

MP-IDSA

Policy Brief

Draft DPP-2020: Standard Contract Document

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May 14, 2020

S*ummary*

The policy brief examines the Standard Contract Document (SCD) of the draft Defence Procurement Procedure 2020 (DPP-2020), released by the Ministry of Defence (MoD) for public comments. Part I of the brief examines six new articles included in the new SCD, while Part II delves into some significant changes made in the existing articles. Two additional provisions – Entire Document Clause and Limitation of Liability – which could be considered for inclusion in the SCD are discussed in Part III of the brief.

The draft Defence Procurement Procedure 2020 (DPP-2020), released by the Ministry of Defence (MoD) on March 20, 2020, contains a Standard Contract Document (SCD). It is intended to serve as the template for all contracts to be signed under various procurement categories.¹ In its present form, the SCD was first introduced in DPP-2005. Some sporadic changes made in the template since then pale in comparison with the changes made in the SCD in the draft DPP-2020. Part I of this brief examines six new articles (or clauses) included in the new SCD, while Part II delves into some significant changes made in the existing articles. Some additional provisions which could be considered for inclusion in the SCD are discussed in Part III. The description of various articles given in this policy brief only represents their main features/gist and is not intended to substitute the actual text of the SCD in the draft DPP-2020.

PART I

New Articles

Article 6: Monitoring of Project Based on Contractual Milestones

This new article provides for monitoring of projects with reference to the mutually negotiated milestones specified in the contract. This is to ensure smooth progress of the project through periodic reviews. The need for project monitoring is unquestionable, but it is inexplicable that this article gives the right but does not cast any obligation on the MoD to monitor the projects. The buyer must also play its part in the successful execution of a contract by not only continuously monitoring its progress but also taking timely action to prevent/remove roadblocks that threaten to frustrate the contract.

Sub-clause (3) of this article empowers the MoD to invoke the termination clause of the contract if the project does not progress as per the contractual milestones. This sub-clause can be deleted as it overlaps with Article 22A of the SCD which covers 'Termination for Default in Delivery or Meeting Milestones by the SELLER'.

Article 12: Title and Risk of Loss

This article specifies when the title of the equipment would get transferred from the seller to the buyer and the documentation required for effecting the transfer. It also specifies the liability of the seller to make good any loss or damage suffered by the

¹ For different procurement categories, see Chapter I on Acquisition Categories, Acquisition Planning and Indigenous Content, in [“Draft DPP-2020”](#), Ministry of Defence, Government of India, March 20, 2020. For an analytical review of the draft DPP-2020, see Laxman Kumar Behera, Vinay Kaushal and Amit Cowshish, [“Refining Draft DPP 2020: Some Suggestions”](#), MP-IDSA Policy Brief, April 08, 2020.

buyer due to any defect in title, quality, and performance of the equipment after delivery/transfer of title but before final acceptance/installation, etc.

This liability will survive termination of the contract, where the buyer chooses to exercise the option of taking over the partially built material at the book value, certified by the buyer-appointed auditors/licensed surveyors. The appointment can, however, be challenged, and if the matter cannot be resolved amicably, it will be settled “as per the dispute resolution procedure”, which seems to imply arbitration.

The text of this article is too wordy and requires to be broken down into clearer sub-clauses.

Article 31A: Buyer’s Rights to Optimise Life Cycle Support Costs and System Enhancements through Indigenous Ecosystem

Like Article 12 on ‘Title and risk of loss’, this newly added article is also long-winded and requires clearer articulation. It is divided into three sub-clauses. While the first two sub-clauses deal with the intellectual property rights (IPR) of the seller (sub-clause 31A.1) and the buyer (sub-clause 31A.2) respectively, the third sub-clause (31A.3) stipulates the conditions under which the buyer could exercise his rights.

The significance of this clause lies in the fact that, for the first time, it expressly acknowledges the seller’s IPR over the equipment being supplied under the contract. But it also empowers the buyer to substitute the originally fitted assemblies/sub-assemblies, etc., with indigenised items and to encourage indigenous development of spares and associated equipment like simulators, as well as improvement/modification of the system. The seller can, of course, take part in this endeavour.

