

## Arbitrators can calculate damages on the basis of “honest guesswork” if there is insufficient evidence

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Recently, in the case of *Cobra Instalaciones Y Servicios v. Haryana Vidyut Prasaran Nigam Ltd*, the Delhi High Court (DHC) upheld the quantification of loss in an award by arbitrators done through “honest guesswork” as there was insufficient evidence on record. The DHC applied the principle set by the Supreme Court (SC) and emphasized that if there is evidence on record indicating damages, but precise details are not available, the arbitrator can use honest estimations or rough methods to calculate damages but must ensure fairness while making such calculations.

### Facts

Pursuant to a successful bidding process, the parties entered into a contract for procurement of plant, design, supply, and installation of sub-stations and bays for the Haryana Power System Improvement Project, which was to be completed within 450 days of commencement. Although the work on the project started on time, delays occurred which triggered the liquidated damages (LD) provisions. Initially, the Haryana Vidyut Prasaran Nigam Ltd. (Respondent) agreed to defer LDs, but subsequently imposed the maximum permitted LDs allowed under the contract, prompting the Cobra Instalaciones Y Servicios (Appellant) to invoke arbitration.

In examining the delays, the arbitrator attributed some delays to the Appellant's actions and others to third-party vendors. In the award, the arbitrator considered the public benefit of the project and determined that although the Respondent could not precisely quantify its losses from the delays, the Respondent should be awarded 50% of the imposed LDs. The arbitrator's decision was based on the “rough and ready” methodology established by the SC in *Construction and Design Services v. Delhi Development Authority*.

Both parties contested the award under Section 34 of the Arbitration and Conciliation Act, 1996 (Act), which resulted in a single judge overturning the award and referring the matter back to the arbitrator for reconsideration. Subsequently, the Appellant appealed under Section 37 of the Act, challenging the decision of the single judge.

### Rationale

In assessing the legitimacy of the arbitrator's decision, the DHC applied the “reasonable man” test and decided on two (2) issues, namely, whether time was of the essence of the contract resulting in damages; and, if so, what percentage of those damages were attributable to the Appellant.

The DHC ruled that though strict adherence to time was not explicitly of essence, the Respondent had repeatedly reminded the Appellant to complete the contract on schedule, and therefore, the Appellant could not have assumed that any delays in

completing the contract were inconsequential. It observed that although losses had been incurred due to delays, the LD clause did not represent a genuine pre-estimate of damages.

Upholding the award, the DHC ruled that arbitrators are permitted to use the “rough and ready” method or “honest guesswork” method when quantifying damages, a practice endorsed not only by the SC but also by other State High Courts, which predates the ruling in the *Construction and Design Services* case. The rationale behind this approach is that if the arbitrator has evidence indicating that damages have occurred but lacks detailed insights, then the arbitrator should have the discretion to employ an honest guesswork or rough method to assess damages. In addition, the DHC held that as the loss incurred could not be attributed to one contractor damages should be distributed on a *pro rata* basis.

### **Our comments**

Applying the “honest guesswork” approach in such cases has certain benefits, as it gives arbitrators some leeway in deciding LDs even in the absence of precise information. Moreover, this approach helps when the aggrieved party is a government body, and the project has public importance. Additionally, per the Supreme Court’s observations in the *ONGC Ltd. v. Saw Pipes Ltd* case, proving actual losses in public projects is difficult as such projects may not necessarily be revenue generating projects.

Although using the “honest guesswork” method at the arbitral stage seems to be time and cost efficient because it eliminates the need to gather detailed evidence or expert opinions, parties often contest such awards under Section 34 of the Act. Sometimes, using “honest guesswork” may result in inaccuracies in assessing damages, leading to unfair outcomes for one or more parties. Additionally, arbitrators’ subjective judgment can be influenced by personal biases or perceptions, raising concerns about impartiality.

Overall, although, the use of honest guesswork is a pragmatic way to calculate damages and resolve disputes, especially when detailed information is lacking, it carries certain risks of inaccuracy and lack of transparency that may undermine the legitimacy of the arbitration process. The SC should come out with guidelines in this regard and should also clarify that this approach should be one of last resort. Additionally, arbitrators should use this approach only when determining damages is “impossible” and not “improbable.”

Similarly, negotiating lawyers must consider including globally acceptable standards to assess damages in commercial contracts, and ensure that LD clauses encompass a wide range of default scenarios.