



Supreme Court invalidates arbitration clauses providing for appointment of sole arbitrator by person having an interest in the dispute¹

Brief Facts

Perkins Eastman Architects (“**Applicant**”) and HSCC (India) Ltd. (“**Respondent**”) entered into a contract, which provided for arbitration by a sole arbitrator. The arbitration clause stipulated that the sole arbitrator would be appointed by the Chairman and Managing Director (CMD) of the Respondent and that no person other than a person appointed by such CMD should act as arbitrator. When disputes arose between the parties, the Respondent terminated the contract. The Applicant invoked the arbitration clause, pursuant to which the Respondent’s Chief General Manager (and not the CMD) appointed the sole arbitrator. Challenging this appointment and the arbitration clause, the Applicant filed an application under Section 11(6) read with Section 11(12)(a) (“**Application**”) of the Arbitration and Conciliation Act, 1996 (“**Act**”) before the Supreme Court (“**Court**”).

Issues

Issue (i): Whether the arbitration is an international commercial arbitration under Section 2(1)(f) of the Act?

Issue (ii): Whether a case has been made out for the Court to appoint an arbitrator under Section 11(6) of the Act?

Issue (iii): If a case has been made out, whether the Court can exercise its power of appointment when an arbitrator has already been appointed or should the aggrieved party be left to challenge the appointment at an appropriate stage in terms of remedies available in law?

Judgment

Issue (i): The Court held that the present arbitration was an international commercial arbitration under Section 2(1)(f) of the Act, thereby

entitling the Court to deal with the Application. Relying on *Larsen and Toubro Limited Scomi Engineering BHD v. Mumbai Metropolitan Regional Development Authority*,² the Court found that the Applicant was the lead member of the consortium whose registered office was in New York. Therefore, the requirements of Section 2(1)(f) were satisfied.

Issue (ii): The Court found that a case has been made out for it to exercise its power of appointment under Section 11(6) of the Act. The Court delineated two categories of arbitration clauses providing for the appointment of sole arbitrators: (1) where an individual has two capacities, first as an arbitrator and second as an appointing authority; and (2) where an individual only has the latter capacity. The Court noted that the arbitration clause in the present case belonged to the second category. Applying its ruling in *TRF Limited v. Energo Engineering Projects Limited*,³ where the arbitration clause fell in the first category, the Court concluded that if the basis to render an individual ineligible to act as or nominate a sole arbitrator is the individual’s interest in the outcome of the dispute, then this basis will always be present irrespective of whether the clause falls in the first or second category.

The Court also distinguished arbitration clauses envisaging a sole arbitrator *vis-à-vis* a three-member tribunal. This is because in the latter, any advantage a party may derive by nominating an arbitrator of its choice would get counter-balanced by the equal power held by the other party. However, where only one party has the right to act as or appoint a sole arbitrator, its choice will always have an element of exclusivity in determining the course for the dispute resolution.

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Issue (iii): The Court held that once a case to exercise its power of appointment under Section 11 of the Act has been made out, it can proceed to appoint an arbitrator, even if one has already been appointed. Accordingly, the Court annulled the appointment of the arbitrator by the Respondent and appointed A.K. Sikri (Retd.), J., as the sole arbitrator.

Analysis

On a first impression, the Supreme Court's decision is a "logical deduction", as stated by the Court as well, of its ruling in *TRF (supra)* in that an individual who has an interest in the outcome of a dispute cannot nominate a sole arbitrator. However, the larger implications of this decision ought to be considered. It appears that the Court has effectively rendered invalid all arbitration clauses that envisage the unilateral appointment of a sole arbitrator by a party to the dispute. While the grounds of bias under Section 12 read with Schedule V of the Act apply to individuals who act as arbitrators, the Court has extended these to individuals who only have the power to nominate an arbitrator. In doing so, the Court has departed from a consistent line of judicial authority upholding arbitration clauses that provide for the unilateral appointment of a sole arbitrator. This could have implications for innumerable commercial contracts, such as government contracts and insurance contracts, which typically confer power on an employee to appoint an arbitrator.

Accordingly, it will be interesting and pertinent to follow the subsequent interpretation and application of this decision. Recently, the Court distinguished this decision in **Central Organisation for Railway Electrification v. M/S ECI-SPIC-SMO-MCML (JV)**.⁴ The Court noted its observation in *Perkins* about the legitimacy of the equal power of parties to nominate an arbitrator. Accordingly, the Court upheld an arbitration clause providing for a three-member tribunal, which empowered the appellant's General Manager to nominate an arbitrator, on the basis that this was counter-balanced by the Respondent's power to select any two out of the four nominees suggested by the General Manager and the requirement of the General Manager to appoint at least one of the two selected by the Respondent as the Respondent's nominee.

It would also be interesting to observe whether the Court's decision in *Perkins* has the, perhaps unintended, effect of providing an impetus to the institutional appointment of arbitrators as provided for by the Arbitration and Conciliation (Amendment) Act, 2019.

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1 Authored by Ila Kapoor, Partner and Juhi Gupta, Associate; *Perkins Eastman Architects DPC & Anr. v. HSCC (India) Ltd.*, Arbitration Application No. 32 of 2019, Supreme Court of India, 2019 SCC OnLine SC 1517, judgment dated 26 November 2019.

Quorum: Uday Umesh Lalit and Indu Malhotra, JJ.

2 (2019) 2 SCC 271.

3 (2017) 8 SCC 377.

4 Civil Appeal Nos. 9486-9487 of 2019.

PRACTICE AREA EXPERTS

Pallavi Shroff

Managing Partner and
National Practice Head Dispute Resolution
+91 98100 99911
E: pallavi.shroff@AMSShardul.com

Rishab Gupta

Partner
+91 98217 80313
E: rishab.gupta@AMSShardul.com

Binsy Susan

Partner
+91 96500 80397
E: binsy.susan@AMSShardul.com

Tejas Karia

Partner and Head, Arbitration Practice sub-group
+91 98107 98570
E: tejas.karia@AMSShardul.com

Siddhartha Datta

Partner
+91 90070 68488
E: siddhartha.datta@AMSShardul.com

Aashish Gupta

Partner
+91 98189 19857
E: aashish.gupta@AMSShardul.com

Anirudh Das

Partner
+91 98100 98329
E: anirudh.das@AMSShardul.com

Ila Kapoor

Partner
+91 98717 92737
E: ila.kapoor@AMSShardul.com

Smarika Singh

Partner
+91 97170 98075
E: smarika.singh@AMSShardul.com

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