According to this article, the seller will not be liable for the items that have been indigenised/substituted or modified/improved but will continue to be liable for the part that is unaffected by such changes. Exercise of these rights by the buyer will be subject to the provisions of the contract and the rights of the third parties. While it is undoubtedly imperative to have such a provision in defence contracts if indigenisation is to be given a fillip, this article could possibly give rise to several irreconcilable disputes, not just on account of its implications but also the way it is worded.

Article 33A: Life Cycle Support Contract

This is probably the longest article in the SCD which provides for simultaneous signing of the Life Cycle Support Contract (LCSC) and the main contract. While the note below the heading of this article says that it is “to be included, if applicable, and as specified in (the) RFP” [Request for Proposal], the very first sentence of the article says that it “would be signed along with the main acquisition contract *for all equipment*” [emphasis added]. This apparent contradiction notwithstanding, it is not

clear why this article has been included in the SCD if, as stated therein, the LCSC is to be signed separately, albeit simultaneously with the main contract.

Be that as it may, the LCSC is intended to cover the supply chain, spares, special tools, repairs, services of specialists, creation of maintenance eco-system, and obsolescence management. Spare parts and repair support will have to be provided through rate contracts covering (i) Itemised Spare Parts Price Lists (ISPPL), (ii) Repairable Items Price Lists (RIPL), (iii) Man-Day Rates for Services/Special Tools, and (iv) Lifetime buy of spares if the production line is closing down.

To facilitate online placement of orders, the seller will be required to provide access to its Online Inventory Management System (OIMS) in all cases beyond Rs 300 crores, but this requirement will be optional for procurement cases that fall in the powers delegated to the services. The seller will also have to provide the methodology for undertaking Active Obsolescence Management through the entire life cycle of the equipment, including upgradation of the system/subsystem/units on completion of its fair service life.

Article 39: Severability

This article provides that if any provision of the contract is found to be invalid or unenforceable, both the parties will continue to perform the remaining unaffected provisions of the contract, unless “the ineffectiveness of such provision would result in such a material change as to cause completion of the transaction contemplated hereby to be unreasonable”, in which case the parties will renegotiate in good faith to ‘reform’ the contract suitably (to achieve the objective of the contract), failing which the matter will be submitted to arbitration in terms of Article 24 of the SCD.

It is good to have such a clause, though not necessarily in all types of contract, particularly those contracts in which severance of a part of the contract could defeat its very purpose. The objective of this article will be better served if the stipulation quoted in the previous para is substituted by a simpler formulation which provides that the parties will continue to perform that part of the contract which is unaffected by invalidity or unenforceability of any of its part, ‘unless such continuation defeats the very purpose of the contract’ which, needless to say, must be defined in the Preamble of every contract.

Article 40: Survival After Termination or Expiration

As the name suggests, this new article lists out the articles which will survive termination or expiration of the contract. This list includes the articles on Arbitration; Non-Disclosure of Contract Documents; Title and Risk of Loss; Warranty; Law; Penalty for Use of Undue Influence; and, Patents and other Industrial Property Rights.

Part II

Significant Changes in Existing Articles

Preamble

The preamble to the SCD has been revised to include a few definitions of the standard terms used therein and a description of the order in which various articles and other provisions incorporated in the contract will take precedence over one another for the purpose of interpretation of the contractual terms. It also provides for an opportunity to either party – buyer and seller – to notify the other party about any inconsistency in the contract or any connected document, so that it could be resolved in accordance with the said order of precedence.

These changes in the Preamble of the SCD are welcome but two aspects stand out. One, not all terms used in the SCD have been defined in the Preamble. The term ‘transshipment’ used in Article 5A.8 is a case in point. There are many other terms used in the contract which have not been included in this part of the Preamble. Incidentally, the term ‘Expiration of Contract’ is mentioned in the Preamble, but it has been left undefined.

Two, the first paragraph of the Preamble ends with the provision that “the SELLER assures the BUYER that the BUYER has the right to have the supplies manufactured in India through a nominated agency and supply it to the BUYER”. The seller can acknowledge or concede this right in the contract document but cannot ‘assure’ the buyer of this right. Moreover, this provision would be applicable to the contracts under the Buy and Make category which, in any case, entails licensed production in India.

It will not be applicable to contracts under the Buy (Global) category as in those cases it will conflict with the clause on the IPR of the seller. It will also not be relevant in the case of procurements under the new Buy (Global – Manufacture in India) included in the draft DPP-2020 as this category entails manufacturing of the equipment in India by the vendor himself.

