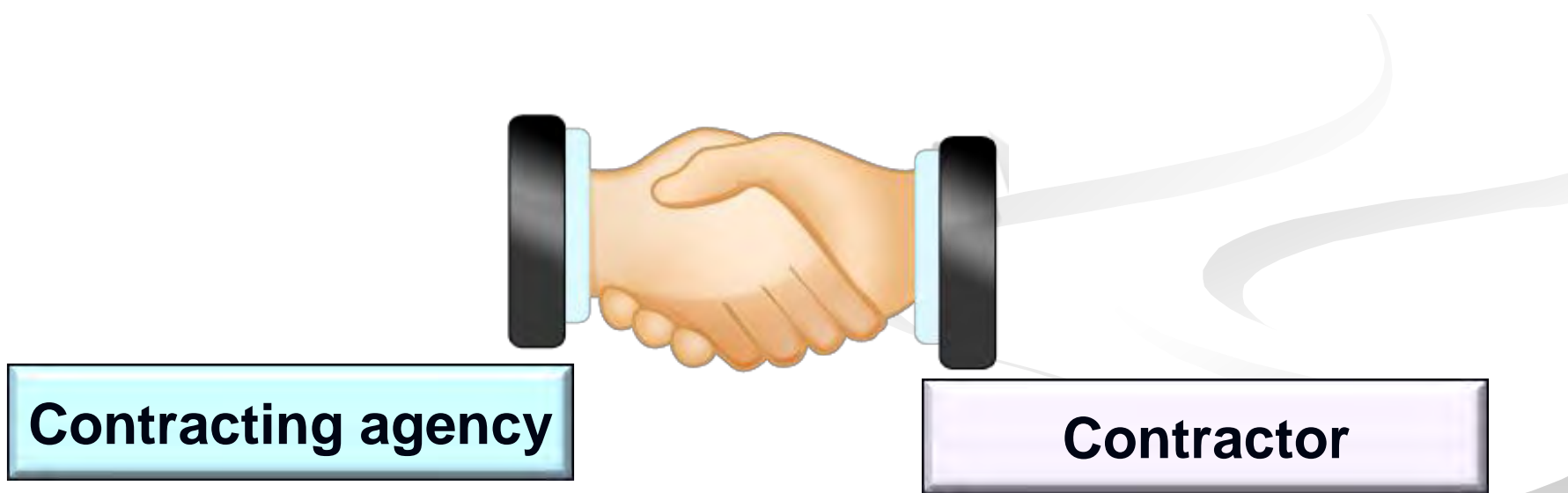
ADR- Alternative Dispute Resolution

Analysis of operation of contract

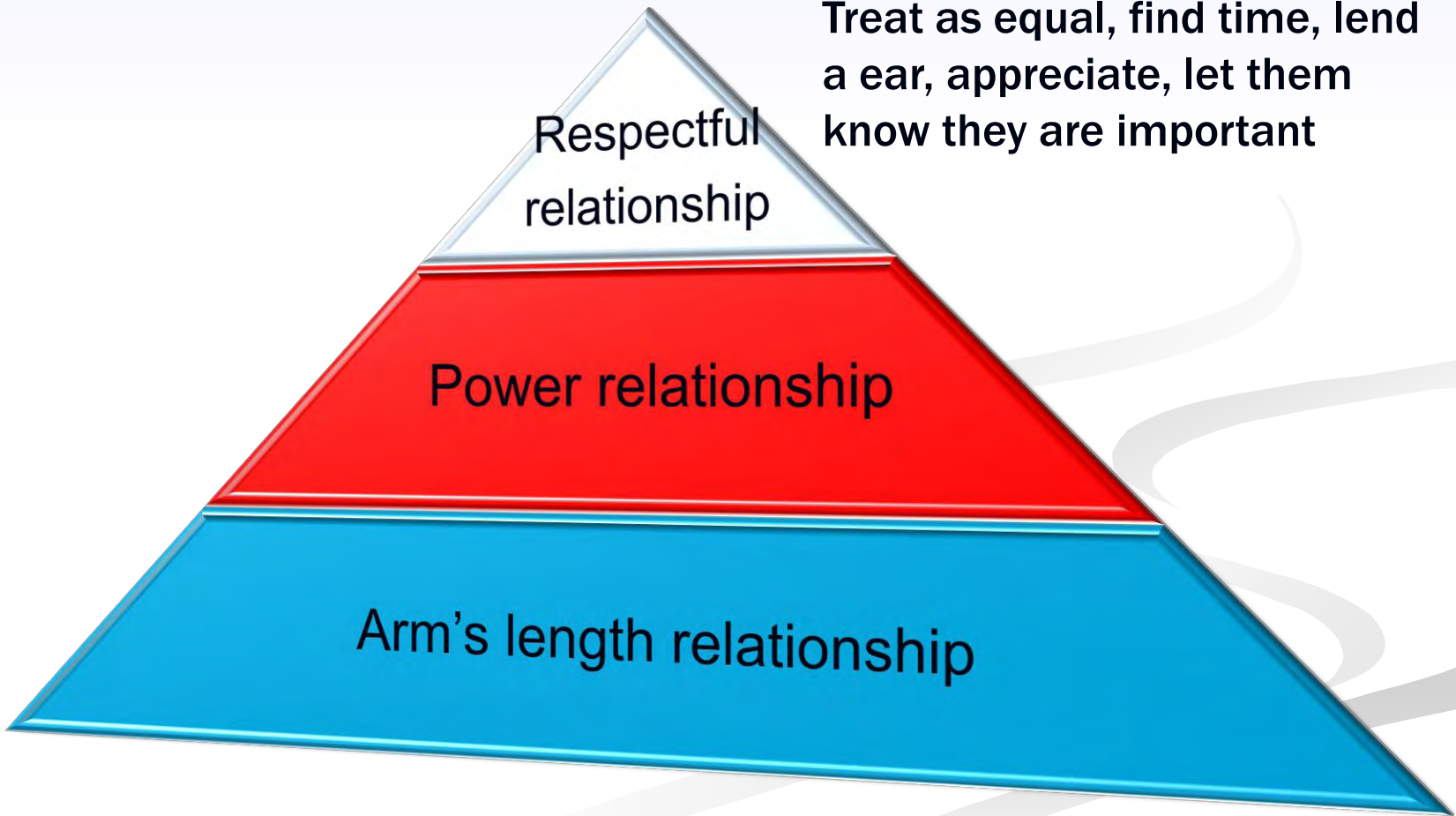
- This is an exercise for continual improvement of our contract clauses and contract management.
- At the close of the contract, a review is undertaken to identify the contract clauses that need refinement in the light of problems faced and experience gained
- During the life of the contract, the world is not standing still. The trade and commerce is progressing. Technology is moving forward. This may demand some changes in your contract clauses also.
- The required changes are incorporated with the approval of Competent Authority in consultation with L. A

A collaborative approach

- It will be desirable to establish harmonious relationship with the contractor in long-term contracts, especially with service element.



Purchaser-Supplier relationship



**Thank you so much
for
active participation**

**Happy Janmastami
and
Ganapati Puja**

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