

Dispute Resolution Hotline

November 12, 2009

SUPREME COURT SAYS COURTS TO DECIDE FRAUD CASES-NOT ARBITRATORS

In *N. Radhkrishnan ("Appellant") v. M/s. Maestro Engineers & Ors. ("Respondents")*¹, the Supreme Court of India ("Court") has upheld the decision of lower courts and reiterated that notwithstanding the existence of an arbitration agreement, where a case *inter alia* relates to allegations of fraud and serious malpractices on the part of the respondents, such a case "must be tried in court and the Arbitrator could not be competent to deal with such matters which involved an elaborate production of evidence to establish the claims relating to fraud and criminal misappropriation".

FACTS:

The Appellant entered into a partnership with the Respondents on April 07, 2003 ("Partnership Deed"). Differences arose between the Appellant and the Respondents resulting in the exchange of several notices including one dated November 03, 2005 wherein, the Appellant offered to withdraw from the partnership subject to being paid his share of the salary and profits of the firm. In the said notices, the Appellant, *inter alia*, alleged that (1) the Respondents had colluded amongst themselves to siphon off the money of the partnership firm for their personal gain and (2) warned the Respondents of serious criminal action for the alleged commission of criminal offences.

While the appellant's case was that he made a conditional offer to withdraw from the partnership, the Respondents reconstituted the partnership firm and filed a suit² seeking a declaration that the Appellant was not a partner of the partnership firm on the ground that the appellant's offer for retirement was accepted by the Respondents. The Respondent also sought an injunction to prevent the Appellant from causing any disturbance to the peaceful running of the partnership firm.

The Appellant filed an application under Section 8³ of the Arbitration & Conciliation Act, 1996 ("the Act"), stating that the dispute fell within the purview of the arbitration clause of the Partnership Deed. The said application was rejected. The Appellant filed a civil revision before the Madras High Court⁴ which was also rejected. It was against this order of rejection that the Appellant approached the Court.

JUDGMENT:

The Court noted that it was apparent that there was a clear dispute regarding the reconstitution of the partnership firm and the subsequent deed framed to the effect. The dispute pertained to the continuation of the Appellant as a partner of the firm. Given that the Respondents had sought a declaration that the Appellant was no longer a partner in the firm after his retirement, the Court upheld the contention of the Appellant that the dispute squarely fell within the purview of the arbitration clause of the Partnership Deed and the subject matter of the suit was within the jurisdiction of the arbitrator.

Interestingly, the Court thereafter analyzed the issue of whether the arbitrator was competent to deal with the dispute raised by the parties and, whilst relying on various earlier judgments⁵, proceeded to uphold the judgment of the Madras High Court wherein it had been held that since the case related to allegations of fraud and serious malpractices on the part of the Respondents, it must be tried by a court and not an arbitrator since the case would require detailed evidence and such a situation could not be properly gone into by an arbitrator.

ANALYSIS:

The object of arbitration is to ensure the fast and efficient disposal of disputes between the parties to the arbitration agreement. For this reason, legislature in its wisdom incorporated Section 8 of the Act making it mandatory upon any judicial authority before whom an action was brought, which was the subject matter of an arbitration agreement, to refer the said matter to arbitration. Innumerable courts around the world, including courts in India, have held time and again that where the parties have entered into an arbitration agreement, the courts must give effect to such an intention of the parties.

By this judgment, the courts are now empowered to analyze the competence of the arbitrator to deal with the disputes before it. Moreover, it is not entirely inconceivable that some parties may make such allegations with an oblique motive being to prolong litigation and frustrate the legitimate claims of the other parties. In such a case an arbitration agreement is of no assistance. This can, in certain cases, lead to the entire concept of arbitration failing the need for which it was conceived.

- Sahil Kanuga & Shafaq Uraizee-Sapre

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- 1 Judgment dated October 22, 2009 passed in Civil Appeal No. 7019 of 2009 arising out of SLP ©No. 5994 of 2007.
- 2 Being O.S. No. 526 of 2006 before the Court of the District Munsif of Coimbatore.
- 3 8. Power to refer parties to arbitration where there is an arbitration agreement.— (1) A judicial authority before which an action is brought in a matter which is the subject of an arbitration agreement shall, if a party so applies not later than when submitting his first statement on the substance of the dispute, refer the parties to arbitration.
- (2) The application referred to in sub-section (1) shall not be entertained unless it is accompanied by the original arbitration agreement or a duly certified copy thereof.
- (3) Notwithstanding that an application has been made under sub-section (1) and that the issue is pending before the judicial authority, an arbitration may be commenced or continued and an arbitral award made.
- 4 CRP(PD) No. 1246 of 2006.
- 5 Abdul Kadir Shamsuddin Bubere v. Madhav Prabhakar Oak & Anr [AIR 1962 SC 406], Haryana Telecom Ltd. v. Sterlite Industries (India) Ltd. [AIR 1999 SC 2354], Oomor Sait HG v. Asiam Sait [2001 (3) CTC 269].

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