SC: EMPLOYEE OF A PARTY ALLOWED AS 'ARBITRATOR' IN PROCEEDINGS INITIATED PRIOR TO 2015 AMENDMENT TO THE ARBITRATION AND CONCILIATION ACT

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On 12 September 2017, the Supreme Court of India, in the matter of Aravali Power Company Private Limited Vs. M/s Era Infra Engineering Limited[1] set-aside the common judgment and order dated 29 July 2016 passed by the Delhi High Court in OMP (T) No. 13/2016 filed under Section 14 of the Arbitration and Conciliation Act, 1996 (hereinafter referred to as "the 1996 Act") seeking termination of mandate of the arbitrator and Arbitration Petition No. 136/2016 filed under Section 11 (6) of the 1996 Act for appointing an independent arbitrator for adjudicating disputes between the parties.

Background

The matter involved an interesting proposition of law in dealing with a challenge raised by Era Infra before the Delhi High Court in two separate petitions filed against Aravali Power under Section 14 and 11(6) of the 1996 Act, *inter alia*, on the grounds of apprehension of bias and justifiable doubts as to the independence and impartiality of the nominated arbitrator appointed as per the arbitration agreement between the parties. The Delhi High Court allowed both petitions holding that Section 12 of the 1996 Act even prior to the amendment in 2015, maintained the neutrality of arbitrators and emphasised appointment of independent and impartial arbitrators so that the arbitration procedure is fair and unbiased.

In the present case, Aravali Power awarded a contract to Era Infra for construction work of permanent township for Indira Gandhi Super Thermal Power Project at Jhajjar. The relevant portion of the arbitration agreement contained in the contract stipulated as under:

"*56. Arbitration:-*

... shall be referred to the Sole Arbitration of the Project In-charge of the Project concerned of the owner, and if the Project In-charge is unable or unwilling to act, to the sole arbitration of some other persons appointed by the Chairman and Managing Director, NTPC limited (Formerly National Thermal Power Corporation Ltd) willing to act as such Arbitrator. There will be no objections, if the Arbitrator so appointed is an employee of NTPC Limited (Formerly National Thermal Power Corporation Ltd), and that he had to deal with the matters to which the contract relates and that in the course of his duties as such he had expressed views on all or any of the matters in disputes or difference. The Arbitrator to whom the matter is originally referred being transferred or vacating his office or being unable to act for any reason as aforesaid at the time of such transfer, vacations of office or inability to act, Chairman and Managing Directors, NTPC limited (Formerly National Thermal Power Corporation Ltd.), shall appoint another person to act as Arbitrator in accordance with the terms of the contract..."

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Era Infra *vide* letter dated 29 July 2015 sought appointment of an arbitrator, being a retired judge of the High Court, for adjudication of disputes which had arisen between the parties on account of delay in completion of the contract by disputing the arbitration agreement, *inter alia*, on the ground that "nobody can be a judge in his own cause" and sought reference to an independent tribunal. Aravali Power, while refuting the contentions raised by Era Infra, proceeded to appoint its chief executive officer as the sole arbitrator on 19 August 2015. Accordingly, the parties appeared before the sole arbitrator on 7 October, 2015 and thereafter Era Infra on 4 December, 2015 sought extension of time to file its statement of claim. However, Era Infra did not raise any dispute regarding the appointment or continuation of the arbitration proceedings. According to the record, the sole arbitrator granted one month's time, as prayed for.

On 12 January, 2016, Era Infra sought to challenge the appointment of the arbitrator and raised an objection regarding constitution of the arbitral tribunal. The sole arbitrator ruled on his jurisdiction and rejected Era Infra's contention on the ground that it had participated in the arbitral proceedings on 7 October, 2015 without raising any protest. Era Infra was then intimated to attend proceedings in the arbitration scheduled to be held on 16 February 2016. Era Infra however, approached the Delhi High Court by filing petitions as aforesaid, seeking termination of the mandate of the arbitrator and for appointing an independent arbitrator.

The Delhi High Court by its common judgment and order dated 29 July 2016 set aside the appointment of the arbitrator primarily on the grounds that "*justice should not only be done but it must also seen to be done*" and that appointment of the CEO as arbitrator is likely to give rise to justifiable doubts as to his neutrality. The Delhi High Court directed Aravali to suggest names of three panel arbitrators from different departments to Era

...so long as there is no justifiable apprehension about his independence or impartiality, the appointment could not be rendered invalid...

Infra who could thereafter choose any one of them to be the arbitrator in the matter. It was directed that in the event of failure by Aravali Power to suggest an appropriate arbitrator, Era Infra would be at liberty to revive the petitions, in which case the Court would appoint a sole arbitrator from the list maintained by Delhi International Arbitration Centre. It was also observed that the arbitrator was CEO of Aravali Power and was previously involved in cases/ contract works similar to the one involved in the present case and it could not be disputed that the decisions of part cancellation were taken at the highest level of Aravali Power. In the circumstances, the Delhi High Court found that the apprehension entertained by Era Infra was reasonable and not a vague or general objection.

