
AN ANALYTICAL STUDY ON GOVERNMENT CONTRACTS WITH REFERENCE TO INDIA

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ABSTRACT

The subject of government contracts has become increasingly relevant in recent years. The nation has become the road to wealth. In the current stage of the welfare state, the state's financial management is expanding and the state is increasingly taking on a profit-sharing role. Today, a significant number of individuals and businesses benefit from government contracts, quotas, licenses, employment, mining rights, and more. Government contracts can offer attractive economic opportunities, but they also pose certain risks and challenges. To comply with contracts, contractors must manage complex regulations, adhere to strict reporting policies, and meet high standards. In addition, unexpected contract adjustments or cancellations may result from changes in governmental objectives or financial constraints. This makes it more likely that the government will use its power to be haphazardly generous. Not to mention the government and everyone wants them. As a result, certain standards need to be developed to manage and defend individual interests in such wealth and to organize and discipline the governmental discretion to grant such interests. Contracts have become an essential aspect of conducting a wide variety of commercial transactions, as they establish the rights and obligations of all parties involved in the transaction and can seek remedies from the courts in the event of a breach of contract. Public procurement is governed by regulations and laws designed to promote accountability, openness, and fairness in the general procurement process. Therefore, government contracts require careful drafting, negotiation, and dispute resolution to ensure a successful outcome for both parties. Government contracts generally contribute significantly to the economy and are an important source of income for many businesses. However, with the strict rules and controls that come with dealing with governments, contractors must be prepared to handle the unique challenges of this market.

INTRODUCTION

Even though the concept of Government Contracts in India is governed by the present Indian Contract Act, 1872 in force, it has quite a distinct form of variation regarding its implications from a private contract, the primary objectives revolve around supplying or obtaining goods and services whereas, in government contracts, the objective can be of providing livelihood and employment or to eradicate poverty or have an effect of subsidy. Thus, it can be seen that in the case of government contracts, the public plays a major role in its formation which remains absent in the field of other categories of contracts. The Indian Contract Act of 1872 has no such explicit provision regarding the capacity of the government to establish a contractual relationship. The government rather gets its authority to enter into a contract through the provision of Article 299 of The Constitution of India which designates the full authority of the government of a state or the government of India to form a contract with other states or individuals.¹ The Government generally invites various parties to place their bids and offers its contract to the most suitable party or candidate through the process of an auction or also known as a ‘tender’.² Basically, or simply a tender is a written offer in which a large number of contractors are invited to either work according to or supply some materials. Another distinguishing factor from private contracts can be drawn is that in the case of government contracts according to Article 299 (1), “All contracts made in the exercise of executive power of the union or a state shall be expressed to be made by the President or by the Governor of the State as the case may be, and all such contracts and all assurances of property made in the exercise of that power shall be executed on behalf of the President or the Governor by such person and in such manner as he may direct or authorize.”³ This clause vests the power and position to direct and authorize in the hands of the President and the Governor but at the same time, Article 299 (2) “Neither the President nor the Governor shall be personally liable in respect of any contract or assurance made or executed for the purpose of any enactment relating to Government of India hereto before in force, nor shall any such contract or assurance on behalf of any of them be personally liable in respect thereof.”⁴ Contrary to this, the position in England opines a different set of opinions and laws. In Britain, before 1947, the Crown (Government) could not be sued in the Court of Law regarding a contract, however, the

¹ INDIA CONST. art. 299.

² Gauransh Vyas, What is the contract of tender: overview, (April 22, 2023, 11:57 PM), <https://blog.ipleaders.in/what-is-the-contract-of-tenders-overview/>

³ INDIA CONST. art. 299. cl. 1, *amended by* The Constitution (Fortieth Amendment) Act, 1976.

⁴ INDIA CONST. art. cl. 2.

aggrieved party could seek out a remedy through a petition of right and if the royal fiat or an authoritative decree is granted, the respective can then bring an action against the Crown in the Court of Law to enforce his contractual rights. Although, the granting of the royal fiat was not a subject of right and could be refused at ease, and once refused, there is no other remedy for the party in distress. In 1947, The Crown Proceedings Act permitted the actions brought by the aggrieved parties against the Crown in the Courts of Law to enforce their contractual rights and liabilities, expecting a few government contracts.

