



## A Breather for Construction Projects under Litigation

*Authors: Naresh Thacker, Partner; Alok Jain, Associate Partner; Ria Dalwani, Senior Associate; Sonia Dasgupta, Associate*

Over the last few years, companies in the construction sector have been hit by cash flow concerns. While these companies may have obtained arbitral awards against government entities, it is seldom that the judgment creditor is able to secure the fruits of the award in reasonable time, considering that a challenge to the award is a likely scenario. To bring much needed relief to judgment creditors, National Institution for Transforming India Aayog (NITI Aayog) proposed measures to address the issues plaguing the construction sector, for consideration of the Cabinet Committee on Economic Affairs (CCEA).

NITI Aayog's suggested measures have been introduced in the General Financial Rules, 2017 by an amendment (referred to as the "Amendment"). The Amendment provides that government entities challenging an arbitral award shall release 75% of the award amount to the contractor/concessionaire (collectively referred to as "Contractor") in an escrow account, against a bank guarantee for the said 75%.

The Amendment assumes significant relevance, in context of proceedings for enforcement of an arbitral award under section 36 of the Arbitration and Conciliation Act, 1996 (referred to as "Act"). As per the judicial trend, courts may or may not insist on a deposit as a condition for staying the execution of an arbitral award under section 36 (3) of the Act. However, with the Amendment in place, the judgment creditor can contend before the courts that the government entity is required to deposit at least 75% of the award amount against a bank guarantee (referred to as a "BG") to proceed with a challenge to such award. The Amendment will aid the contractor/judgement creditor to secure and utilise a major portion of the amounts awarded, notwithstanding long drawn proceedings challenging the arbitral award.

### Tracing the developments in 2016 and 2019

In August 2016, CCEA approved the measures proposed by NITI Aayog, which included for government entities to pay 75% of the award to the Contractor against a BG. Accordingly, NITI Aayog issued two office memoranda dated 5 September 2016 (collectively referred to as "2016 OM") i.e., for measures to revive the construction sector<sup>1</sup> (referred to as "OM 1") and for initiatives on the measures for revival<sup>2</sup> (referred to as "OM 2"), respectively. The 2016 OM provided that Government departments / ministries shall comply with the measures set out therein and directed them to issue necessary instructions. OM 1, inter alia, provided the following reliefs to judgment creditors:

---

<sup>1</sup> Office Memorandum dated 5 September 2016 bearing reference number N-14070/14/2016-PPAU titled '*Measures to revive the Construction Sector*' issued by the NITI Aayog.

<sup>2</sup> Office Memorandum dated 5 September 2016 bearing reference number N-14070/14/2016-PPAU titled '*Initiatives on the measures for revival of the Construction Sector*' issued by the NITI Aayog.



(i) an interim payment of 75% of the arbitral award to be made to a Contractor against a BG, in the event the arbitral award was sought to be challenged by a public sector undertaking / government department (collectively referred to as “PSU”)<sup>3</sup>;

(ii) the payment was to be made by the PSU to a designated escrow account with stipulations that the amount released would be utilised in the sequence more particularly provided under OM 1.<sup>4</sup>

(iii) the Contractor shall refund the money paid by the PSU in case of a subsequent direction of the court, along with appropriate interest which would be decided by the PSU itself<sup>5</sup>.

Upon perusal of the CCEA’s Press Release<sup>6</sup> and 2019 OM (defined hereinafter), it appears that at the time of implementing the 2016 OM, there was an insistence on a BG for the interest component as well, should the subsequent court order require refund of the amount paid by the PSU. This policy of the PSUs demanding BG for the interest component was also discussed in the Supreme Court judgement in Hindustan Construction Company Limited<sup>7</sup>, wherein the Supreme Court held that the requirement of the additional BG was not arbitrary. Resultantly, the CCEA and NITI Aayog found that the policy for 75% deposit failed to achieve its objective of infusion of liquidity into the construction sector<sup>8</sup>.

