Dispute Resolution Hotline

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RETURN OF THE JEDI: SUPREME COURT STRIKES DOWN SECTION 87 OF THE ARBITRATION ACT

- No automatic stay on enforcement of arbitral award due to pendency of a set aside application.
- Section 87 of the Arbitration & Conciliation Act, 1996 violates Article 14 of the Constitution of India.
- Section 26 of the 2015 Amendment Act restored along with the BCCI Judgment.

BACKGROUND

The Supreme Court ("**Court**") in the recent case of *Hindustan Construction Company Limited & anr. v. Union of India,*[1] struck down Section 87 of the Arbitration and Conciliation Act, 1996 ("**Arbitration Act**") as unconstitutional. This judgment marks yet another turning point in the arbitration law in India.

At the beginning, the Arbitration Act was found to be suffering from the disease of automatic stay of award if a challenge to such award was filed under Section 34. This effectively led to all awards being challenged before the court as it automatically stayed any payment thereunder and consequently deprived the award holder of due amount. The problem was cured by the **Arbitration and Conciliation (Amendment) Act, 2015** (**"2015 Amendment Act"**). The 2015 Amendment Act provided that there shall be no automatic stay of the award merely upon filing of a challenge under Section 34.

However, the 2015 Amendment Act created another problem. It was unclear in what circumstances the Arbitration Act as amended by 2015 Amendment Act would apply. Particularly it was unclear if the amended provisions applied to court proceedings that arose from arbitrations which had commenced prior to the commencement date of the 2015 Amendment Act i.e. October 23, 2015 ("**Commencement Date**"). Further, it was also uncertain if the automatic stay on enforcement of awards would continue where proceedings under Section 34 were pending at the Commencement Date.

Ultimately, the Court settled this controversy by its judgment in the case of **BCCI v. Kochi Cricket Private Limited**[2] . It held that Section 26[3] of the 2015 Amendment Act provides that unless the parties agreed otherwise, the amendments would be prospective i.e. it would apply to court proceedings which commenced on or after the Commencement Date irrespective of whether the connected arbitration had commenced prior to Commencement Date. Crucially, the court also held that there would be no automatic stay operating on the award even when the challenge application in court had been filed prior to the Commencement Date.

Interestingly, at the time arguments in the BCCI Case were ongoing, the government, approved the text of Arbitration & Conciliation (Amendment) Bill, 2018 ("**Bill**"). Clause 87 of the Bill provided that the 2015 Amendment Act shall apply only where the arbitration had commenced prior to the Commencement Date. With Clause 87 the automatic stay on enforcement of award upon a challenge being filed would apply for all awards arising out of an arbitration that commenced prior to October 23, 2015. Upon the Bill being brought to the notice of the Supreme Court, the Supreme Court in the BCCI Judgment advised the government to not enact Clause 87.

However, in 2019, the government enacted the said Clause 87 through the **Arbitration and Conciliation (Amendment) Act, 2019**. The 2019 Amendment Act further repealed Section 26 of the 2015 Amendment Act.

FACTS

The petitioners in the BCCI case challenged the constitutional validity of the newly inserted Section 87 of the Arbitration Act. The petitioners in the case were construction engineering companies. These companies were undertaking projects for government bodies and would typically have large claims on account of cost overruns, delays etc. They were facing a situation where large amounts of money were locked because of the automatic stay on awards which were passed in their favour. On the other hand, such companies were facing threat of insolvency proceedings for not having paid off the operational creditors.

With the BCCI Judgment, it was clear that there would not be an automatic stay on awards. However, due to the reversal of position by the 2019 Amendment Act, the petitioners challenged the constitutionality of Section 87.

JUDGMENT

Automatic Stay was never inherent in Section 36

The Court, at the outset, held that even prior to the 2015 Amendment Act the concept of automatic stay could not be inferred from Section 36 of the Arbitration Act. The Court referred to its judgment of *National Aluminium Company Ltd. v. Presstel & Fabrications (P) Ltd. & Anr,*[4] ("**NALCO Judgment**") and *Fiza Developers and Inter-trade Pvt. Ltd. v. AMCI (India) Pvt. Ltd.*[5] ("**Fiza Developers Judgment**") and held that both of them have incorrectly interpreted Section 36. In both NALCO Judgment and Fiza Developers Judgment, the Court had held that an award shall be enforced as

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if it was a decree of court, but only on the expiry of the time for making an application to set aside the award under Section 34, or when such application having been made, has been refused. The Court, in NALCO Judgment, also held that the language 36, leaves no discretion with courts to pass any interlocutory order in regard to the awards, once an application for set aside has been made.