DIFFERENCE BETWEEN CONTRACTS AND GOVERNMENT CONTRACTS

Since the contract is entered into by the parties under the provisions of the Indian Contracts Act, of 1872, no other Indian law applies to individual rights. Contract parties can manage their obligations and rights through the contract. However, Indian contract law does not act as a comprehensive law governing all forms of transactions. It does not cover all contract law, so in situations where the law is silent, the national law of the country may apply. However, this does not mean that Indian contract law will be superseded in any way.

In the case of *State of Bihar v. Abdul Majid*,⁵ the Apex Court has held that;

“It may be noted that like other contracts, a Government contract is also governed by the Indian Contract Act, yet it is distinct a thing apart. In addition to the requirements of the Indian Contract Act such as offer, acceptance and consideration, a Government contract has to comply with the provisions of Article 299 of the Constitution. Thus subject to the formalities prescribed by Article 299 the contractual liability of the Central or State Government is same as that of any individual under the ordinary law of contract.”

When interpreting contracts, no distinction is made between contracts in which one party is the government and the other private parties. Although there is little advantage in the interpretation and enforceability of contracts between private parties and governments, there are some concessions to governments in the form of separate treatment in the statute of limitations.⁶

In addition, governments are accorded several advantages related to the power to enforce their obligations before going to court.

⁵ *State of Bihar v. Majeed*, AIR 1954 SC 786

⁶ *Nav Rattanmal and Others v. State of Rajasthan*, AIR 1961 SC 1704

FORMATION OF GOVERNMENT CONTRACTS

Central and state governments have legal obligations under the Indian Constitution. The powers of the federal and state governments to engage in any transaction or business, to acquire, retain and dispose of property, and to enter into contracts for any reason are expressly outlined in Article 298 of the Constitution. It is the union and the executive branch of the country. Like the preceding Article, Article 299 sets out the form and procedure for such contracts.

Contracts with governments must be "expressed", but the parties to a regular contract depend on their ability to agree to the contract through their explicit or implied actions.

In the judgment in the case of *Bhikraj Jaipuria v. Union of India*⁷ it has been held that;

"It is clear from the words "expressed to be made" and "executed" that there must be a formal written contract...The provisions of Article 299(1) are mandatory in character and any contravention thereof nullifies the contract and makes it void. The provisions of Article 299(1) have not been enacted for the sake of mere form but they have been enacted for safeguarding the Government against the unauthorized contracts. The provisions are embodied in the constitution on the ground of public policy on the ground of protection of the general public and these formalities cannot be waived or dispensed with."

Implied contracts do not apply to government contracts. These restrictions are designed to protect governments from fictitious contracts that may be entered into on their behalf to mislead the public.

The Supreme Court of India in the case of *K.P. Chowdhry v. State of Madhya Pradesh and Others*⁸ held that;

"In view of Article 299(1) there can be no implied contract between the Government and another person, the reason being that if such implied contracts between the Government and another person were allowed, they would in effect make Article 299(1) useless, for then a person who had a contract with Government which was not executed at all in the manner provided in Article 299(1) could get away by saying that an implied contract may be inferred on the facts and circumstances of a particular case."

⁷ *Bhikraj Jaipuria v. Union of India*, AIR 1962 SC 113

⁸ *K.P. Chowdhry v. State of Madhya Pradesh and Others*, AIR 1967 SC 203

JUDICIAL REVIEW

Government contracts are not as simple as private contracts. The court occasionally questions the prudence behind the decision to enter into a contract while contracting privately. However, because the public interest is involved with government contracts, this is not the case. The edifice of government contracts moreover puts taxpayers' money in jeopardy but also is subject to public perusal provided many parties contest for the same tender with the government. Government contracts are made with the executive of the government, it is apparent that these contracts are subject to judicial review. The court's outlook has been fluctuating between exercising notable judicial control in contracts relating to the government and at times, exerting considerable interference from the judiciary while making decisions relating to the matter in government contracts.

The judicial review can be categorized into 3 different phases based on development;

1. Beginning of legal review of government tenders

From 1950 to 1979, the judicial oversight of government contracts was essentially nonexistent. In the case of *C.K. Achuthan v. State of Kerala*,⁹ the Apex Court held that "The government had the freedom to choose a contracting party to fulfill contracts and that an aggrieved party who was not chosen cannot claim cannot claim discrimination and therefore the protection of article 14". This statement if not considered would make the situation of the government indistinguishable equivalent to some undisclosed party to the contract.

In the case, *Erusian Equipment & Chemicals v. State of West Bengal*,¹⁰ The Supreme Court held that "The executive powers of the state under article 298 (including to enter into public contracts) is subject to the principle of equality of opportunity under Article 14 of the constitution."

