DISCRETION AND ITS CONSTITUTIONAL LIMITS: STATUTORY AUTHORITIES AND THE FREEDOM TO CONTRACT

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ABSTRACT

Administrative law does not end when a statutory authority decides to make a contract; it also looks at the constitutional rules that affect that decision, both before and after the contract is made. This article is concerned with the limits on contracting by statutory authorities and explores the cases where such authorities use their discretion to enter into agreements with private companies, and how much that freedom is controlled by constitutional principles. It examines how far, if at all, the constitutional principles and these restrictions operate as a standard to assess the exercise of discretion in contracting by statutory authorities. It analyzes the Indian situation from the former position of the doctrinal separation of the executive power of the state to contract from the invalidity of contract, and traces the jurisprudential position from the near-total deference to the standards of rationality and non-arbitrariness. It identifies and evaluates the discernible limits to the statutory authority's discretion in contracting in different areas such as the building and allied professions, medicine, and other allied professions, and public-private partnerships. It examines the non-fettering principle and determines that, in the absence of open tendering, the government's discretion in contracting is defensible only in a public works contract.

1. Introduction

Herbert Hart once referred to making a contract 'as the exercise of limited legislative powers by individuals'.[1]

The theoretical precincts of administrative law are not limited to administrative authorities exercising their discretion in the sphere of contracting, but also extend beyond the point at which contracts are actually formed between the statutory authorities and private entities. While the exercise of discretionary power before a contract is signed is closely governed by constitutional principle, once contractual obligations have been undertaken, courts have tended to fall back on private law to resolve disputes arising from them.

Statutory authorities are those organs of the government which came into existence with a specific piece of legislation conferring it a statutory status. Central government departments, local authorities, administrative tribunals, courts, and other institutions are significant arms of the administrative machinery.[2] Wherever a function of statutory nature is conferred on the central government, there is a significant policy element in the process of decision-making wherein every statutory authority is expected to act in a manner consistent with achieving the twin goals of growth and development.

Contracting with private entities is one of the principal ways in which this gap between statutory mandate and practical delivery is filled, and the general contractual capacity of statutory bodies, their standing as 'persons of capacity' competent to bind themselves, is what makes this possible.

2. Statutory Contracts and Discretionary Powers

Whether a government department is initiating administrative action, supervising other administrative agencies in exercise of various statutory functions or acting as an adjudicative agency from a decision of another administrative agency, such functions are usually defined in terms of discretion. The essence of any such discretion is that the administrative agency has the opportunity to make a choice, as long as that choice is made within the limits of statutory powers concerned. It is equally important that this discretion be exercised with some degree of

[1] HLA Hart, The Concept of Law, 2nd edition (Clarendon ,1994) 96
[2] Neil Hawke and Neil Papworth, Introduction to Administrative Law (Lawman (India) Pvt Ltd) 23.

guidance rather than none at all.[3]

Half a century ago, contract was a peripheral feature of the administrative law landscape. However, today, in contrast, contract and regulation are twin pillars of the modern architecture of governance.[4] As per Dicey, the basic premise was that government contracts should be subject to the ordinary private law; on the other hand, a history of Crown immunities and privileges reinforced the sense of an internal, executive-owned activity devoid of formal legal regulation.[5]

Before 1947, the Crown could not be sued in contract in ordinary courts, granting them feudal immunity resting on the maxim of *rex non potest peccare* (the king can do no wrong). The Crown Proceedings Act, 1947 abolished this immunity and opened the Crown to ordinary suits, barring a few categories of contract.[6]

Kagzi's historical account traces the pre-constitutional legal position where the Secretary of State for India-in-Council enjoyed sovereign immunity. This doctrine limited the enforceability of government undertakings to matters *intra commercium* (commercial transactions and proprietary rights), while sovereign acts could not give rise to a contractual claim. This position was abandoned while framing the Constitution, and the Union and States emerged as full "persons of capacity" competent to contracts as a straightforward exercise of executive power.[7]

Although contract is generally a private law matter, Indian jurisprudence which has developed over the years treated statutory contracts as raising public law questions, since such contracts cannot simply be equated with ordinary contracts between two private individuals. [8] In the case of *District Forest Officer v Ram Sanehi Singh*[9], it was held that in case of government contracts, the administrative character of the transaction deserved greater emphasis than its purely contractual character.