However, the Court in the present case held that both the NALCO Judgment and Fiza Developers Judgment are incorrect as they fail to consider Section 9 and Section 35 of the Arbitration Act. It observed that Section 9 also gives the courts the liberty to pass any interlocutory even after passing of the award prior to its enforcement. It also held that Section 36 has to be read with Section 35, which provides that arbitral award shall be final and binding on parties and persons claiming under them. Reading Section 36 in a manner that leads to automatic stay on award upon an application under Section 34 being filed, would amount to reading something into Section 36, which is incorrect. Thus, there is no implied concept of automatic stay merely because an application under Section 34 (challenge to award) is filed. It further observed that 2015 Amendment Act is clarificatory in nature and merely states that the unamended Section 36 does not stand in the way of law to grant a stay of a money decree under the provisions of the Civil Procedure Code ("**CPC**").

Constitutional Challenge to the 2019 Amendment Act

The petitioners challenged the constitutional validity Section 87 in the Arbitration Act and removal of Section 26 from the 2015 Amendment Act as being violative of Article 14, 19(1)(g), 21 and 300-A of the Constitution of India.

The Court observed that the B N Srikrishna Committee in its Report dated July 30, 2017 ("**Srikrishna Report**") recommended the introduction of Section 87 because there were conflicting views from different High Courts as to the applicability of 2015 Amendment Act. However, the Court in its BCCI Judgment had pointed out the pitfalls if such a Section 87 would be inserted into the Arbitration Act. In fact, whatever uncertainty that Srikrishna Report sought to clear by recommending insertion of Section 87 was already cleared by BCCI Judgment. Therefore, as 2019 Amendment Act failed to consider the observations of the Court in the BCCI Judgment, it rendered insertion of Section 87 and deletion of Section 26 from 2015 Amendment Act manifestly arbitrary, having been enacted, without adequate determining principle, and contrary to public interest sought to be achieved by Arbitration Act and 2015 Amendment Act.

The court noted that in a civil suit, the judgment of a court is not automatically stayed upon filing of the appeal. On the contrary, even though the scope of a challenge against an award is significantly narrower than an appeal, filing of a challenge leads to an automatic stay. This the court noted is arbitrary and goes against the enactment of Section 87.

Lastly, the court also noted that the Sri Krishna Committee failed to take into account the Insolvency Code. The court noted that on one hand the award holders are unable to recover their dues due to the automatic stay and on the other hand they are faced with insolvency proceedings under the new code. This also the court noted is arbitrary.

Accordingly, the court struck down Section 87 of the Arbitration Act as violative of Article 14 of the Constitution of India.

ANALYSIS AND CONCLUSION

The 2019 Amendment Act has been subject of much **debate and criticism**. Insertion of Section 87, without even considering the judgment of the Hon'ble Supreme Court is one amongst the many issues that plague the 2019 Amendment Act. The BCCI Judgment had resolved certain issues around the applicability of 2015 Amendment Act. However, despite the judgment, the government choose to amend the law in a manner that the identified shortcoming in the law was given a new lease of life. Such amendment has now been found to arbitrary. It can now be hoped that the government does not take any further action on this. Such swings in the applicable law does not bode well for Indian arbitration. The focus should now be on removing other issues that have come in due to the 2019 Amendment Act. At some point, not just Section 87, but the entire the 2019 Amendment Act would have to be reconsidered.

Lastly, the BCCI Judgment says that the 2015 Amendment Act applies prospectively i.e. to those arbitration proceedings and court proceedings which have commenced on or after the Commencement Date. However, there are some concerns about how it would play out in practice in context of areas like enforceability of orders under Section 17, interplay between Section 9 and Section 17 particularly where the arbitration commenced prior to the Commencement Date, law applicable to an application under Section 8 and appeal thereof under Section 37 etc.

– Mohammad Kamran, Ashish Kabra & Vyapak Desai
You can direct your queries or comments to the authors

[1] Writ Petition (Civil) No. 1074 of 2019

[2] (2018) 6 SCC 287

[3] Section 26 - **Act not to apply to pending arbitral proceedings**: Nothing contained in this Act shall apply to the arbitral proceedings commenced, in accordance with the provisions of Section 21 of the principal Act, before the commencement of this Act unless the parties otherwise agree but this Act shall apply in relation to arbitral proceedings commenced on or after the date of commencement of this Act.

[4] (2004) 1 SCC 540

[5] (2009) 17 SCC 796

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