

Dispute Resolution Hotline

August 05, 2019

PARTY AUTONOMY WINS! ARBITRAL FEES CAN BE DETERMINED BY AGREEMENT OF PARTIES

- The Arbitration and Conciliation Act, 1996 ("**A&C Act**") and amendments thereto do not preclude a party from deciding a fee structure for arbitrators through mutual agreement.
- Deletion of the words "unless otherwise agreed" in Section 31A of the A&C Act implies that parties cannot contract out of costs; and not that they cannot agree on arbitral fees.

INTRODUCTION

The Arbitration and Conciliation Act, 1996 has witnessed several key amendments through the Arbitration and Conciliation (Amendment) Act, 2015 ("**Amendment Act**").

One such notable amendment under Section 31A provides for effective framework for allocation and ascertainment of costs of arbitration. "Costs" include arbitrator fees. While recommending this amendment along-with amendment to Section 11, the 246th Law Commission suggested a model schedule of fees which empowers the High Court to frame appropriate rules for fixation of fees for arbitrators and for which purpose it may take the said model schedule of fees into account.¹ Subsequently, the Amendment Act introduced the fourth schedule to the A&C Act, which provides model fees for arbitrators ("**Fourth Schedule**"). The Central Government has been given the power to amend the Fourth Schedule.²

Recently, in the case of *National Highways Authority of India v. Gayatri Jhansi Roadways Limited with Gammon Engineers and Contractors v. National Highways Authority of India*,³ the Supreme Court was faced with the issue of whether courts can enforce an agreement containing a fee schedule for arbitrators which is not as per the Fourth Schedule of the A&C Act. The Supreme Court, in a bench comprising of Justice R F Nariman and Justice Surya Kant, held that the Section 31(8) and Section 31A of the A&C Act do not preclude the parties from agreeing on a fee structure for the arbitrators.

FACTS

- Proceedings before the Arbitral Tribunal

The Gammon Engineers and Contractors Pvt. Ltd. ("**Appellant/Claimant**") and National Highways Authority of India ("**NHAI / Respondent**") entered into a contract on 7 February 2006 ("**Contract**"). The Contract contained an arbitration clause that fixed the fees payable to the arbitrators under a policy circular of the, the Respondent. This circular was subsequently replaced with another policy circular dated 1 June 2017 ("**NHAI Circular**").

Disputes arose between the parties. After an arbitral tribunal was constituted, it passed an order on 23 August 2017 stating that the Claimant had informed the tribunal that there is no agreement between the parties regarding the arbitrator fees; while the Respondent requested that the fees be fixed in terms of the NHAI Circular. The Tribunal considered the application and stated that the arbitrator fees shall be regulated as per provisions of the Fourth Schedule proposed by the Amendment Act.

The Respondent moved another application before the arbitral tribunal for review of the fees fixed by it. It reminded the Tribunal about the fees was fixed as per agreement and that the same ought not to be fixed as per the Fourth Schedule. However, the arbitral tribunal held that, "*in view of the latest provision in the amended Act, the AT is competent to fix the fees regardless of the agreement of the parties. This is as per judgment dated 11.09.2017 of the Hon'ble High Court in the matter of NHAI vs Gayatri Jhansi Roadways. Accordingly, fees shall be regulated as per provisions of the fourth schedule of the amended Arbitration and Conciliation Act, 1996.*" (emphasis supplied).

In *National Highways Authority of India v. Gayatri Jhansi Roadways Limited*⁴ ("**Gayatri Jhansi High Court Judgment**"), a Single Judge of the Delhi High Court had held on 11 September 2017 that arbitrator fees must be fixed in accordance with the Fourth Schedule of the A&C Act, irrespective of an agreement between the parties. The Single Judge had reasoned that prior to the Amendment Act, Section 31(8) of the A&C Act,⁵ *inter alia*, provided that "*Unless otherwise agreed by the parties; a. the costs of an arbitration shall be fixed by the arbitral tribunal*". (emphasis supplied)

However, amended Section 31(8) deleted the words "unless otherwise agreed by the parties" and replaced this provision to provide that "*the costs of an arbitration shall be fixed by the arbitral tribunal in accordance with section 31A*". Section 31A provides that the arbitral tribunal shall have discretion to determine costs, including fees and expenses of arbitrators. The Court referred then referred to the Fourth Schedule of the A&C Act and held that parties were bound by the model fee schedule irrespective of agreement, in light of deletion of the words "unless otherwise agreed by the parties" under Section 31(8).

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■ Proceedings before the Delhi High Court (“**Gammon Engineers High Court Judgment**”):

The Respondent then filed an application under Section 14 of the A&C Act⁶ before the Delhi High Court claiming that the mandate of the arbitral tribunal should be terminated as the arbitral tribunal willfully disregarded the agreement between the parties. The Respondent claimed that the tribunal is therefore ‘*de jure*’ unable to act any further in the proceedings. Meanwhile, the tribunal passed another order on 19 July 2019 stating that it had no objection to payment of any fees as determined by the Delhi High Court.

The Delhi High Court differed with the findings of the *Gayatri Jhansi High Court Judgment* and held that “*the deletion of words “unless otherwise agreed by the parties” in Section 31A only signifies that the parties, by an agreement, cannot contract out of payment of ‘costs’ and denude the Arbitral Tribunal to award ‘costs’ of arbitration in favour of the successful party.*” Thus, the Delhi High Court held that the Amendment Act does not take away the earlier position under the A&C Act, and parties are free to agree on the fees of arbitrators. The Delhi High Court further held that the finding in the *Gayatri Jhansi High Court Judgment* was *per incuriam*, i.e., rendered without sufficient adherence to law.