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[3] Prof Neil Hawke & Neil Papworth, Introduction to Administrative Law, (Lawman (India) Pvt. Ltd.) 22,23
[4] R. De Hoog and L. Salamon, 'Purchase-of-Service Contracting' in L. Salamon (ed), The Tools of Government: A Guide to the New Governance (Oxford University Press 2002); P. Vincent-Jones, The New Public Contracting (Oxford University Press 2006).
[5] P. Hogg and P. Monahan, The Liability of the Crown (3rd edn, Carswell 2000); N. Seddon, Government Contracts (3rd edn, Federation Press 2005); T. Daintith, 'Regulation by Contract: The New Prerogative' (1979) 32 CLP 41.
[6] Wade and Phillips, Constitutional Law 623 et seq (1977); G.L. Williams, The Crown Proceedings Act, 1947.
[7] M.C. Jain Kagzi, The Indian Administrative Law (6th edn, Universal Law Publishing Co Pvt Ltd) 461-462.
[8] M.P. Jain, Treatise on Administrative Law 1605.
[9]District Forest Officer v Ram Sanehi Singh, 1971 (3) SCC 864.

3. Distinguishing Executive Power to Contract from Formal Validity Requirement

Article 298 and 299(1) of the Constitution widely delineate the executive powers of the Government to trade, hold property, run businesses, and enter into legally binding contracts. This power is essentially framed in terms of—the power to enter into (or decline) any contract for any purpose is treated as an exercise of executive administrative power, which under Article 298, "must... be informed by reason, and governed by rule of law"[10].

The doctrinal separation between Article 298 and 299(1) falls mainly upon the reliance of Article 299's procedural formalities upon the substantive executive power to contract under Article 298. Article 299, by contrast, "in itself has a very limited range," prescribes only formalities of expression and execution, and says nothing about how the discretion to award contracts is to be exercised.[11] Nonetheless, Article 298 empowers the State to enter into contracts, thereby making it a "person of capacity" to exercise its executive power under Article 299 read with Article 53 of the Constitution.

Kagzi identifies three cumulative requisites for a valid *contract administratif*:

(i) it must be expressed to be made in the name of the President/Governor;

(ii) it must be in writing, though not necessarily in a formal instrument; and

(iii) it must be executed by an authorised person (or one holding special agency power, which itself need not be conferred in writing)

However, on the other hand, a series of authorities hold how Article 299(1) does not apply to statutory contracts altogether. Authorities such as *B.C. Gowda V. State of Mysore*[12] and *A. Damodaran V. State of Kerala*[13] draw a distinction between a contract made in exercise of statutory powers and one made in exercise of general executive powers. The Supreme Court in *Lalji Khimji V. State of Gujarat* summarised the position: *"There is a marked distinction between contracts which are executed in exercise of the executive powers and agreements or*

[10] M.C. Jain Kagzi, The Indian Administrative Law 459.
[11] M.P. Jain, Treatise on Administrative Law 1644.
[12] B.C. Gowda v State of Mysore, AIR 1974 Kant 135.
[13] A. Damodaran v State of Kerala, AIR 1976 SC 1533: (1976) 3 SCC 61.

orders made which are statutory in nature."[14]

The earliest case formulation represented a high-water mark of unrestricted governmental discretion. In *C.K. Achutan V. State of Kerala*[15] the government cancelled a milk-supply contract with the petitioner, who challenged this action by a writ petition under Articles 14, 19(1)(g) and 31. The court held that the aggrieved party could not claim protection under Article 14 solely since "the choice of the person to fulfil a particular contract must be left to the Government".

The watershed development occurred in 1979 in *R.D Shetty V. International Airport Authority of India*[16], where the administrative authority (IAAI) departed from its own prescribed eligibility norms in choosing a tender, albeit discriminatory and arbitrary. Bhagwati J. laid down the foundational principle that the government, unlike a private individual, *"cannot act arbitrarily at its sweet will... but its action must be in conformity with standard or norm,"* to prevent invalidity of its actions. This judgement laid down five governing propositions—(1) government has no open, unrestricted choice in awarding contracts; (2) it must act per standards/principles it has laid down; (3) it is bound by its own eligibility conditions; (4) those standards must be "rational, relevant and non-discriminatory"; (5) departure is permissible only where justified on a valid, non-arbitrary principle. [17]

Article 14 plays a significant role here, not merely to prevent discrimination through the exercise of discretionary power, but as a two-pronged structural constraint. This was realized in *Kasturi Lal Lakshmi Reddy V. State of Jammu & Kashmir*[18] wherein Justice Bhagwati identified two structural limits on government's discretion to confer largesse: first, on the terms on which such largesse is granted, and second, on the class of persons who may receive it. Both limits ultimately trace back to a single guiding principle that this activity carries a public element and must therefore be governed by public interest rather than by arbitrary preference.

