JUDICIARY'S ROLE IN SETTLING CHALLENGES TO ARBITRAL AWARDS: A CASE FOR VIGILANCE

*Ms. Ragini Agarwal**

ABSTRACT

Arbitral awards have a tendency to be challenged frequently in Indian Courts on grounds of being erroneous. These can be 'errors in law' amounting to a conflict with public policy; 'errors in fact' amounting to patent illegality; or jurisdictional errors. While the grounds of challenge to awards under the Arbitration and Conciliation Act, 1996 have a limited scope of review, the interpretation of open-ended grounds such as public policy and patent illegality, has established a wide field within which arbitral awards can be challenged. This not only leads to a delay of decades in the awards achieving finality but also undermines party autonomy in choosing the arbitral process. The delay often sparks debates on whether the Indian jurisdiction is pro-arbitration or anti-arbitration. The author finely combs through declaring awards to be 'erroneous' and shows that the determination of 'error' in awards is an exercise in interpretation. Being such an exercise, the various interpretations arrived at can be used to expand or narrow down the scope of the Section. In such a case, the author contends that an attempt to avoid such binary debates of pro and anti-arbitration must be made and instead the role of the judiciary in the arbitral process as mere supervisors must be emphasized. Otherwise, the challenges to awards will continue to be Matryoshka Dolls, wherein every case will reveal a new interpretation on the basis of which challenges can be made, and the sanctity of awards will continue to be violated.

***Keywords**: Section 34, interest, error in awards, public policy, patent illegality, supervisory role of judges, vigilance.*

TABLE OF CONTENTS

* Ms. Ragini Agarwal is a graduate student from National Law University Jodhpur.

I. INTRODUCTION

There is an increasing tendency to view debates on setting aside awards under Section 34 of the Arbitration and Conciliation Act, 1996 ["**A&C Act**"] as binary,[1] with judgments being represented as either pro-arbitration or anti-arbitration. On one hand, upholding party autonomy dictates that if the parties have consciously consented to refer a dispute to arbitration, the finding of the arbitrator should not be interfered with.[2] Interference with the jurisdiction of the arbitrator is hastily termed as an anti-arbitration approach. On the other hand, the requirement of judicial supervision in arbitration is undeniable for ensuring that the arbitrator does not exceed their jurisdiction.[3]

Judicial supervision must, however, not interfere with the independence of the arbitrator and the autonomy of the parties. In India, when this act of judicial supervision became overbearing, bordering on hampering party autonomy, the Arbitration Act, 1940 gave way to the A&C Act and brought in a sea of reforms.[4] Under this new A&C Act, the power of the courts to interfere with arbitral proceedings was limited in extent.[5]An award, once given, had an extremely limited scope of challenge before the judiciary. Only if the award violated any of the grounds provided for under Section 34 of the Statute, was it allowed to be set aside.[6]

Section 34 provides that parties will have recourse against an arbitral award on the satisfaction of certain grounds, such as proof of some incapacity of the party, the award being in conflict with public policy, or the award being patently illegal. The compass of adjudication by courts in awards given by arbitrators is admittedly very narrow. However, even today, it cannot be said with certainty whether a particular case would fall foul of the grounds enumerated under Section 34, while applying the principles evolved by courts. The ambiguity surrounding the terms 'public policy' and 'patent illegality' gave rise to substantively wide grounds of challenge to the awards despite being phrased in a manner that provided for limited examination of awards. Given the complexities surrounding the interpretation of the two terms, there is a lack of uniformity in the standards for evaluating breach of public policy or patent illegality in an award.

The examination having become subjective, even today, after two and a half decades of the A&C Act holding field in India, it cannot be said with certainty when applying the legislative principles coupled with the principles evolved by courts, whether a particular case falls foul of the limited scope of grounds enumerated. As will be observed below, it seems that every case on Section 34 in India becomes analogous to a Matryoshka doll, with every decision revealing new rule on how the cases on setting aside of awards are dealt with. This is of concern since it suggests that the principle of consistency[7] in upholding awards is violated. Cases under this section, thus, need delicate balancing and firmer principles to determine a breach.

---

[1] 'Pro-Arbitration Trend Continues in India?' (2014) PSA E-Newsline <https://psalegal.com/wp-content/uploads/2017/01/ENewslineMarch2014.pdf> accessed 21 September 2020.
[2] *Numaligarh Refinery Ltd v Daelim Industrial Co Ltd* (2007) 8 SCC 466.
[3] Ibid.
[4] The Arbitration and Conciliation Bill 1995, Objects and Reasons ["**A&C Bill**"].
[5] Arbitration and Conciliation Act 1996, s 5 ["**A&C Act 1996**"].
[6] A&C Act 1996, s 34.
[7] *State of AP v AP Jaiswal* (2001) 1 SCC 748 ¶24.

