

Dispute Resolution Hotline

August 26, 2008

EXHAUST REMEDIES IN AGREEMENT BEFORE ASKING COURT TO APPOINT ARBITRATOR

In a judgment passed on August 18, 2008 by the Hon'ble Supreme Court of India ("**Supreme Court**") in Northern Railway Administration, Ministry of Railway, New Delhi Vs. Patel Engineering Company Ltd. ("**Northern Railway**"), it was held that courts must first ensure that the remedies provided for in the agreement between the parties must be exhausted before the court appoints an arbitrator. The Supreme Court noted that a bare reading of the scheme of Section 11¹ of the Arbitration and Conciliation Act, 1996 ("**the Act**") showed that the emphasis was on the terms of the agreement being adhered to and/or being given effect to as closely as possible. It was also held that it is not mandatory for the Chief Justice of the appropriate court or any person or institution designated by him to appoint a named person as an arbitrator upon an application made by any party but at the same time, while appointing an arbitrator, the courts shall have due regard to the twin requirements of Section 11(8) of the Act without which consideration, such appointment would be vulnerable.

BACKGROUND:

Northern Railway was referred to a larger bench of the Supreme Court as there appeared to be two conflicting views taken by two different benches of the Court being in Ace Pipeline Contracts (P) Ltd. Vs. Bharat Petroleum Corpn Ltd.² ("**Ace Pipeline**") and Union of India Vs. Bharat Battery Mfg. Co. (P) Ltd.³ ("**Bharat Battery**"). Interestingly, as is noted by the Court, the earlier decision of the Court in Ace Pipeline (dated April 04, 2007) was not brought to the notice of the bench in Bharat Battery (dated August 13, 2007), which perhaps led to the ensuing confusion and necessitated reference to a larger bench.

SUBMISSIONS:

Senior Counsel Harish Salve and Additional Solicitor General Mr. B. Dutta *inter alia* argued that Section 11(6) of the Act was infact an exception to the statutory procedure set out in Section 11(2) of the Act and where there was no agreed procedure between the parties, then in that event sub-sections (3), (4) and (5) of Section 11 of the Act would apply. Counsels pointed out that '*there was a statutory mandate to take necessary measures unless the agreement on appointment procedure provided other means for securing appointment*' and therefore submitted that it was '*necessary that the agreed procedure be exhausted before any alternative was resorted to*' and the '*agreement had to be given effect to*' and the '*contract had to be adhered to as closely as possible*'. They further pointed out that '*corrective measures have to be taken first and the Court is the last resort*'.

Thereafter, counsels also pointed out that the Court had to give due regard to any qualification required for the arbitrator under the agreement between the parties and other considerations required to secure the appointment of an independent and impartial arbitrator when appointing an arbitrator in terms of section 11(8) of the Act and finally submitted that the Court should not directly make an appointment as it first had to ensure that the provided remedy is exhausted and where not exhausted, the Court could ask (to do) what has not been done.

On the other hand senior counsel Mr. Ashok Desai appearing for certain parties seeking the appointment of an arbitrator *inter alia* argued that the expression 'due regard' related to some of the factors which have to be considered and it was not mandatory that the qualifications and the considerations referred to in Section 11(8) of the Act had to be applied as it was a question of degree of the parameters of consideration.

JUDGMENT:

After carefully assessing the various submissions of the parties, the Supreme Court stated that sub-sections (3) to (5) of Section 11 of the Act referred to cases where there was no agreed procedure whilst sub-section (2) provided that subject to sub-section (6), the parties were free to agree on a procedure for appointing the arbitrator(s). The Supreme Court also held that sub-section (6) of Section 11 of the Act set out the various contingencies when a party may request the Chief Justice or any person or institution designated by him to take necessary measures unless the agreement on the appointment procedure provides other means for securing the appointment.

ANALYSIS AND IMPLICATIONS:

- Courts to lay emphasis on the terms of the agreement being adhered to and given effect to as closely as possible and therefore, may ask parties to first do what has not been done.
- Courts to first ensure that the remedies provided for in the agreement between the parties are exhausted.
- Courts to ensure that the provisions of Section 11(8) of the Act are considered each time an arbitrator is required to be appointed. Thus, Courts will need to ensure that proper attention to the several circumstances has been focussed and all reasonable steps required are taken.
- Where such provisions of Section 11(8) of the Act are not kept in view, considered and taken into account, such appointment of arbitrator by the court becomes vulnerable.

