CHANGING JUDICIAL TRENDS *QUA* ARBITRAL AWARDS

By:

P.C. Markanda, Senior Advocate
Naresh Markanda and Rajesh Markanda, Advocates
111, Sector 16-A, Chandigarh - 160015

INTRODUCTION

The basic idea behind taking recourse to alternate dispute resolution mechanism was to seek a quick remedy from an informal forum of one's choice – whether an arbitrator or mediator or conciliator rather than from the Courts. With this aim in view, the parties started providing for an arbitration clause in the contract. Power to appoint an arbitrator was often given to the employer and it was expected that he would show no favour to his department and appoint an independent and impartial person to act as the arbitrator in the matter of disputes between the contracting parties.

Till late seventies of the last century, all the awards (barring exceptions) were non-speaking awards. No duty was cast on the arbitrator to pass a speaking award. At least in engineering contracts, it was more or less a practice to pass a non-speaking award. Even the losing party did not grudge the verdict of the arbitrator. Such was the faith of the parties in the arbitrator.

Times changed and so did the thinking process of the parties. The awards were doubted by one or both the parties. Reason: lack of faith in

the arbitrators, for good or bad reasons. Challenge to awards became a rule rather than an exception. More and more cases started coming to the Courts. The Supreme Court, thus, was compelled to make the following observations in M/s Guru Nanak Foundation vs Rattan Singh & Sons, AIR 1981 SC 2075:

> "Interminable, time consuming, complex and expensive court procedures impelled jurists to search for an alternative forum, less formal, more effective and speedy for resolution of disputes avoiding procedural claptrap and this led them to Arbitration Act, 1940 (Act, for Short). However, the way in which the arbitration proceedings under the Act are conducted and without an exception challenged in courts has made lawyers laugh and legal philosophers weep. Experience shows and law reports bear ample testimony that the proceedings under the Act have become highly technical accompanied by unending prolixity at every stage providing a legal trap to the unwary. Informal forum chosen by the parties for expeditious disposal of their disputes has by the decisions of the Courts been clothed with 'legalese' of unforeseeable complexity."

In yet another case, reported as Ramji Dayawala & Sons (P) Ltd. vs Invest Import, AIR 1981 SC 2085, the Apex Court observed thus:

> "Protracted, time consuming, exasperating and atrociously expensive courts trials impelled an alternative mode of resolution of disputes between the parties: arbitrate, don't litigate. Arbitration being a mode of resolution of disputes by a Judge of the choice of the parties was considered preferable to adjudication of disputes by Courts. If expeditious, less expensive resolution of disputes by a Judge of the choice of the parties was the consummation devoutly to be wished through arbitration, experience shows and this

> case illustrates that the hope is wholly belied because in the words of Edmond Davis J., in Price vs Milner, (1966)1 WLR 1235, these may be disastrous proceedings."

It will be useful to refer to the observations of Edmond Davis J., in Price vs. Milner, which are as follows:

> "Many years ago, a top-hatted old gentleman used to parade outside these law Courts carrying a placard which bore the stirring injunction 'Arbitrate – don't litigate'. I wonder whether the ardour of that old gentleman would not have been dampened somewhat had he survived long enough to learn something about the present case."

ADJUDICATION PROCESS MUST BE QUICK

Under the Arbitration Act, 1940, it had been stipulated that the arbitrator would have to make the award within a period of four months from the date of entering upon the reference and in case it was not possible on his part to do so, then he could, with the consent of the parties, extend the time for making and publishing the award by four months at a time. In the event of one or both the parties not agreeing to extend the time, the extension could be granted by the Court. True that the period of four months was quite inadequate but nevertheless it showed that the intent of the Legislature that the disputes should be resolved in a short time. But the Arbitration and Conciliation Act, 1996, which came into being on 25th January 1996, does not provide any time limit within which the arbitrator must publish the award. However, this does not mean that the arbitrator may prolong the proceedings and delay adjudication of the disputes. If

the arbitrator unduly delays the proceedings then under section 14(1)(a) of the Act his authority to act as arbitrator shall be terminated since he would be deemed "unable to perform his functions or for other reasons fails to act without undue delay."