In this article, the author shall assess exactly how limited is the ground of review of arbitral awards under Section 34. First, a brief background of the evolution of the grounds of public policy and patent illegality is given [**II.**]. Then, the author highlights the particulars of the award which are subject to challenge to showcase the lack of a principled decision-making when challenging the legitimacy of the award [**III.**]. Finally, the author argues for a judicial approach that eschews the binary debate and instead looks at challenges in the role of a supervisor [**IV.**].

II. EVOLUTION OF GROUNDS OF PUBLIC POLICY AND PATENT ILLEGALITY

Section 34 of the A&C Act evolved from Section 30 of the 1940 Act in an attempt to limit the scope of review to ensure that the sanctity of an arbitral proceeding is respected, and the cases are disposed of expeditiously.[8]The ethos of Section 34 requires that the courts act merely as courts of review rather than as courts of appeal, in examining challenges to the arbitral award.[9]Accordingly, sub-section (2)(a) of Section 34 provides certain circumstances, such as party being under incapacity, arbitration agreement being invalid, improper notice for the appointment of the arbitrator or composition of the tribunal not being in accordance with the agreement between the parties, for challenging an award. In contrast, Section 34(2)(b) and Section 34(2A) provide particularly open-ended terms on the basis of which an award can be set aside. These are namely, the award being in conflict with the public policy in India or being patently illegal. Courts cannot go beyond the grounds specified herein to evaluate the legality of the award or the merits of the claim.[10]

The complexities in defining the term 'public policy' are amplified by the fact that it is not defined in the A&C Act or any other Statute.[11]Its inclusion in even the United Nations Commission on International Trade Law ["**UNCITRAL**"] Model Law on International Commercial Arbitration ["**Model Law**"] was protested by U.K.[12] It has been called an 'unruly horse'; a description coined for the phrase 'public policy' in England as far back as in 1824.[13] The intention of inclusion of the term in the Model Law as well as the A&C Act was never meant to be a licence to overturn an arbitral award on merits.[14] Public policy was a ground to challenge both domestic awards and awards passed under international commercial arbitration.

In India, courts attempted to structurally define the term, however, the interpretation of the term saw a pendulum-like-swing between a narrow interpretation and a wider one. The Supreme Court, in *Renusagar Power Co. Ltd.* v *General Electric Co*.,[15]["***Renusagar***"]interpreted the term, 'public policy 'by stating that it would encompass any conflict with (i) the fundamental policy of Indian law, or (ii) the interests of India, or (iii) justice or morality. Later, the phrase 'public policy of India' was given an expansive

[8] A&C Bill (n 4).
[9] *Fiza Developers and Inter-Trade Private Limited v AMCI (India) Private Ltd* (2009) 17 SCC 796 ["**Fiza Developers**"]; *Emkay Global Financial Services Ltd v Girdhar Sondhi*(2018) 9 SCC 49 ["**Emkay Global**"].
[10] *Venture Global Engineering LLC v Tech Mahindra Ltd* (2018) 1 SCC 656.
[11] *Gherulal Parakh v Mahadeodas Maiya* AIR 1959 SC 781.
[12] UNCITRAL Model Law on International Commercial Arbitration, art 34(2)(b)(ii).
[13] *P Rathinam v Union of India* (1994) 3 SCC 394; *Richardson v Mellish* (1824)2 Bing (229) (Burrough J).
[14] Jean-Paul Beraudo, 'Egregious Error of Law as Grounds for Setting Aside an Arbitral Award' (2006)23(4) J of Intl Arbitration 351.
[15] *Renusagar Power Co Ltd v General Electric Co* AIR 1994 SC 860.

construction in *ONGC Ltd.* v *Saw Pipes [*"***Saw Pipes***"].[16]Therein, it was held that the award could be set aside under the public policy exception if it was patently illegal, i.e., possessed an illegality that went to the root of the matter. If the illegality was of trivial nature, it could not be held that award was against public policy.[17]This judgement opened the floodgates of judicial interference.

The expansionist and liberal approach of the courts in construing 'public policy' in the absence of a legislative definition created legal mischief as litigation increased, despite the fact that the very object of arbitration was to minimise judicial intervention. This disappointing turn of events was lamented by eminent lawyer Fali S. Nariman who remarked,

"*It was also contrary to the plain intent of the 1996 Act, namely the need of finality in alternative method of dispute resolution without court interference […] The Division Bench of two judges of the Court has altered the entire road map of arbitration law and put the clock back where we started under the old 1940 Act.*"[18]

The Law Commission in its Report No. 246, 'Amendments to the Arbitration and Conciliation Act, 1996' ["**246th Report**"], proposed a narrow standard, namely, that a mere violation of any law of India would not be a violation of public policy in cases of international commercial arbitrations held in India.[19] It suggested substantial amendments to Section 34 of the A&C Act with an endeavour to ensure that the *Renusagar* position applies to all foreign awards, and all awards passed in international commercial arbitrations. With respect to domestic arbitrations, the Commission recommended that the patent illegality test should be retained, although it was to be construed more narrowly than its construction in *Saw Pipes*.