Article 13: Transportation

The existing article on transportation in DPP-2016 contains separate textual formulations for transportation by sea and air, and also mentions certain International Commercial Terms (INCOTERMS)² for delivery of goods, giving MoD the

² As per INCOTERMS, DDP “means that the seller delivers the goods when the goods are placed at the disposal of the buyer, cleared for import on the arriving means of transport ready for unloading at the named place of destination. The seller bears all the costs and risks involved in bringing the goods to the place of destination and has an obligation to clear the goods not only for export but also for import, to pay any duty for both export and import and to carry out all customs formalities”; and Delivered at Place (DAP) “means that the seller

option to select the term considered appropriate in individual cases. The chosen term is indicated in the RFP and later incorporated in the contract.³ The existing article has been replaced by a simple formulation in the draft DPP-2020 which provides that (a) the stores shall be delivered on Delivered Duty Paid (DDP) INCOTERM, (ii) the date of the Certified Receipt Voucher (CRV) shall be considered as the date of delivery, and (iii) part shipment of goods will be permitted.

In a broad sense, the term DDP means that the seller would bear the cost of, and undertake all other risk/responsibilities for, delivering the goods at the destination specified in the contract. The buyer faces no risk and incurs no cost under the DDP terms till the goods are unloaded at the destination, which is usually the buyer's premises. While this frees the buyer from the hassles and the cost of getting the goods cleared for imports and inland transportation to the destination, it could be slightly cumbersome for the foreign sellers.

Article 21: Taxes and Duties

DPP-2016 has a simple, though probably also a bit problematic, clause on taxes and duties which provides that "All taxes, duties, levies and charges which are to be paid for the delivery of goods, including advance samples, shall be paid by the parties under the present contract in their respective countries."⁴ There is a subtle, almost imperceptible, change in this clause in the draft DPP-2020.

The new clause reads: "All taxes, duties, levies and charges which are to be paid for the deliverables, including advance samples, shall be paid by the parties under the present Contract. All Indirect Taxes and Duties will be paid at actuals or as quoted by the SELLER, whichever is lower. In case of any change in the tax structure/rates by BUYER's Government, only incremental change will be paid. The same will not require any Contract amendment."

While the provision that payment which becomes due because of any change in the tax structure will not require any amendment to the contract and will cut down the delay that such amendments normally entail, the stipulation that 'only incremental change' will be paid is confusing. Secondly, the stipulation that the taxes and duties will be paid as quoted by the seller or 'on actuals', whichever is lower, maybe iniquitous. The taxes and duties should always be paid 'on actuals.'

Most importantly, the text of this clause seems to suggest that the foreign sellers may have to pay taxes, if any, related to the delivery of the goods in India, as the

delivers when the goods are placed at the disposal of the buyer on the arriving means of transport ready for unloading at the named place of destination. The seller bears all risks involved in bringing the goods to the named place." See "[Global Trade Guide](#)", *IncoDocs*, March 2020.

³ "[Defence Procurement Procedure 2016](#)", *Ministry of Defence*, Government of India, p. 424.

⁴ *Ibid* p. 428.

contracts are supposed to be on DDP terms under which the seller incurs the risk and cost of delivery at the designated destination. This may be problematic for some foreign vendors.

Article 22A: Termination

This article subsumes the existing article on termination in DPP-2016 and also provides for (i) taking over of the partially built material, designs, drawings and documents, etc., in the event of premature termination, (ii) risk purchase by the buyer at the cost of the seller, and (iii) full or partial termination of the contract in public interest. There are several sub-clauses of this article, each of which is applicable to the types of contract as indicated in the SCD.

The risk (and expense) sub-clause empowers the buyer to procure requisite material for fulfilment of the seller's obligations under the contract (if he fails to discharge those obligations) from alternative sources at the seller's risk, responsibility and cost. It also requires the seller to agree to all such costs incurred by the buyer being recovered from him. Such clauses are normally associated with procurements under the rate contracts. It remains to be seen how this clause will be implemented in the context of the capital acquisitions, considering that one of the generally acknowledged pre-conditions – though not specifically mentioned in the SCD – for invocation of this clause is that the specifications of the material procured from the alternative sources should be exactly the same as those mentioned in the contract.