In the circumstances, NITI Aayog suggested ameliorative measures which were then approved by the CCEA at its meeting held in November 2019; and encapsulated in the office memorandum dated 28 November 2019 issued by the NITI Aayog (referred to as “2019 OM”).<sup>9</sup> The 2019 OM, inter alia, prohibited the requirement of the Contractor providing BG for the interest on 75% of the arbitral award that was required to be paid by the government entity. The 2019 OM further provided that (i) in cases where the BG for interest had already been supplied by the Contractor, the same would be returned by the concerned government entity; and (ii) the opinion of a law officer of India, in consultation with the Department of Legal Affairs, must be sought prior to initiating proceedings for setting aside arbitral award(s), and any appeal(s) thereto.

### **Recent Insertion of Rule 227A in General Financial Rules (GFRs), 2017**

By a department order dated 7 October 2021, NITI Aayog directed the Department of Expenditure, Ministry of Finance (referred to as “DOE”) to incorporate the above decisions of the CCEA under the General Financial Rules (GFRs), 2017 (referred to as “GFR”). Accordingly, the DOE issued office memorandum dated 29 October 2021<sup>10</sup> to insert Rule 227A, which inter alia provided that:

---

<sup>3</sup> Paragraph 2.2 of OM 1

<sup>4</sup> Ibid.

<sup>5</sup> Paragraph 2.3 of OM 1

<sup>6</sup> Press Release dated 20 November, 2019, Press Information Bureau, Government of India, Release ID: 1592542 <<https://pib.gov.in/PressReleasePage.aspx?PRID=1592542>>.

<sup>7</sup> *Hindustan Construction Company Limited & Anr. v. Union of India & Ors.* [2019 SCC OnLine SC 1520].

<sup>8</sup> Paragraph 2 of Office Memorandum dated 28 November 2019 bearing reference number N-14070/14/2016-PPAU titled ‘*Initiatives on the measures for revival of the Construction Sector – Implementation of CCEA decision dated 31 August 2016*’ issued by the NITI Aayog.

<sup>9</sup> Ibid.

<sup>10</sup> Office Memorandum dated 29 October 2021 bearing reference number F.1/9/2021-PPD titled ‘*Insertion of Rule 227A in General Financial Rules (GFRs) 2017 – Arbitration Awards*’ issued by the Department of Expenditure, Ministry of Finance.



(i) Where the Ministry / Department (collectively “Ministry”) has challenged an arbitral award, 75% of the arbitral award (which may include interest up to the date of the award) shall be paid by the Ministry to the Contractor against a BG. The BG would only be for the said 75% of the arbitral award as above and not for the interest which may become payable to the Ministry should a subsequent court order require the refund of the amount.

(ii) The payment would be made into a designated escrow account and would be subject to the same stipulations as to its utilisation, as set out in OM 1; and

(iii) Retention money and other amounts withheld may also be released against the BG if found eligible and subject to contractual provisions.

### **Impact**

Rule 227A of the GFR seeks to align itself with CCEA’s decisions and the office memoranda issued by NITI Aayog. In a welcome move, the Amendment is likely to infuse much-needed liquidity in infrastructure companies, whose funds have either been spread thin or entangled in disputes with government entities. Rule 227A of the GFR has also been introduced at a time when construction companies are grappling with the aftermath of the pandemic.

Interestingly, in cases such as Godawari Marathawada Irrigation Development Corporation<sup>11</sup>, Candor Gurgaon Two Developers and Projects Ltd.<sup>12</sup>, and Power Mech Projects Ltd.<sup>13</sup>, the Supreme Court and high courts have recently directed deposit of 100% of the award amount before staying the enforcement of an arbitral award under section 36 (3) of Act. Therefore, the Amendment is also in consonance with the recent judicial trends, which seems to pursue the same objective i.e., secure the award amount in favour of the judgment creditor.

- *This article has been printed in Construction Week*

---

<sup>11</sup> *Manish v. Godawari Marathawada Irrigation Development Corporation Order*, dated 16 July 2018 passed by the Supreme Court in Petitions for Special Leave to Appeal (C) No. 11760-11761 of 2018.

<sup>12</sup> *SREI Infrastructure Finance Limited v. Candor Gurgaon Two Developers and Projects (P) Limited*; Order dated 14 September 2018 passed by the Supreme Court in Petitions for Special Leave to Appeal (C) Nos.20895-20897/2018.

<sup>13</sup> *Power Mech Projects Limited v. SEPCO Electric Power Construction Corporation*, 2020 SCC OnLine Del 2049.