PATENT IRREGULARITIES WARRANT INTERFERENCE IN AWARDS

In the early 20th Century, it was only non-application or misapplication of law, which could form the basis for setting aside of arbitral awards. Way back in 1923, the Privy Counsel held that "An error of law on the face of the award means that you can find in the award or a document actually incorporated thereto, as for instance a note appended to by the arbitrator, stating the reasons for his judgment or some legal provisions which is the basis of the award and which you can then say is erroneous." [Champsey Bhara & Co. vs Jivraj Balloo and Weaving Co. Ltd., AIR 1923 PC 66]. This judgment was followed in letter and spirit by all the High Courts as well as the Supreme Court for well over 6 – 7 decades. Judicial decisions over the decades have indicated that an error of law or fact committed by an arbitrator itself does not constitute misconduct warranting interference in the award.

Section 30 of the Arbitration Act, 1940 provided for setting aside of award *inter alia* on the basis of misconduct. The Courts started setting aside some of the awards on the ground of misconduct, but still maintained that the award of the arbitrator demands respect. It was commonly known that an award was a decision of the arbitrator, whether a lawyer or a layman, chosen by the parties and entrusted with power to decide a dispute

submitted to him, and was not ordinarily not liable to be challenged on the ground that it was erroneous. It is also well-settled that the civil courts are entrusted with the power to facilitate arbitration and to effectuate the awards and not to exercise appellate powers over the decisions of the arbitrators; the decisions are binding, whether these have been reached rightly or wrongly, after giving adequate opportunity to the parties to put forth their respective cases.

AWARDS BY EXPERTS DESERVE EXTRA CONSIDERATION

Despite the well-established principles of law for giving due respect to the award of the arbitrator, still the Courts, here and there, set aside part or whole of the award on the ground of 'misconduct'. But some consideration was shown to the awards made by the experts. In Mediterranean & Eastern Export Co. Ltd. vs Fortress Fabrics Ltd., (1948-2 All ER 186), Goddard, C.J., observed:

> "The modern tendency is in my opinion more especially in commercial arbitrations, to endeavor to uphold awards of the skilled persons that the parties have themselves selected to decide the questions at issue between them, if the arbitrator has acted within the terms of his submission and has not violated any rules the courts should be slow indeed to set aside the award."

A number of judgments of various High Courts are a clear pointer to the fact that the awards of technically qualified people were not interfered with simply because they were presumed to know the technicalities involved in the controversy between the parties. The Courts generally

refrain from interfering with the awards made by technically qualified persons and desist from substituting their own decisions for those of the arbitrators even if the Courts were to come to a different conclusion, until and unless the award of the arbitrator was manifestly perverse or had been arrived at on the basis of wrong application of law.

The Judges were conscious of the fact that the day had long gone by when the Courts looked with jealousy on the jurisdiction of the arbitrators. The modern tendency, more especially in commercial transactions, is to uphold the awards of the skilled persons that the parties have themselves selected to decide the controversy between them. It was also understood that such awards which had been made by technical experts and moreso when appointed by the employers, should not be lightly interfered with.

Even though the verdict of various Courts that the award made by the Judge who had been selected by the parties should be upheld and not interfered with, but still, day in and day out, cases were reported where, for one reason or the other, the award was wholly or in part set aside. At times, the award was set aside on the ground of ‘error apparent on the face of the award’ or ‘misconduct’ or when it hurt the conscience of the Court.