Meanwhile, in *ONGC Ltd.* v *Western Geco International Ltd*.,[20] the Supreme Court interpreted the term 'public policy' widely to include reasonableness as a ground within the phrase 'fundamental policy of Indian law'.[21]This endangered the finality of arbitral awards by giving sanction to review the award on merits. Further, *Associate Builders* v *DDA*[22] explained the concept of perversity as a determination that the view of the arbitrator is completely implausible and not based on any evidence,[23] including evidence not led by the parties, or has been arrived at by ignoring vital evidence.[24]On the basis of the recommendations of the 246th Report (including the supplementary to the report),[25] the Arbitration and Conciliation (Amendment) Act, 2015 ["**Amendment Act, 2015**"] added Explanation I to Section

---

[16] *ONGC Ltd v Saw Pipes* (2003) 5 SCC 705 ¶31 ["**Saw Pipes**"].
[17] Ibid ¶30.
[18] Extract from the transcript of the speech delivered by Mr FS Nariman at the inaugural session of 'Legal Reforms in Infrastructure' New Delhi (2nd May 2003) quoted in S Kachwaha, 'The Indian Arbitration Law: Towards a New Jurisprudence' (2007) 10(1) International Arbitration Law Review [13]-[17].
[19] Law Commission of India, *'Amendments to the Arbitration and Conciliation Act 1996'* (246th Report, 2014) <http://lawcommissionofindia.nic.in/reports/Report246.pdf> last accessed September 21, 2020 ["**Report No, 246**"].
[20] *ONGC Ltd v Western Geco International Ltd* (2014) 9 SCC 263.
[21] See also, *Associated Provincial Picture Houses Ltd v Wednesbury Corpn* [1948] 1 KB 223.
[22] *Associate Builders v DDA* (2015) 3 SCC 49 ["**Associate Builders**"].
[23] *MMTC v Anglo American Metallurgical Coal Pty Ltd* MANU/DE/0664/2020 ["**MMTC**"].
[24] Ibid ¶¶31-32.
[25] Report No. 246 (n 19); Law Commission of India, *'Supplementary to Report No. 246 on Amendments to Arbitration and Conciliation Act, 1996'* (2015) <https://lawcommissionofindia.nic.in/reports/Supplementary_to_Report_No._246.pdf///9=8> last accessed September 21, 2020.

34(2)(b)(ii) and a new provision, Section 34(2A) which specified that 'patent illegality' would only be a recourse against domestic arbitral awards.[26]

Recently, in *Ssangyong Constructions* v *NHAI,*[27]the Supreme Court clarified that the Amendment Act, 2015 essentially relegated the understanding of 'fundamental policy of law' to the *Renusagar* era which meant that the principle of reasonableness as well as the ground of 'interest of India' for judicial intervention had been done away with. Thus, the power of the courts to review awards was substantially altered and narrowed down. This march of law shows how the Amendment Act, 2015 was intended to legislatively reinforce the narrow scope of challenge to awards. However, courts still struggle with the pendulum-like-swing between a narrow one and a wider one. While the current understanding has been relegated in principle to a narrow interpretation, as will be seen below, the application of these principles results in a wide scope of interference with the award.

III. CHALLENGING THE AWARD: OBSERVING THE HODGKINSON PRINCIPLE

While a substantive understanding of the power to review has been limited, in reality the practice of determining perversity is an interpretative exercise. A petition under this Section cannot be considered an appeal or a revision but rather a one issue summary procedure.[28]The Hodgkinson Principle states that an arbitrator is the sole and final judge of the quality and quantity of evidence before him.[29]Re-examining the facts to check if a different decision could be arrived at is also not permissible.[30] Only the record of the arbitrator must suffice to consider whether the grounds of Section 34 are made out.[31] In *Bharat Coking Coal Ltd* v *L.K Ahuja*,[32] the Supreme Court held that if the arbitrator has applied their mind on the pleadings and evidence adduced before them, courts cannot re-appraise the matter and state that their view is a more reasonable one. To respect the arbitrator's jurisdiction, the courts in their supervising capacity can only check that the reasoning given by the arbitrator is not outrageous and the view taken by the arbitrator is not implausible.[33]

Practically, however, the Indian courts have found it difficult to abide by the Hodgkinson principle. The courts cannot merely observe that the arbitrator has meticulously considered every piece of evidence and then arrived at the conclusion by the parties. The dilemma arises between giving a reasoned judgment that has discussed the case of the parties in-depth, and respecting the boundaries of narrow scope of examination. Whereas going through the arbitral record, reading the contract in the court and giving the parties the opportunity to address the inference drawn by the arbitral tribunal would make the procedure