The provision for termination of contract in public interest is ostensibly meant to protect the interest of the buyer in unforeseen circumstances that may call for cancellation of the contract, either fully or partially. The relevant sub-clause provides for a written notice to be given to the seller before termination of the contract, without prejudice to the seller's legal rights. The legal rights of the seller notwithstanding, this sub-clause would act as the proverbial Damocles sword over the seller's head as 'public interest' is not a defined term and lends itself to self-serving interpretations by the buyer.

The new clause seems to be influenced by Article 9.8.3 (Termination of Contract for Convenience) of the Ministry of Finance's (MoF) *Manual for Procurement of Goods 2017*. However, while the MoF's manual clearly states that the seller "has to be persuaded to acquiesce" and needs to be suitably compensated,⁵ the new sub-clause in the SCD is silent on this.

There is another alternative Article 22B in the SCD which also deals with termination of contracts, but it is applicable to shipbuilding contracts only. Considering that there is a separate full-fledged and self-contained chapter on shipbuilding and ship

⁵ ["Manual for Procurement of Goods 2017"](#), Ministry of Finance, Government of India, p. 134.

repairs in the draft DPP-2020 – which should actually be delinked from the DPP and notified as a separate procedure as it is relevant only for the Indian Navy and the Coast Guard - inclusion of this article in the SCD needs reconsideration.

Part III

Miscellaneous

Entire Document Clause

An ‘Entire Document Clause’ in a contract makes it a self-contained document. This clause acts as an assurance for both the parties, especially the seller, that the contract will be governed only by the provisions explicitly mentioned in it. Inclusion of this clause in complex defence contracts would impart an element of finality to the contractual provisions. It will also prevent the parties from invoking extraneous provisions of the DPP or any other document in the context of disputes about fulfilment of the contractual obligations. This assurance is important as, at times, the negotiated terms incorporated in the contracts vary from the corresponding provisions in the DPP, in which case the contractual provision must prevail.

It bears recalling that some offset contracts have run into problems in the past due to variations between the express contractual clauses and the text of the corresponding provisions in the relevant chapter in the DPP. Inclusion of an ‘Entire Document Clause’ would go a long way in preventing such situations and removing uncertainties in the execution of the contracts. Inclusion of this clause in the SCD will not take away the buyer’s right to decide to what extent it wants to deviate from the DPP/RFP provisions at any stage till the negotiations are over. This clause will only ensure that once the terms and conditions are negotiated and finalised by inclusion in the contract, these cannot be given a meaning, by invoking extraneous provisions of the DPP/RFP, etc., which is different from what the parties intended them to mean when they agreed to their inclusion in the contract.

Limitation of Liability

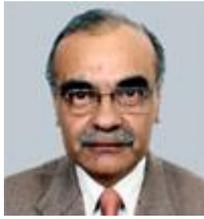
The foreign companies have for long been seeking inclusion of a clause on ‘limitation of liability’ in the SCD. They would be disappointed by its non-inclusion in the draft DPP-2020. This omission could be a cause for concern for the Indian industry as well as it also requires to operate in an environment of predictability about the extent of their liability under a contract. The absence of this clause in the SCD exposes the seller to an open-ended liability for losses caused to the user or any third party due to any defect in, or malfunctioning of, the equipment during, or arguably even after, the warranty period.

Inclusion of this clause in the SCD, capping the seller's liability during and after the warranty period, needs to be considered. The cap could vary, depending on the nature of the equipment contracted for, but it needs to be mentioned upfront in the RFP and later included in the contract. This issue has been hanging fire for close to a decade. It would be desirable to put an end to this legacy issue either by including the clause in the DPP or making it clear to the industry that it is not acceptable to the MoD.

Summing up

Inclusion of new clauses in the draft DPP-2020 and changes made in some of the existing ones are intended to make the SCD more comprehensive, in tune with the procurement policies and procedures that MoD considers necessary for promoting Make-in-India in defence. However, there is a scope for bringing about textual clarity in the new, as well as some of the existing, clauses of the SCD, especially those which have been modified. There is also a case for considering the inclusion of the two clauses mentioned in Part III, apart from considering all suggestions MoD may have received from the various stakeholders.

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