



Arbitration Update

October 13, 2017

SUPREME COURT REITERATES THAT AN ARBITRATOR CANNOT AWARD PENDENTE LITE INTEREST IF PAYMENT OF INTEREST IS BARRED BY THE CONTRACT

SRI CHITTARANJAN MAITY. (“MAITY”) V. UNION OF INDIA (“UOI”) (3 OCTOBER 2017)

- Maity and UOI entered into a contract for a railway works project (“Contract”). Disputes arose between the parties and Maity referred the disputes to arbitration. The arbitral tribunal awarded the claim amount along with interest for the pre-reference period and pendente lite interest, by an Award dated 6 November 2010 (“Award”). Pertinently, the Contract contained a clause expressly barring payment of interest on amounts payable to Maity.
- UOI filed an application under Section 34 of the Act for setting aside the Award and the same was dismissed by the Learned Single Judge. The decision of the High Court was challenged before the Division Bench of the High Court. The Division Bench held in favour of UOI and set aside the Award and the order of the Learned Single Judge, and directed a fresh reference of disputes before the arbitral tribunal. Maity filed a Special Leave Petition before the Supreme Court.
- The issue which arose for consideration before the Supreme Court was whether the arbitral tribunal was justified in awarding interest on delayed payments, when the Contract prohibited awarding interest.
- The Supreme Court clarified that Section 31 (7) (a) of the Arbitration and Conciliation Act, 1996 (“Act”) which provides for payment of interest, begins with the words “unless otherwise agreed by the parties” and therefore bars an arbitrator from awarding interest when the contract itself prohibits the award of interest for the pre-award period i.e. pre-reference and pendente lite period.
- Relying upon *Sree Kamatchi Amman Constructions v. Divisional Railway Manager (Works), Palghat and Others*¹ and *Union of India v. Bright Power Projects (India) Pvt. Ltd.*², the Supreme Court concurred that when the terms of the agreement prohibits award of interest, the arbitrator cannot award interest for the pendente lite period.
- Based on the above findings, the Supreme Court held that Maity is not entitled to any interest on the award amount. Having regard to the facts and circumstances of the case, the Supreme Court directed that UOI is not entitled to recover the excess amount withdrawn by Maity from the deposit, even though Maity had withdrawn amounts exceeding the award amount exclusive of interest.

THE KARNATAKA HIGH COURT HOLDS THAT A COURT IS EMPOWERED TO APPOINT ARBITRATOR WHEN NOMINATED ARBITRATORS DECLINE APPOINTMENT

JMC PROJECTS (INDIA) LIMITED (“JMC”) V. BANGALORE METRO RAIL CORPORATION LIMITED (“BMRC”) (6 SEPTEMBER 2017)

- JMC and BMRC entered into a contract for the construction of elevated structures (“Contract”). The terms of the Contract provided for claims exceeding Rs.15 million to be adjudicated by three arbitrators. The selection of arbitrators was to be made from a panel of 5 members nominated by BMRC. From the panel of 5 members, each party was to choose one arbitrator and the two arbitrators were to choose the third arbitrator.
- In the present case, since the claim exceeded Rs.15 million, BMRC constituted a panel of 5 members. JMC selected a nominee from the panel. The nominee arbitrator however, declined to accept the nomination. JMC thereafter appointed another nominee from the remaining members of the panel and again, the nominated arbitrator declined the appointment. Out of the three remaining arbitrators on the panel, one arbitrator indicated his unwillingness to act as arbitrator.
- BMRC then constituted a fresh panel of 5 arbitrators. JMC however filed an application under Section 11(6) of the Arbitration and Conciliation Act, 1996 (“Act”) before the High Court of Karnataka for the constitution of the arbitral tribunal. BMRC opposed the application.
- The High Court took note of the fact that the Contract did not envisage any contingency procedure in the event the nominated

¹ (2010) 8 SCC 767

² (2015) 9 SCC 695

arbitrator declined the appointment. Further, since only two members remained on the panel, constitution of the arbitral tribunal in the manner provided in the Contract (i.e. a 3 member tribunal) was not possible.

- The High Court relied on a letter addressed by BMRC wherein BMRC had taken the stand that there is no provision in the Contract for providing a fresh panel. The High Court held that since the parties understanding of the clause was that no fresh panel was to be constituted and since only 2 members remained on the panel, the constitution of the three member arbitral tribunal became unworkable.
- The High Court relied upon *San-A Trading Company Ltd. v. I.C. Textiles Ltd.* 3., and held that when the contract does not prescribe a procedure authorizing the appointment of another arbitrator the contractual clause shall cease to operate, and it would be for the court to appoint an arbitrator under Section 11 (6) of the Act once such contractual clause is rendered exhausted.
- Relying upon *S.B.P. and Company v. Patel Engineering Ltd.*, 4 the High Court held that the appointment of a substitute arbitrator cannot be assumed as an implicit right of the party when the contract does not provide for the appointment of an alternate arbitrator in case the nominated arbitrator rejects the appointment.
- The Court held that it stood empowered to constitute the arbitral tribunal and accordingly constituted a 3 member arbitral tribunal.
- It is debatable whether a Court appointing an arbitrator when the nominated arbitrator declines, is permissible. In accordance with Section 15 of the Act, when an arbitrator withdraws from office, the mandate of the arbitrator terminates and a substitute arbitrator is to be appointed according to the rules which were applicable to the appointment of the arbitrator being replaced. If parties are permitted to approach the court under Section 11 when an arbitrator declines to accept the nomination, the question is, whether it would be in derogation of a parties' right to substitute the arbitrator in accordance with Section 15 of the Act.

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³ (2012) 7 SCC 192
⁴ (2009) 10 SCC 293