[26] Arbitration and Conciliation (Amendment) Act 2015 ["**Amendment Act 2015**"].
[27] *Ssangyong Constructions* v *NHAI* (2019) AIR SC 5041 ["**Ssangyong**"].
[28] Fiza Developers (n 9); Emkay Global (n 9).
[29] *Hodgkinson v Fernie* (1857) 3 CBNS 189.
[30] *PR Shah Shares and Stock Brokers Private Limited v BHH Securities Private Ltd* (2012) 1 SCC 594.
[31] *Sandeep Kumar v Dr Ashok Hans* (2004) SCC OnLine Del 106.
[32] *Bharat Coking Coal Ltd v LK Ahuja* (2004) 5 SCC 109.
[33] *KV Mohd. Zakir v Regional Sports Centre* AIR 2009 SC (Supp) 2517.

akin to an appeal,[34] not considering every piece of evidence that was considered by the arbitrator in arriving at their decision would make the judgment unreasoned and faulty.[35]

Admittedly, the scope of review in challenge to awards is limited, however, the methodology adopted to assess the challenge has widened the scope of interference and converted the review of awards effectively, into an appeal. For instance, in *Pondicherry University* v *B.E. Billimoria& Co. Ltd.*, the Court found that the presumption of the tribunal on a particular issue was incorrect and proceeded to set aside the award on that basis. In view of the Hodgkinson Principle, Courts must avoid re-appreciation of evidence and must not supplant their views. They must be cognizant of their supervisory role in the adjudicatory mechanism.

The task of the courts becomes difficult in such challenges as not only is the procedural methodology to be adopted in assessing the challenge to awards of Section 34 unclear, the interpretation of the substantive grounds has kept zigzagging between a narrow scope and a wide one, since the past two and a half decades. Judges must carefully scrutinise the parties' arguments and the awards without allowing this to descend into a disguised appeal. This requires interpretation of the facts and evidence by courts and it seems that with each case, a new layer is peeled off, revealing a new aspect on which awards can be challenged. This is akin to the enigmatic Matryoshka Doll where one layer contains within it many layers and does not afford clarity in the first glance; on how many heads it contains.

Courts must be cognizant of their supervisory jurisdiction in the adjudicatory mechanism in arbitration. It is essential that judges exercise restraint in correcting what they perceive as errors in awards so as to follow a policy of minimal curial intervention. In this section, two aspects of determining errors shall be discussed in the consideration of which, the judges must endeavour to find the right balance. The first is determining errors of fact and law in awards [**A.**]; and the second is in the determination of arbitrator jurisdictional errors in the face of questions such as grant of compensation and interest [**B.**].

A. WHEN ASSESSING ERRORS OF FACT AND LAW

Errors of law cannot come within the ambit of challenge unless it goes against the public policy and breaches the fundamental policy of Indian law.[36] Only errors of fact are susceptible to challenge as being perverse under the grounds of patent illegality.[37] This is to prevent backdoor entry of a provision not intended by legislators.[38] Patent illegality in awards has a high threshold and trivial errors of fact do not make the awards patently illegal.[39] For establishing patent illegality, the awards must be shown to be perverse. Care must be taken to not interfere with the award merely on the basis of an *alternative* interpretation of the facts in a contract.

An 'alternative' interpretation of the facts in a contract cannot be qualified as an 'error' in fact to set aside the award.[40] The scale of reference thus ranges from an award being

[34] *State Trading Corporation v Toepfer International Asia* 2014(3) ArbLR 105 (Del); *National Highways Authority of India v Oriental Structural India Pvt Ltd* 2015(1) ArbLR 322 (Del).
[35] *Union of India v Alok Kansal*(2017) SCC OnLine Del 11473; *Kaur Bhatia v Aadya Trading & Investment Pvt Ltd*(2017) SCC OnLine Del 9176.
[36] *Ssangyong* (n 27).
[37] ibid
[38] ibid
[39] *Triveni Rubber & Plastics v CCE* AIR 1994 SC 1341 ["**Triveni Rubber**"].
[40] *Dyna Technologies Pvt Ltd v Crompton Greaves Ltd* 2019 SCCOnline SC 1656.

'reasonable' or 'possible' to being 'implausible'. Only if the assessment of the arbitrator is implausible will it be considered perverse and patently illegal. If multiple interpretations are possible, then irrespective of which one is more likely, the judgment of the arbitrator shall prevail. In *Dyna Technologies Pvt. Ltd.* v *Crompton Greaves Ltd.,*[41] the Supreme Court had stated,

> "*[A]wards should not be interfered with in a casual and cavalier manner unless the Court comes to a conclusion that the perversity of the award goes to the root of the matter without there being a possibility of alternative interpretation which may sustain the arbitral award*."[42]

This principle is not strictly followed in some cases which leads to inconsistencies in the standard for setting aside awards. Take, for instance, the *South East Asia Marine Engineering and Constructions Ltd.* v *Oil India Ltd.*[43]case, where the Supreme Court held that the arbitral tribunal had not evaluated the contract terms and conditions properly. It held that the interpretation of the 'change in law' clause of the contract by the arbitral tribunal was perverse since executive orders would not come within the ambit of 'law' contemplated in the clause. The wide interpretation by the arbitral tribunal was not accepted by the Supreme Court.[44] In failing to apply this standard, the Court ended up re-appreciating the evidence and re-interpreting the contract to eventually set the award aside. The award had been dated December 19, 2003, which meant that even after more than sixteen years of the award being granted, the successful party could not enjoy the fruits of its award because of an erroneous interpretation.