This stance was further carried in *M.I. Builders V. Radhey Shyam Sahu*[19] , wherein a Lucknow Municipal Corporation contract for an underground commercial complex beneath a public park

[14] Lalji Khimji v State of Gujarat, (1993) Suppl (3) SCC 567 : JT 1993 (2) SC 89.
[15] C.K. Achutan v State of Kerala, AIR 1959 SC 490.
[16] Ramana Dayaram Shetty v International Airport Authority of India, AIR 1979 SC 1628 ('Airport case').
[17] M.P. Jain, Treatise on Administrative Law 1656.
[18] Kasturi Lal Lakshmi Reddy v State of Jammu and Kashmir, AIR 1980 SC 1992.
[19] M.I. Builders Pvt Ltd v Radhey Shyam Sahu, AIR 1999 SC 2468; M.P. Jain, Treatise on Administrative Law 1660.

was characterized as "atrocious" since it was awarded without calling any tenders.

4. **Necessity - Conflict between state flexibility and private reliance interest**

Presently, the welfare state has to look beyond the traditional sovereign duties like maintaining law and order. Changing needs and demands driven by economic development, owing to large-scale infrastructural demands, have made it necessary for government to enter into statutory contracts with private entities to deliver the citizens' dreams of development. Modern governance therefore relies heavily on statutory contracts to fill the gap in ways ranging from Public-Private Partnerships (PPPs) to public procurement to effectively execute these goals.

When statutory bodies exercise discretionary power in commercial spheres, it creates a fundamental institutional tension between state's need for flexibility (a public law concern) and private party's reliance interests (a private law matter). This dichotomy proves the inadequacy of ordinary private law contract principles. Unlike private actors who can act out of pure self-interest, statutory authorities remain bound by the obligations of fairness, proportionality and non-arbitrariness.

Consequently, courts have imported the public law standards of judicial review in the contractual realm. Dr. Jason Varuhas observed that since the landmark judgement of *Braganza V. BP Shipping Ltd. [2015] 4 All ER 639*, the Wednesbury standard of unreasonableness has been carried into this space, holding that the exercise of contractual discretion is now judged by the same principles as the public law discretion. [20] The incorporation of public law principles and bringing it under the purview of judicial review serves a dual purpose of guarding against executive overreach while protecting private parties from arbitrary statutory discretion. In *Tata Cellular V. Union of India*[21] the court later confined judicial review of tender terms to illegality, irrationality (Wednesbury unreasonableness) and procedural impropriety.

Typology and Sector-Specific Application of Statutory Contracts

1. Public Works Department (PWD) and Infrastructure Tenders

This is a traditional domain of state contracting typically conducted through standard-

[20] Jason N.E. Varuhas, 'Three Issues in the Law of Contractual Discretion' (2022) 42(3) Oxford Journal of Legal Studies 787.
[21] Tata Cellular v Union of India, (1994) 6 SCC 651.

form agreements that vest broad discretionary powers in administrative authorities, for instance, the inclusion of unilateral variation clauses or price escalation adjustments.

2. Healthcare and Medical Procurement

   This sector requires a delicate balance between public health obligations and demands of a commercial supply chain calling for stringent quality parameters, as healthcare sector demands strict transparency.

3. The Doctrine of Level Playing Field: Sports Procurement and Youth Services

   In Vinishma Technologies Pvt. Ltd. V. State of Chhattisgarh & Anr. (2025)[22] it was held that while the State retain the discretion to set the conditions of a tender, it cannot exercise that power to create an artificial barrier or a closed market to restrict competition. Doing so violates Article 14 and Article 19(1)(g), defeating the rule of a level-playing field.

4. Public-Private Partnerships and Concession Agreements

   Administrative discretion plays a central role in the modern PPP model, which forms the foundation for the rapid influx of statutory contracting.