GROUNDS FOR SETTING ASIDE AWARD UNDER THE 1996 ACT

The Legislature, in its wisdom, while enacting Arbitration and Conciliation Act, 1996, made a provision for setting aside of awards on very limited grounds. Repeatedly, the Supreme Court has mandated that the award

could be set aside only if the grounds set out in Section 34 were attarcted. Briefly, the grounds for setting aside award are:

- Incapacitation of a party;
- Arbitration agreement is invalid; or
- Lack of notice of appointment of arbitrator/arbitration proceedings or the party was unable to present the case; or
- Excess of jurisdiction on the part of the arbitrator; or
- Arbitration tribunal not properly constituted; or
- Subject-matter of dispute not capable of settlement by arbitration; or
- Award was in conflict with the public policy of India

The Legislature broadly defined public policy to mean 'The making of the award was induced or affected by fraud or corruption.' It would, therefore, leave no manner of doubt that such awards which had been made on the basis of fraud or corruption could be set aside. The Legislature had thus, confined setting aside of awards on the basis of fraud or corruption under the category of public policy of India.

BROADENING DEFINITION OF "PUBLIC POLICY OF INDIA"

The concept of "public policy of India" was considerably broadened by the Supreme Court in Oil & Natural Gas Corporation Ltd. vs SAW Pipes Ltd., (2003)5 SCC 705. It was held that the phrase "public policy of India" was required to be given a wider meaning and an award which is patently illegal deserved to be set aside if it is contrary to: -

(a) fundamental policy of Indian Law; or
(b) the interest of India; or
(c) justice or morality; or
(d) in addition, if it is patently illegal.

It was also laid down in the aforesaid judgment that “an award could also be set aside if it is so unfair and unreasonable that it shocks the conscience of the Court”. This expression, respectfully stating, is quite subjective. An award may shock the conscience of one court, but it may not shock the conscience of another court. There can be no water-tight or compartmentalized definition of “shocking the conscience of the court”. This could lead to increased interference in awards by the courts, which was not the avowed object of the Act of 1996.

The old practice of honouring the award must be revived. The very spirit of resorting to arbitration is to have quick, efficacious and inexpensive decision on controversies between the parties. There can be no doubt that an arbitrator cannot do what he thinks is right; he must follow the substantive law of India, as laid down in Section 28 of the Act. Any award which is against the express terms of the agreement between the parties or which is against the substantive law of India cannot be upheld.

LOSSES SUFFERED BY A PARTY NEED NOT BE PROVED

In a very recent decision, the Supreme Court in McDermott International Inc. vs Burn Standard Ltd., 2006(2) RAJ 661, has recognized the

supremacy of the arbitrator. Whereas, in earlier cases, the claimant was required to prove losses, particularly in case of prolongation of contracts, now the position is totally reversed. It was held in the aforesaid case that the arbitrators can base their awards for compensation for prolongation of the contract period even on theoretical formulas, evolved over a period of time and universally recognized. The *Emden* formula was held to be most realistic in so far as computation of compensation was concerned. Other formulas were also held to be reasonable. The *Eichleay formula* was evolved in America and derived its name from a case heard by Armed Services Board of Contract Appeals. This formula is used where it is not possible to prove loss of opportunity and the claim is based on actual cost. Even the *Hudson formula* got recognition in the said decision. However, it was noted that though the *Hudson formula* received judicial support in many cases, it has been criticized principally because it adopts head office overhead percentage from the contract as the factor for calculating the costs and this may bear little or no relation to actual head office costs of contractor. In fact, it had been observed that parties would file evidence in the form of vouchers to prove their losses. Most of the vouchers were challenged by the opposite party as being false and fabricated. It thus, fell to the lot of the arbitrator to determine the authenticity of the same, which also consumed ample time, thereby delaying the adjudication process. This time wastage would, hopefully, be eradicated with the latest judgment.

Many awards in the past had been set aside by the Courts on the ground that the proof in support of damages was not sufficient or was inadequate. With the above judgment, at least uncertainty about

insufficient or inadequate proof of loss has been removed. Hopefully, this trend will continue.