In the above background, Aravali Power preferred a Special Leave Petition before the Supreme Court of India challenging the said order dated 29 July 2016 passed by the Delhi High Court on the ground that the appointment of the arbitrator was completely in tune with Clause 56 of the GCC and there was no occasion for the Delhi High Court to exercise any power or jurisdiction and that the 1996 Act contemplated clear and definite procedure for challenging the arbitrator, and even if such challenge were to fail the remedy under Section 13 of the 1996 Act was specific and of different nature. To the extent the Delhi High Court had directed Aravali Power to submit three names from its panel of arbitrators from which list Era Infra was to select the sole Arbitrator, Aravali Power challenged that part of the judgment by filing SLP (Civil) Nos. 503-504 of 2017.

Judgment

The Supreme Court, at the very outset, observed that the parties invoked arbitration on 29 July, 2015, the arbitrator was appointed on 19 August, 2015 and the parties appeared before the arbitrator on 7 October, 2015, well before 23 October 2015 *i.e.* the date on which the 2015 Amendment was deemed to have come into force. It was *prima facie* held that the statutory provisions that would therefore govern the present controversy are those that were in force before the 2015 Amendment came into effect. The Supreme Court further relied on the judgment in the matter of *Indian Oil Corporation Ltd. and Others v. Raja Transport Private Ltd.*[2] while holding that the fact that the named arbitrator happens to be an employee of one of the parties to the arbitration agreement has not by itself, before the 2015 Amendment came into force, rendered such appointment invalid and unenforceable. It was observed that the sole arbitrator undoubtedly was an employee of Aravali Power but so long as there is no justifiable apprehension about his independence or impartiality, the appointment could not be rendered invalid and unenforceable.

The Supreme Court while discussing the judgment passed in the matter of *Northern Railway Administration, Ministry of Railway, New Delhi v. Patel Engineering Company Ltd.*[3], along with various other judgments, observed and held that referring the disputes to the named arbitrator, by way of an arbitration agreement, shall be the rule. The Chief Justice or his designate will have to merely reiterate the arbitration agreement by referring the parties to the named arbitrator or named arbitral tribunal. Ignoring the named arbitrator/ arbitral tribunal and nominating an independent arbitrator shall be the exception to the rule, to be resorted for valid reasons.

The Supreme Court also discussed the judgment passed in the matter of *Voestalpine Schienen GMBH vs. Delhi Metro Rail Corporation Limited*[4] and distinguished the same by observing that this was the only decision in which the invocation of arbitration was after the 2015 Amendment but the same would not apply to the facts of the present case.

In light of the rival contentions, the Supreme Court held as under:

- Except the decision of this Court in *Voestalpine Schienen GMBH* (supra) referred to above, all other decisions arose out of matters where invocation of arbitration was before the 2015 Amendment came into force. *Voestalpine Schienen GMBH* (supra) was a case where the invocation was on 14 June, 2016 *i.e.* after the 2015 Amendment and the observations in para 18 clearly show that since "the arbitration clause finds foul with the amended provisions", the Court was empowered to appoint such arbitrator(s) as may be permissible.

- The ineligibility of the arbitrator was found in the context of amended Section 12 read with Seventh Schedule (which was brought in by the 2015 Amendment) in a matter where invocation for arbitration was after the 2015 Amendment had come into force. It is thus clear that in cases prior to the 2015 Amendment, the law laid

down in *Northern Railway Administration* (*Supra*), as followed in all the aforesaid cases, must be applied, in that, the terms of the agreement ought to be adhered to and/or given effect to as closely as possible.

• The jurisdiction of the Court under Section 11 of 1996 Act would arise only if the conditions specified in clauses (a), (b) and (c) are satisfied. The cases referred to above show that once the conditions for exercise of jurisdiction under Section 11(6) were satisfied, in the exercise of consequential power under Section 11(8), the Court had on certain occasions gone beyond the scope of the concerned arbitration clauses and appointed independent arbitrators. What is clear is, for exercise of such power under Section 11(8), the case must first be made out for exercise of jurisdiction under Section 11(6) of the 1996 Act.

In view of the above, the Supreme Court allowed the appeal filed by Aravali Power and held that:

• Observations of the High Court show that the exercise was undertaken by the High Court, "in order to make neutrality or to avoid doubt in the mind of the petitioner" and ensure that justice must not only be done and must also be seen to be done.