5. Commercial and Public Procurement

   Macneil's distinction between 'discrete' and 'relational' contracts offers a useful lens through which public procurement and its legal regulation can be viewed.[23] Discretionary allocation of natural resources or public contracts on a "nomination basis" is inherently suspect under Article 14. Such allocation is permissible only under exceptional, demonstrable public interest conditions (*e.g.*, national security, emergency relief, or single-source technological monopolies).[24]

5. Limitational aspects

When the government outsources public services to private companies, the concern regarding

[22] Vinishma Technologies Pvt Ltd v State of Chhattisgarh & Anr, 2025 INSC 1182.
[23] Carol Harlow and Richard Rawlings, Law and Administration (3rd edn, Cambridge University Press) 349.
[24]'Legality of Nomination-Basis Government Contracts under Article 14' (SupremeToday AI) <https://supremetoday.ai/issue/nomination-basis-government-contract-legality-article-14>

third-party rights comes sharply into focus. Conventional contract law practices only recognize the classical bipolar model of contract. However, English Law has moved past this traditional two-party framework. For a structure that directly benefits the consumer, two conditions ought to be met—one, the public authority must have negotiated terms genuinely protecting public interest, and two, the contract must not bar the third-party beneficiary from enforcing redress for poor performance.[25]

Case law in this field sits at the intersection of ordinary private-law doctrine, the demands of public policy and administration, and the need to protect individual interests. Because the dominant common-law position still treats government contracts as governed by general private-law doctrine, courts and administrators retain considerable room to rely on informal, negotiated rules rather than formal regulation.[26]

The 1979 *Shetty* line of cases crystallised three constitutional questions that continue to structure this area: how contracts are to be awarded; whether government is free to award a contract to whomever it pleases; and the extent of judicial review available over such awards.

The Doctrine of Executive Necessity serves as a bridge between these constitutional restrictions and the law of contractual fettering. It holds that the mere fact that the State has entered into a contract cannot disable it from exercising the powers it needs for the smooth administration and welfare of the public.[27]

It is a fundamental rule of law that a local authority cannot use a contract or, indeed, any other means in order to fetter or avoid its exercise of function prescribed by statute.[28] In *Indian Aluminium Co v Kerala State Electricity Board*, the Supreme Court articulated the **non-fettering principle** along similar lines**,** in which where a stipulation is made under a public authority's *general* powers, it cannot bind the future exercise of a *statutory* power; but where the stipulation is itself an exercise of that statutory power, it validly binds the authority even at the cost of restricting its later use of the same power. [29]

Australian jurisprudence has moved away from strict rules towards a modern realistic

[25] Carol Harlow and Richard Rawlings, Law and Administration (3rd edn, Cambridge University Press) 343.
[26]Carol Harlow and Richard Rawlings, Law and Administration (3rd edn, Cambridge University Press) 367.
[27]M.P. Jain and S.N. Jain, Principles of Administrative Law, vol I.
[28] Stringer v Minister of Housing and Local Government [1971] 1 All ER 65.
[29] Indian Aluminium Co v Kerala State Electricity Board, AIR 1975 SC 1967.

approach. While India still leans towards the blunt "automatic voidness" rule, Australia is moving forward with a flexible balance between private interests and government policy changes. [30]

Another significantly practical limitation rather than a doctrinal one is that private parties, particularly the smaller contractors involved in contractual relation with the government frequently struggle with one-sided terms favouring the government, and often lack resources or legal awareness needed to invoke these doctrines effectively against the State.

6. Way Forward

The preferred mode for norms of tendering slightly inclines towards public auctioning or invitation to tenders rather than mere negotiations. This is not incidental. It ensures transparency and fairness, and also reduces the risk of bias or nepotism.[31]

As Jain observes, the function of judicial review in this context is "to prevent arbitrariness and favouritism and to ensure that the power is exercised in public interest and not for a collateral purpose", and a government decision awarding a contract in breach of this standard is liable to be quashed under Article 226.[32]

7. Conclusion

The trajectory from *Achutan's* near-total deference to the *Shetty* line's insistence on rational, non-arbitrary standards bears out Hart's opening insight: that contracting is itself an exercise of power, and one that the Constitution refuses to leave unchecked at the point of award.

Justice Bhagwati put this most directly: "Every activity of the Government has a public element in it and it must, therefore, be informed with reason and guided by public interest. Every action taken by the Government must be in public interest; the Government cannot act arbitrarily and without reason and if it does, its action would be liable to be invalidated."[33]

[30] Ansett Transport Industries (Operations) Pty Ltd v Commonwealth (1977) 139 CLR 54; Searle v Commonwealth of Australia [2019] NSWCA 127.
[31] M.C. Jain Kagzi, The Indian Administrative Law 470.
[32] M.P. Jain, Treatise on Administrative Law 1660.
[33] Kasturi Lal Lakshmi Reddy v State of Jammu and Kashmir, AIR 1980 SC 1992.