In the case of *Ramana Dayaram Shetty v. International Airport Authority of India*,¹¹ The Supreme Court used the fundamentals of administrative law to expand the role of the state, assuming responsibility for intervening "to structure and restrict the power of executive government to prevent its arbitrary application or exercise." The court highlighted the significant distinction between public and private contracts. The court further stated "The

⁹ C. K. Achuthan v. State of Kerala and Others, AIR 1959 SC 490

¹⁰ Erusian Equipment & Chemicals Ltd. v. State of West Bengal and Others, (1975) 1 Supreme Court Cases 70

¹¹ Ramana Dayaram Shetty v. International Airport Authority of India and Others, (1973) 3 Supreme Court Cases 489

government does not enjoy certain freedom and discretion of a private party in entering into contracts and it cannot act arbitrarily”, “but its action must be in conformity with standard or norms which is not arbitrary, irrational, or irrelevant”.

2. The Period of Firm Judicial Intervention

This period can be dated from 1980 to 2011. While the 1980s were fairly quiet when it came to judicial review of government contracts, the 1990s proved to be an important decade for judicial review. The problem at the time was the size and scope of the inspection authority. The issue at that time was the purview and extent of review power. When there was clear proof of malice or arbitrariness in government contracts during those times, the courts often exercised caution and intervened to annul them, striking a balance between contract freedom and the needs of the general public.

In the case of *Sterling Computers Ltd. v. M&N Publications Ltd.*,¹² The court clarifies that “by way of judicial review the court is not expected to act as a court of appeal while examining an administrative decision and to record a finding whether such decision could have been taken otherwise in the facts and circumstances of the case.” Additionally, while the judicial review was being conducted, the court focuses on the process by which the government has decided to allot the contract.

In the case of *Delhi Science Forum v. Union of India*,¹³ which is related to telecom license awarding policy, The courts are very sensitive to economic policy decisions and have expressed their willingness to intervene when constitutional or statutory provisions are violated. The court made it clear that “the burden of invoking judicial review, by stating that the onus of demonstrating the vitiation of a decision to enter into a contract on any of the recognized grounds vested in the person challenging the decision. Unless the aggrieved party was able to discharge that burden, the courts would hesitate to intervene.” During this phase, Concerns about economic policy issues and judicial restraints on government contracts outweigh judicial action.

3. Judicial Involvement and the Era of Disruption

“Beginning in 2012, it is possible to see the process of deciding the scope of judicial review of

¹² *Sterling Computers Limited v. M/s M & N Publications and Others*, (1993) 1 Supreme Court Cases 445

¹³ *Delhi Science Forum and Others v. Union of India and Another*, (1996) 2 Supreme Court Cases 405

government decisions regarding the allocation of natural resources among private parties.”

In the case of *Centre for Public Interest Litigation v. Union of India*,¹⁴ which is also referred to as the “2G spectrum case” the Supreme Court directed the cancellation of 122 UAS licenses. The “2G spectrum case” involved a type of government procurement that has increased in frequency over the past decade as a result of the privatization of several government affairs.

It is evident from the court's invasive approach to government decision-making that its contribution to evaluating government contracts or licenses has grown over time. The “2G spectrum case” in addition resulted in substantive dismay among private players but has also invited analysis of government contracting and policy.

DISPUTES RELATING TO A GOVERNMENT CONTRACT

The doctrine of sovereign immunity which means that a sovereign nation cannot commit a legal wrong is not applicable in this context. Even though the President or Governor is not personally liable as per Article 299¹⁵ of the Indian Constitution, the State is liable and can be sued for any breach in a contract as equal to a private individual.

In *The Secretary of State for India In Council v. Hari Bhanji*,¹⁶ a lawsuit was filed to recover overage charges charged by the state for salt shipments. The Madras High Court denied the exemption request, ruling that only state acts fell within the scope of the East India Company's exemption and that activities conducted in violation of municipal law did not receive an exemption.

In a Government Contract alike other general contracts, disputes may arise at any given point in time. A contract is valid only when both parties agree on a subject matter in the same sense at the same time, i.e., the maxim of *ad idem*. When this condition is not fulfilled, a dispute may arise and the agreement formed goes into a state of dormancy. The main cause of the rise of these disputes is the negligence on behalf of the drafters. Government contracts can sometimes develop into considerable size with a massive number of pages and clauses due to which it is common for draftsmen to commit a small number of errors or omissions. Other causes such as errors in estimated costs and changes in conditions due to stakeholder's reactions can also be included. It is also to be noted that several disputes may arise when project participants under

¹⁴ Centre for Public Interest Litigation v. Union of India, 2012 SCC OnLine Del 3223

¹⁵ INDIA CONST. art. 299.