Another example is *MMTC Ltd.* v *Anglo-American Metallurgical Coal Pty. Ltd.*,[45]where the Delhi High Court held that the interpretation of the arbitrators was not supported by a 'plain, objective and clear-eyed reading' of the contract and hence, was liable to be set aside. Principles of perversity in awards have been set to be very high in judgments such as *Triveni Rubber & Plastics* v. *CCE*.[46]Perversity has been found in three scenarios: when the awardisbased on no evidence altogether, when it is based on imaginary evidence constructed from existing evidence, or when the arbitrator has ignored vital evidence.[47] This strict standard is often deviated from, as disagreements with the views of the arbitrator is cloaked in a language that make it seem like errors amounting to perversity and violating Section 34(2A) of the A&C Act.

The author opines that the gap between a view that is merely 'alternative' and a view that is 'impossible' is very thin. It depends on the psyche of the judges sitting in the bench making the determination subjective. Considering determination of patent illegality as an exercise in interpretation, the varied interpretations by the courts end up expanding and narrowing down the scope of perversity without laying down a strict standard which must be followed. Moreover, judges must attempt to keep in check their instincts about correcting the wrong position of law if it does not violate the public policy. The following example is a fine illustration of the boundaries which a court in its supervisory jurisdiction should observe.

---

[41] ibid.
[42] ibid ¶26.
[43] *Seamec v Oil* (2020) 5 SCC 164 ¶30.
[44] ibid ¶28.
[45] *MMTC* (n 23).
[46] *Triveni Rubber* (n 39).
[47] ibid

In *Ms. G* v *Isg Novasoft Technologies Ltd.*[48]before the Madras High Court, the arbitrator had observed that the employee cannot claim price payable on termination of contract beyond the price provided in the contract, even if the termination is illegal. Here, despite concluding that this was an erroneous legal position, the Madras High Court refused to interfere holding that interpretation of the contract and law was strictly within the arbitrator's domain.[49] However, in the same case, the Court was quick to intervene in a claim where such interpretation of the arbitrator amounted to condonation of the lapse on the part of the company to form a committee to address the allegations of sexual harassment.[50]This was because such a lapse in law amounted to conflict with public policy.

Thresholds to determine errors of fact and law are thus varied, and intervention must be done keeping these high thresholds in mind. While errors in law are interfered with only if they amount to a violation of public policy, errors of fact are interfered with only if they amount to perversity in the award.

B. WHEN ASSESSING WHETHER THE AWARD IS WITHIN THE TERMS OF THE CONTRACT

> "*The arbitrator derives the authority from the contract and if he acts in manifest disregard of contract, the award given by him would be an arbitrary one*."[51]

The observation that the arbitrator is a creature of the contract and must operate within the four corners of the contract has been reiterated in numerous cases, as well as in the Statute.[52]For instance, Section 28(3) of the A&C Act states that the arbitral tribunal while deciding and making any award must take into account the terms of the contract and trade usages applicable to the transaction. If the arbitrator goes beyond the contract, they commit an error of jurisdiction which would fall under the ground of patent illegality under Section 34(2A), when challenged.[53]Often, the disagreement with the arbitrator's opinion on say, whether the contract permitted award of costs is cloaked as a jurisdictional error on the arbitrator's part and set aside.[54]

In the following sub-parts, the author analyses peculiar terms that are frequently mentioned in cases to set aside arbitral awards. The author argues that these are cases in which the courts must exercise its supervisory jurisdiction with caution. The author begins by addressing the law concerning determination of damages and quantification of compensation [**a.**] and then addresses the grant of interest on the award as a part of the arbitrator's jurisdiction [**b.**]. With this analysis, the author seeks to show the ambiguity surrounding the interpretation of such clauses, and to establish the multiple inroads created by the courts for interference within the arbitrator's domain, which is unwarranted.