• In effect, the High Court applied principles of neutrality and impartiality which have been expanded by way of the 2015 Amendment, even when no cause of action for exercise of power under Section 11(6) had arisen.

• The procedure as laid down in Section 12 of the 1996 Act prior to the 2015 Amendment mandated disclosure of circumstances likely to give rise to justifiable doubts as to independence and impartiality of the arbitrator. It is not the case of Era Infra that the provisions of Section 12 of the 1996 Act in un-amended form stood violated on any count. The provision contemplated clear and precise procedure under which the arbitrator could be challenged and the objections in that behalf under Section 13 of the 1996 Act could be raised within prescribed time and in accordance with the procedure detailed therein. The record shows that no such challenge was raised within the time and in terms of the procedure prescribed.

• As a matter of fact, Era Infra had participated in the arbitration and by its communication dated 4 December 2015, had sought extension of time to file its statement of claim.

• Accordingly, it was held that the Delhi High Court was clearly in error in exercising jurisdiction in the present case and it ought not to have interfered with the process and progress of arbitration. Therefore, the challenge raised by Aravali Power was accepted and the contentions raised by Era Infra were rejected.

Comment

The judgment delivered by the Supreme Court comes as a step back in implementing the true nature and spirit of the 1996 Act particularly with the advent of the 2015 Amendment and is conservative in approach in the light of the judgment of the Supreme Court in the *Voestalpine* Case (*Supra*).

The primary reason for allowing the employee of a party to continue as the nominated arbitrator by the Supreme Court is the distinction sought to be drawn with the pre-2015 Amendment period as compared to the post-2015 Amendment period. However, the Supreme Court ignored the legal position that existed even prior to the 2015 Amendment in as much as the principles of independence and impartiality were embedded in the provisions contained in Section 12 read with Section 11(8) of the 1996 Act even prior to the 2015 Amendment. The 2015 Amendment clarified the position by emphasising specific categories under Schedule V and VII of the 1996 Act.

Even on facts, the Supreme Court has ignored the factual findings of the Delhi High Court that though the CEO of Aravali Power was not the Engineer-in-Charge or the day-to-day in-charge of the work which was to be performed by Era Infra, but those who were responsible for such day-to-day work ultimately reported to the CEO. Therefore, the CEO had a controlling influence in Aravali Power against whom Era Infra sought to assert claims. In view of the above, circumstances existed for Era Infra to have justifiable doubts as to the independence and impartiality of the tribunal or that the arbitration procedure would be fair and unbiased.

Independence and impartiality are the touchstone of any adjudication process and more so in an arbitration process, where it is an alternative dispute resolution mechanism created by agreement between the parties. The endeavour of the legislature and the judiciary in the recent past has been to promote faster dispute redressal through mechanisms like – arbitration as compared to tardy and cumbersome Court process. Therefore, the role of fairness, independence and impartiality of the tribunals are indispensable. In view of limited judicial interference in the adjudication and post-adjudication stage, it is quintessential that there is a fair and unbiased adjudication. Apprehension of bias or justifiable doubts to the independence and impartiality of arbitral tribunals are to be resolved at the very outset rather than leaving it to a challenge at a later stage so as to avoid multiplicity of judicial proceedings, which has been one of the primary objectives of alternative dispute resolution. The whole scheme behind ensuring independence and impartiality of an arbitrator is to provide the necessary confidence and relief to contesting parties involved in the process of dispute resolution by resorting to the machinery of alternative disputes redressal. This becomes more important when a private party is contracting with a dominant government undertaking or a public sector undertaking (PSU), where the private party has minimal negotiating powers. In view of settled legal position, such government undertakings/ PSUs may strive to defend claims of the private contracting parties on merits rather than resorting to technical pleas.

Though the arbitration proceedings which have commenced post 2015 Amendment will continue to reap the benefits of the order passed in *Voestalpine* (*Supra*), the arbitration proceedings which commenced pre-2015 Amendment are bound to receive a differential treatment in this regard. The above judgment also dilutes the directives, with respect to procedure of appointment of arbitrators especially in cases of various Government agencies/ PSUs, as laid in another recent judgment of the Hon'ble Supreme Court dated 03 July 2017 passed in *TRF Limited v. Energo Engineering Projects Limited*[5]. A party, left with no choice or freedom of selection of an independent and impartial arbitral tribunal under the 1996 Act, will be left at the mercy of such an arbitral tribunal without any effective recourse to seek a fair, unbiased and reasonable adjudication of its disputes.

The content of this document does not necessarily reflect the views / position of Khaitan & Co but remain solely those of the author(s).

End Notes

1- Civil Appeal Nos. 12627 - 12628 of 2017

2- (2009) 8 SCC 520

3- (2008) 10 SCC 240

4- (2017) 4 SCC 665

5- (2017) 8 SCC 377