¹⁶ The Secretary of State for India In Council v. Hari Bhanji, (1882) ILR 5 Mad 273

a government contract are performing. Their quality and nature of communication and interaction may also pave the path for additional disputes arising. Although, it can be considered that the greatest number of disputes arise from the relationship between the owner, i.e., the government and the contractor. Issues regarding on-time payment of installments, change in the total number of working project days, cost incurred exceeding the budget determined, debt settlements, changes in design, etc. are the most prevalent issues of dispute that arise between the owner and the contractor.

These disputes that arise pose a great threat to the common good and welfare of the State as government contracts are executed for the good governance of the State and its people. It stops and indefinitely delays the activity initiated or in progress by the Government for the prosperity of the nation when these kinds of disputes become a source of an institution of a plant or a petition in a Court of law. This is the primary reason why in most government contracts nowadays, a clause referring to Alternative Dispute Resolution is mentioned regarding any disputes that arise in between the proceeding of a contract rather than resorting to the traditional method of approaching the Court of law to resolve the conflict.

Alternative Dispute Resolution mechanisms are being adopted nowadays in Government Contracts for several various crucial reasons, namely the speedy judgment and the subject-matter confidentiality it offers. The speedy judgment that it provides is an indispensable advantage to the government in contractual matters due to the large number of contracts that the government needs to institute and deal with every day and also the preservation of information regarding the case from spilling out may also sometimes act pivotal regarding sensitive subject-matters such as contracts in the field of defense, medicine, etc. The Government of India on 8th February 2023 has even proposed quick settlement of contractual disputes to ease business. The government is doing this as such cases are holding back fresh and new investments and at the same time, the settling of those disputes will also ease the way of doing business for the government even more. Currently, its rank is at 63rd position for India in the "World Bank's Ease of Doing Business" among 190 plus countries. Previously India was ranked at the 142nd position in the year 2014, by noticing this rapid improvement in India's standing, the conclusion that can be implied or drawn from this is that the government is encouraging the adoption of Alternative Dispute Resolutions to facilitate the speedy judgment of cases.

The most preferable way among the alternatives of settlement of disputes is negotiation. This

is so as it neglects the troublesome process which the other methods have altogether. Both parties come to an amicable settlement or solution together, which generally results in a win-win situation. Adjacent to this method, lies the method of Conciliation which is duly recognized by the Indian statutory provisions. Conciliation keeps open the option of the parties to appeal to the court if the parties are not satisfied with the award as it is non-binding in nature. Mediation is also similar in nature. Although, there are many methods of dispute resolution, the most common is Arbitration. The government of India has even issued guidelines from time to time mentioning the establishment of Permanent Machinery of Arbitration (PMA) Cells for this very specific purpose of resolving the disputes that arise in Government Contracts. This was done by the government to reduce the time consumed and to reduce avoidable expenditure in resolving the plethora of disputes that arise regarding government disputes as stated in a notice dated 22nd January 2004. Either party can approach and refer their case to a PMA, but the PMA can only be moved when both parties agree to do so. PMAs are primarily set up for the speedy jurisdiction of cases regarding disputes that transpire in government contracts.

CONCLUSION

Government contracts are an essential part of everyday contract law without that no financial transaction could take place. By providing income, jobs, and economic growth, government contracts can give the economy a huge boost. When a government wins a contract, companies often need to hire staff, purchase supplies and materials, and make investments in infrastructure. From consumers to workers to businesses, everyone can benefit from increased economic activity. Public procurement helps improve public services by funding needed projects and services. Government contracts can be used, for example, to fund the construction of roads and bridges, healthcare, or the maintenance of public structures. This makes these services more accessible, more effective and benefits the community as a whole. Government contracts can also foster innovation by supporting otherwise financially unfeasible research and development initiatives. This can lead to new innovations, goods, and services that benefit everyone, from customers to businesses to governments. In most cases, when a government contract is awarded, the contractor must meet specific requirements and time frames. This helps reduce fraud, waste, and abuse and maintains accountability. Government contracts help ensure that public funds are properly spent by ensuring that contractors meet their obligations.

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