The Supreme Court has by this judgment provided some much-needed guidance on Section 11(6) of the Act. This

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judgment will ensure that the courts are aware of the powers granted to them under the Act and that they stay within its bounds. This judgment will also ensure that the courts will only appoint an arbitrator when all remedies agreed to by the parties under the agreement are exhausted. Whilst this may not necessarily make the arbitral process more efficient, it will definitely aid in executing the process set out under the agreement.

- By **Dispute Resolution Team**

1 Section 11. Appointment of arbitrators

11. Appointment of arbitrators.—(1) A person of any nationality may be an arbitrator, unless otherwise agreed by the parties.

(2) Subject to sub-section (6), the parties are free to agree on a procedure for appointing the arbitrator or arbitrators.

(3) Failing any agreement referred to in sub-section (2), in an arbitration with three arbitrators, each party shall appoint one arbitrator, and the two appointed arbitrators shall appoint the third arbitrator who shall act as the presiding arbitrator.

(4) If the appointment procedure in sub-section (3) applies and—

1. a party fails to appoint an arbitrator within thirty days from the receipt of a request to do so from the other party; or
2. the two appointed arbitrators fail to agree on the third arbitrator within thirty days from the date of their appointment,

the appointment shall be made, upon request of a party, by the Chief Justice or any person or institution designated by him.

(5) Failing any agreement referred to in sub-section (2), in an arbitration with a sole arbitrator, if the parties fail to agree on the arbitrator within thirty days from receipt of a request by one party from the other party to so agree the appointment shall be made, upon request of a party, by the Chief Justice or any person or institution designated by him.

(6) Where, under an appointment procedure agreed upon by the parties,—

1. a party fails to act as required under that procedure; or
2. the parties, or the two appointed arbitrators, fail to reach an agreement expected of them under that procedure; or
3. a person, including an institution, fails to perform any function entrusted to him or it under that procedure,

a party may request the Chief Justice or any person or institution designated by him to take the necessary measure, unless the agreement on the appointment procedure provides other means for securing the appointment.

(7) A decision on a matter entrusted by sub-section (4) or sub-section (5) or sub-section (6) to the Chief Justice or the person or institution designated by him is final.

(8) The Chief Justice or the person or institution designated by him, in appointing an arbitrator, shall have due regard to—

1. any qualifications required of the arbitrator by the agreement of the parties; and
2. other considerations as are likely to secure the appointment of an independent and impartial arbitrator.

(9) In the case of appointment of sole or third arbitrator in an international commercial arbitration, the Chief Justice of India or the person or institution designated by him may appoint an arbitrator of a nationality other than the nationalities of the parties where the parties belong to different nationalities.

(10) The Chief Justice may make such scheme as he may deem appropriate for dealing with matters entrusted by sub-section (4) or sub-section (5) or sub-section (6) to him.

(11) Where more than one request has been made under sub-section (4) or sub-section (5) or sub-section (6) to the Chief Justices of different High Courts or their designates, the Chief Justice or his designate to whom the request has been first made under the relevant sub-section shall alone be competent to decide on the request.

(12) (a) Where the matters referred to in sub-sections (4), (5), (6), (7), (8) and (10) arise in an international commercial arbitration, the reference to "Chief Justice" in those sub-sections shall be construed as a reference to the "Chief Justice of India".

(b) Where the matters referred to in sub-sections (4), (5), (6), (7), (8) and (10) arise in any other arbitration, the reference to "Chief Justice" in those sub-sections shall be construed as a reference to the Chief Justice of the High Court within whose local limits the principal Civil Court referred to in clause (e) of sub-section (1) of Section 2 is situate and, where the High Court itself is the Court referred to in that clause, to the Chief Justice of that High Court.

2 (2007) 5 SCC 304

3 (2007) 7 SCC 684

Source: Judgment of the Supreme Court dated August 18, 2008, in the matter of Northern Railway Administration, Ministry of Railway, New Delhi Vs. Patel Engineering Company Ltd. being Civil Appeal No. 5067 of 2008 arising out of SLP (C) No.16196 of 2006

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