Determining damages and quantifying compensation:

The question of damages and compensation particularly vexes construction contracts where there may be delays. In works contracts containing arbitration clauses, for instance,

---

[48] *Ms G v ISG Novasoft Technologies Ltd* (2014) SCC OnLine Mad 6568 ¶86 ["**ISG Novasoft**"].
[49] ibid ¶86.
[50] ibid ¶133.
[51] *Steel Authority of India Ltd v JC Budhiraja* (1999) 8 SCC 122.
[52] *New India Civil Erectors (P) Ltd v Oil and Natural Gas Corporation* (1997) 11 SCC 75.
[53] *Ssangyong* (n 27) ¶29.
[54] *NHAI v HCC Ltd* (2016) SCC OnLine Delhi 6112 ¶75.

time is usually of essence.[55]*Chitty on Contracts* states that failure to perform a contract by the stipulated time would entitle the innocent party to (a) terminate the contract; and (b) claim damages.[56]Compensation for loss caused due to delay or breach of contract otherwise may be prescribed contractually or be governed by common law provisions on damages.

Moreover, the basic rule that 'if no loss is suffered, then damages cannot be payable 'must be followed in cases dealing with compensation in accordance with the Section 73 of the Indian Contract Act, 1872.[57] In *NTPC Ltd.* v. *Avantika Contractors*,[58] the tribunal had allowed the claim of 'loss of profit' without proof of loss, by taking profit as ten percent of the value of the balance work as a norm. This claim was set aside by the Delhi High Court on grounds of being against the settled law in India since damages required not only putting the innocent party in as good a situation as if the contract had been performed, but also conferred the duty to take all reasonable steps to mitigate losses.[59]

Where compensation is not contractually provided, the loss or damage for which compensation is claimed must arise in the usual course of things due to breach, and must not be given for any remote or indirect loss or damage sustained by the said breach.[60] Where a genuine reasonable pre-estimate of damages is already provided under a contract, the compensation may be paid accordingly as per Section 74 of the Indian Contract Act, 1872, unless the term contemplating damages is actually a penalty clause.[61] If the stipulation is in the nature of a penalty clause, the Court may award a sum that it considers reasonable but it must not exceed the amount specified in the contract.[62] Here too, the reasonability of the compensation is determined on the basis of principles in Section 73.

In the context of arbitration, two aspects become important. One is the aspect of determining whether or not damages are payable by taking into account any exclusionary clauses that might exist in the contract. The other is dealing with the quantification of such compensation.

Exclusionary clauses:

In *Ramnath International Construction (P) Ltd.* v. *Union of India*,[63] the Supreme Court stated that if there is a bar on escalation charges or compensation due to delay, such compensation cannot be awarded by travelling beyond the terms of the contract. On the other hand, in *K. N. Sathyapalan v. State of Kerala*,[64] it was stated that if the delay is attributable to the employer, it must entitle the contractor to damages irrespective of the exclusionary clause. Thus, while exclusionary clauses were given effect in one case, they were ignored in the other. The wording of such clauses must be clear in prohibiting escalation claims lest it not be given effect before the judicial authorities.[65]

---

[55] Indian Contract Act 1872, ss 55-56.
[56] HG Beale & J Chitty (eds), *Chitty on Contracts* (28thedn, Sweet & Maxwell 1999) ¶22-015.
[57] *Essar Procurement Service Ltd v Paramount Constructions* (2016) SCC Online Bom 9697; *Ajay Singh v Suneel Darshan* (2015) SCC Online Bom 1412*; Maharashtra State Electricity Board v Sterlite Industries (India) Ltd* (2000) SCC Online Bom 89.
[58] *NTPC Ltd v Avantika Contractors* (2020) SCC OnLine Del 1121.
[59] *Murlidhar Chiranji Lal v Harishchandra Dwarkadas & Anr* AIR 1962 SC 366 ¶9.
[60] *ISG Novasoft* (n 48) ¶75-79.
[61] *Saw Pipes* (n 16).
[62] *Kailash Nath Associates v DDA* (2015) 4 SCC 136 ¶43; *Fateh Chand v Balkishan Dass* AIR 1963 SC 1405.
[63] *Ramnath International Construction (P) Ltd v Union of India* (2007) 2 SCC 453.
[64] *K N Sathyapalan v. State of Kerala* (2007) 13 SCC 43.
[65] *Asian Techs Ltd v Union of India* (2009) 10 SCC 354.

The lack of clarity with respect to an arbitrator's jurisdiction to award damages in light of exclusionary clauses does not end here. For instance, in *Simplex Concrete Piles* v. *Union of India*,[66] the Delhi High Court stated that such exclusionary clauses which prohibit the entitlement to rightful damages of a person (under Sections 55 and 73 of the Contract Act, 1872) are void by virtue of Section 23 of the Contract Act, 1872. In *G.M. Northern Railway* v. *Sarvesh Chopra*,[67] on the other hand, it was stated that the non-defaulting party must expressly admit the loss due to delay or the intention to claim compensation, if it went ahead with the contract after delay.

Where there is no uniform principle followed by the courts themselves, it cannot be expected that the interpretation of contractual clauses by arbitrators would achieve finality.