However, the Delhi High Court also held that the mandate of the tribunal shall stand terminated as the arbitral tribunal was bound to respect the arbitration agreement between the parties, which provides for a schedule of arbitrator fees.

Appeals against this order as well as the *Gayatri Jhansi High Court Judgment* were tagged and heard by the Supreme Court.

JUDGMENT OF THE SUPREME COURT

■ Applicability of Section 31A and the Fourth Schedule of the A&C Act

The Supreme Court noted that the fee schedule for the arbitrators was indeed agreed between the parties. It agreed with the conclusion in the *Gammon India High Court Judgment* and held that the change in language of section 31(8) read with Section 31A which deals only with the costs generally and not with arbitrator’s fees, is correct in law.

The Supreme Court acknowledged that arbitral fees are a component of the ‘costs’ under Section 31A of the A&C Act. However, the Supreme Court held that it is a ‘far cry’ to state that Section 31(8) and Section 31(A) of the A&C Act would directly govern contracts wherein a fee structure has already been laid down – and therefore imply the use of the Fourth Schedule instead of these agreements. Whilst upholding the conclusion of *Gammon India High Court Judgment on Section 31(8) and Section 31(A)*, the Supreme Court set aside the *Gayatri Jhansi High Court Judgment* in its entirety. However, the Supreme Court qualified that setting aside the *Gayatri Jhansi High Court Judgment* would not affect the arbitral award already rendered in that arbitration which has been upheld by the Supreme Court.

■ Interpretation of Section 14 of the A&C Act

In considering the *Gammon India High Court Judgment* on the issue of termination of arbitrator mandate under Section 14 of the A&C Act, the Supreme Court held that arbitrators did not become ‘*de jure*’ unable to perform their functions if they have acknowledged that party agreement existed on arbitral fees but considered themselves bound by the *Gayatri Jhansi High Court Judgment* (which was in force as of the time) which mandated that the Fourth Schedule, and not the agreement, would govern the arbitration fees. The Supreme Court held that since the arbitrators followed the law laid down by the Delhi High Court, their mandate should not have been terminated, thus overruling the *Gammon India High Court Judgment* on the issue of Section 14.

ANALYSIS

The Amendment Act introduced the ‘loser pays’ principle through Section 31A. While deleting the words “unless otherwise agreed” in Section 31(8), and allowing the arbitrator to exercise her/his discretion to determine costs of arbitration including allocation of arbitrator fees through the ‘loser pays’ principle, it is implied by this Section that parties cannot contract out of this principle. Through this decision, the Supreme Court has established that party agreement for determining arbitrator fees does not fall foul of Section 31(8) read with Section 31A, and that party agreement on arbitrator fees must be accorded primacy.

Further, this judgment also prevents termination of arbitrator mandate under Section 14 of the A&C Act where the order is based on law propounded by the court; valid at the time the order is made by the arbitrator. This will helpfully curtail applications made to terminate the mandate of an arbitrator where its order abides by the applicable case law at the time. Thus, it will be helpful for arbitrators to set out the law on which an order is made. This could save the mandate of the arbitrator, even if the case law undergoes change after the order is passed.

The Supreme Court’s judgment is significant as it provides much needed clarity on the applicability of the Fourth Schedule. Section 11(14) of the A&C Act states that the High Court may frame rules for the purpose of determination of fees of the arbitral tribunal after taking into account the rates specified in the Fourth Schedule. Considering this, the Bombay High Court has incorporated the Fourth Schedule into Bombay High Court (Fee Payable to Arbitrators) Rules, 2018. The Delhi International Arbitration Centre has recently adopted the Fourth Schedule guidance into the Delhi International Arbitration Centre (DIAC) (Administrative Cost and Arbitrators Fees) Rules, 2018. Noteworthy efforts taken by the Bombay and Delhi High Courts could also be adopted by other High Courts in considering the Fourth Schedule as a reference point to determine the fees payable to arbitrators.

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You can direct your queries or comments to the authors

¹ Page 11, Report No. 246, Amendments to the Arbitration and Conciliation Act 1996, Law Commission of India, August 2014.

² Section 11A, Arbitration and Conciliation Act, 1996 (“**A&C Act**”).

³ Civil Appeal No. 5383 OF 2019 with CIVIL APPEAL NO. 5384 OF 2019.

⁴ ARB.A. 1/2017, I.A. NOS.8086/2017 (STAY) & 9441/2017.

⁵ The un-amended Section 38 read as follows: “*Unless otherwise agreed by the parties,-*

a. the costs of an arbitration shall be fixed by the arbitral tribunal;

b. the arbitral tribunal shall specify-

i. the party entitled to costs,

ii. the party who shall pay the costs,

iii. the amount of costs or method of determining that amount, and
iv. the manner which the costs shall be paid⁶

⁶ Section 14(1)(a) of the A&C Act reads as follows: "14. Failure or impossibility to act.—(1) The mandate of an arbitrator shall terminate and he shall be substituted by another arbitrator, if — (a) he becomes de jure or de facto unable to perform his functions or for other reasons fails to act without undue delay"

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