Formulae for quantifying compensation:

Unless contractually specified, calculation of damages or compensation payable to the parties has been acknowledged to be within the arbitrator's domain.[68] To determine such compensation for heads such as loss of profits, certain formulae such as the Hudson's formula, Emden formula, and the Eichleay formula, which were referred to in *McDermott International Inc* v *Burn Standard Co Ltd &Ors*[69] as well, are used. These formulae do not have a common standard for cases of invocation, make certain assumptions and can be applied discretionarily.[70]

Even in this established domain of the arbitrator, there have been cases where courts deemed it fit to interfere with the compensation granted by the arbitrator in their jurisdiction and set aside the award. For instance, in the 2013 Bombay High Court case of *Edifice Developers and Project Engineers Ltd.* v *M/S. Essar Projects (India) Ltd*.,[71] the Division Bench upheld the decision to set aside the arbitral award on the ground that the arbitrator had made it on an erroneous premise. The premise was said to be faulty by the Court, since the arbitrator had failed to consider other formulae for evaluating overheads and applied a formula that was neither the prevalent trade practice nor accepted by the Supreme Court.

This interference in the domain of the arbitrator is, in the opinion of the author, unwarranted, and attacks the sanctity of the award since the courts fail to reserve their role as mere supervisors. The above Bombay High Court case is not an aberration. Recently, the Delhi High Court in *SMS Ltd.* v *Konkan Railway Corporation Ltd.*,[72] set aside an award where the tribunal had applied a formula hitherto unknown. Determining the method of quantifying claims is strictly within the arbitrator's jurisdiction.[73]Courts must be careful to not impose their views of what is the correct method of determining compensation, since this amounts to undue interference with the arbitrator's jurisdiction.

---

[66] *Simplex Concrete Piles v. Union of India* (2010) II Delhi 699.
[67] *GM Northern Railway v Sarvesh Chopra* (2002) 4 SCC 45.
[68] *McDermott International Inc v Burn Standard Co Ltd &Ors* (2006) 11 SCC 181 ¶104; *Associate Builders* (n 22) ¶48; *NHAI v M/S Ijm-Gayatri Joint Venture* MANU/DE/1925/2020 ["**Ijm-Gayatri**"].
[69] *McDermott International Inc v Burn Standard Co Ltd &Ors* (2006) 11 SCC 181.
[70] Julian Bailey, *Construction Law* (1st edn, Routledge Taylor & Francis Group 2011) 874.
[71] *Edifice Developers and Project Engineers Ltd. v M/S. Essar Projects (India) Ltd* (2013) SCC OnLine Bom 18.
[72] *SMS Ltd. v Konkan Railway Corporation Ltd.* MANU/DE/1029/2020.
[73] *Ijm-Gayatri* (n 68).

Determining the rate of interest payable on awards:

Normally, there are three periods for which interest may be awarded: (i) Pre-reference period, i.e. from the date of cause of action to the date of reference of the dispute for arbitration; (ii) *pendente lite* period, i.e. from the date of reference to the date of the award; and (iii) post-award period, i.e. from the date of award to the date of realisation. Arbitrators are permitted to grant interest for the pre-award stage (including pre-reference and *pendente lite* interest) as well as post-award stage in accordance with Section 31(7) of the A&C Act unless it is expressly barred by the parties.

Section 31(7)(b) mandates that the award will carry interest at the rate of eighteen percent per annum in the post-award stage unless the award otherwise directs. This provision cannot be deviated by the courts,[74]and the arbitrator's decision with respect to the rate of interest is final.[75]Vide the Amendment Act, 2015, the clause providing for interest at the rate of eighteen percent was amended to read that the sum of money awarded would carry (unless otherwise directed) interest at the rate of two percent higher than the rate of interest prevalent on the date of the award.[76]

It may be noted that when parties agree to a specified rate of interest in the contract, that rate of interest must be followed and should not be interfered with on the grounds of reasonableness. In *M/S Morgan Securities and Credits* v *Videocon Industries (Through RP)*,[77] interest at the rate of twenty-one percent per annum and thirty-six percent per annum were permitted to be charged for the pre-reference stage because the same was provided for in the contract. Where interest rate is not provided contractually, the discretion of the arbitrator becomes the determining factor.

Normally, the rate of interest granted must be compensatory and not punitive.[78]In *Vedanta Ltd.* v *Shenzhen Shandong Nuclear Power Construction Co. Ltd.*,[79] the Supreme Court laid down a host of factors which must be considered by the tribunals before awarding interest. It was given in the international context; however, these factors are relevant enough to be considered for domestic awards as well.[80] These factors are loss of use of sum, types of sums to which interest applies, time period, prevailing rates, simple or compound interest, commercial prudence from an economic standpoint, inflation rates, and proportionality.[81] It was also categorically stated that courts could reduce the rate of interest when it does not reflect economic conditions or where it was not found reasonable or promoting the interests of justice.[82]

In the case of *Krishna Bhagya Jala Nigam Ltd.* v *G. Harishchandra Reddy*,[83] rate of interest for *pendente lite* and future period was reduced to nine percent. In *V4 Infrastructure Private Limited* v *Jindal Biochem Private Limited*,[84]the Delhi High Court had the opinion that

---

[74] *M/s Sayeed Ahmed & Co. v State of Uttar Pradesh* JT (2009) 9 SC 429 ¶18.
[75] M*/s. Shahi and Associates v State of Uttar Pradesh* (2019) 8 SCC 329 ¶11.
[76] Amendment Act, 2015 (n 27).
[77] MANU/DE/0642/2020; See also, *PEL Industries Ltd v SE Investment Limited* (2018) SCC Online Del 8746.
[78] *Vedanta Limited v Union of India and Ors* (2018) SCC OnLine Del 11253.
[79] *Vedanta Ltd v Shenzhen Shandong Nuclear Power Construction Co. Ltd.* (2018) SCC Online SC 1922.
[80] *SAIL v Primetals Technologies Limited* MANU/DE/0808/2020.
[81] Ibid ¶6.
[82] Ibid
[83] *Krishna Bhagya Jala Nigam Ltd v G. Harishchandra Reddy* (2007) 2 SCC 720.
[84] *V4 Infrastructure Private Limited v Jindal Biochem Private Limited* MANU/DE/1011/2020.

interest at the rate of eighteen percent per annum was exorbitant considering the facts of the case and went on to reduce it to nine percent per annum. The vital factor of the foundation of arbitration claims changing from recovery of property to getting the amount of money back had been ignored by the tribunal. In *Turner Morrison Ltd.* v *Rani Parvati Devi*,[85] instead of providing the contractual rate of interest on the amount to be recovered, the arbitrator granted interest based on the rates under Usurious Loans Act, 1918.

The Delhi High Court set aside such grant of interest declaring it to be outside the bounds of the contract. Thus, it is seen that although the grant of interest and the rate thereof come within the domain of the arbitrator, courts often deem it reasonable to interfere upon satisfaction of the ground of patent illegality. On the rate of interest, courts have virtually emerged as the courts of appeal modifying the interest as per their ideas of right and wrong. This has the potential to be a typical case of courts exceeding jurisdiction.

In this section, an analysis of the decisions of courts setting aside awards on grounds of errors in interpretation of facts or law, as well as on the basis of errors in exercising jurisdiction by arbitrators has been done. The decisions lead the author to conclude that despite a limited power of review under Section 34 of the A&C Act, the courts have been successful in establishing a wide range of tests on the touchstone of which, the validity of awards may be determined.

IV. CONCLUSION: CALL FOR A BALANCED AND VIGILANT APPROACH

The conflict which becomes apparent is a narrow scope of examination with the wider scope of substantive tests adopted. This can be differentiated from successful arbitration jurisdictions such as Singapore, where courts have repeatedly affirmed the policy of minimal interference in curing defects of arbitral awards in deference to allowing the principle of finality of awards to stand.[86]To affirm its commitment to finality of awards in India, the courts must observe the policy of minimal curial intervention and avoid the power of review under Section 34 being converted into an appeal. The provision for recourse against arbitral awards walks a very fine and delicate balance between the sacrosanct nature of judicial review and finality of awards. Differences in approach for cases involving similar fact scenarios and almost identical clauses have been noted in this paper and the resulting ambiguity in the position of law has been highlighted.

Assessing errors of law and fact, determining whether a factual conclusion is an impossible conclusion or merely alternative, assessing whether interest or damages are barred in a contractual provision or not requires interpretation by the Courts. However, courts must only see whether the evidence in question has been *considered* by the tribunal or not. Assessing the weightage given by the arbitral tribunal to that particular fact would result in re-appreciation of evidence and the courts sitting in appeal over the award. This is beyond the jurisdictional scope of Section 34 of the A&C Act. The jurisdiction of the arbitrator must be clearly recognised from an assessment of the contract and an attempt at non-interference with the domain of the arbitrator must be made.

Role of the judges must not be seen in a binary of either being indifferent towards the proceedings or too interfering. The middle ground to take would be for the Courts to take on a role as a guardian, with some questions such as those pertaining to determination of

[85] *Turner Morrison Ltd v Rani Parvati Devi* MANU/DE/1053/2020.
[86] *AJU v AJT* (2011) SGCA 41 (Sing.); *AQU v AQV* (2015) SGHC 26 (Sing).

compensation, damages and interest best left to be determined by the arbitrator. As long as the arbitrator considers the questions fairly, the conclusion derived should not be interfered with. Thus, a shift towards procedural fairness is demanded. For certain other questions, however, where the fundamental policy of Indian law is being questioned, the judges must set the course right. Judges must be able to avoid considering whether a particular decision would be pro-arbitration or anti-arbitration and rather assess each case independently. They must be sympathetic and vigilant in guiding the parties to a solution without interfering with their autonomy.