

Dispute Resolution Hotline

March 31, 2010

PRINCIPLE OF SEVERABILITY MADE APPLICABLE TO ARBITRATION AWARD

In a landmark Judgment passed by the Bombay High Court in *RS Jiwani v. Ircon International Ltd* ("Ircon Case"), it was held that an arbitration award is severable and if a part of it is illegal and incapable of enforcement the other part that is valid and legal can still be enforced.

One of the key concerns of recent times has been the interference of the courts in the process of arbitration in India. The judgment passed in the Ircon Case has provided new hope to parties seeking enforcement of awards in India.

FACTS OF THE CASE

M/s Ircon International Limited ("Respondent") was awarded a contract by the Maharashtra State Road Development Corporation ("MSRDC") for constructing a rail over bridge. The Respondent floated a tender for sub-contracting a part of the project which was thereafter awarded to RS Jiwani ("Appellant") and the parties signed an agreement dated January 29, 1999 ("Agreement"). Although the Agreement stipulated that the work was to be completed by November 18, 1999, the Respondent alleged that there was considerable delay and thus disputes arose between the parties. The Appellant also raised claims on account of extra expenses incurred and unanticipated losses. The Appellant invoked arbitration in terms of clause 29 of the Agreement. Accordingly, an arbitrator was appointed and Appellant submitted his claim while the Respondent filed reply as well as raised its counter claims. The Appellant had filed 32 claims before the arbitrator out of which 15 claims with interest were allowed while the remaining claims were rejected. All the counter-claims raised by the Respondent were also rejected. Aggrieved from the award, the Respondent filed petition for setting aside the award dated May 5, 2005 in terms of section 34¹ and 16 (6)² of the Arbitration and Conciliation Act, 1996 (the "Act"). However, the Appellant did not challenge the award or any part thereof. The petition was admitted and the learned Single Judge recorded the findings that out of the 15 claims allowed by the learned Arbitrator, 11 claims were sustainable and the appellant was entitled to those claims but referring to the Division Bench judgment of the Bombay High Court in *Mrs. Pushpa P. Mulchandani v. Admiral Radhakrishin Tahiliani*, 2008 (7) LJ Soft, 161 the learned Single Judge set aside the entire award.

In *Mrs. Pushpa P. Mulchandani v. Admiral Radhakrishin Tahiliani* the Division Bench had held :

"Power to set aside only part of the award is conferred on court by section 34 of the Arbitration Act only in one contingency which is to be found in clause (iv) of sub-section (2) of section 42 of the Arbitration Act. In all other cases, if the Court finds that only a part of the award is affected by illegality which is pointed out to the court, the court cannot itself modify the award, but if a party to the petition applies to the court in exercise of its power under sub-section 4 of section 34, the court can direct the arbitral tribunal to resume the proceedings and take such action to eliminate the ground for setting aside the award. In such situation, the arbitral tribunal on resumption may be able to delete that part of the award which the Court finds to be invalid and illegal and make suitable modification in the award."

Aggrieved by the decision of the Single Judge, the Appellant appealed to the Larger Bench which accordingly framed the following questions for consideration:

1. Whether doctrine of severability can be applied to an award while dealing with a petition under section 34 of the Arbitration Act, 1996; and
2. What is the scope of proviso to Section 32 (2) (iv) and whether its application is restricted to clause (iv) alone or it applies to the whole of section 34 (2) of the Arbitration Act, 1996

DECISION OF THE LARGER BENCH

The Larger Bench rejected the interpretation put forth by the Respondent and observed that such interpretation would cause great hardship, inconvenience and even injustice to the parties. Accordingly the Larger Bench expressed the view that the dictum of law in the case of *Mrs. Pushpa P. Mulchandani v. Admiral Radhakrishin Tahiliani* is not the correct position of law. The Larger Bench predicated the contrary view which it felt was in comity with the legislative intent and object of the Arbitration Act, 1940. The Larger Bench held that the judicial discretion vested in the court in terms of section 34 of the Arbitration Act, 1996 takes within its ambit power to set aside an award partly or wholly depending on the facts and circumstances of the given case. The Legislature has vested wide discretion in the court to set aside an award wholly or partly, of course, within the strict limitations stated in the said provisions. The proviso to section 34 (2) (a) (iv) has to be read ejusdem generis to the main section, as in cases falling in that category, there would be an absolute duty on the court to invoke the principle of severability, where the matter submitted to arbitration can clearly be separated from matters not referred to arbitration and a decision has been given thereupon by the arbitral tribunal.

CONCLUSION

The judgment clearly sets out the correct position of law with regard to severability of an arbitration award. The

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decision will ensure that parties successful in arbitration are not caused unnecessary hardship when losing parties attempt to second guess arbitral awards in courts. While the decision is binding only on the Bombay High Court, it holds persuasive value and will come to the rescue of several such matters where due to a defect within a part of the arbitration award, the entire award was in the danger of being set aside. This decision will be helpful in saving considerable time both of the court and the parties, as the parties will not need to commence fresh arbitration or approach the courts for other reliefs.

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1 34. Application for setting aside arbitral award.- (1) Recourse to a Court against an arbitral award may be made only by an application for setting aside such award in accordance with sub-section (2) and sub-section (3).

(2) An arbitral award may be set aside by the Court only if---

(a) the party making the application furnishes proof that-----

(i) a party was under some incapacity, or

(ii) the arbitration agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law for the time being in force; or

(iii) the party making the application was not given proper notice of the appointment of an arbitrator or of the arbitral proceedings or was otherwise unable to present his case; or

(iv) the arbitral award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matter beyond the scope of the submission to arbitration:

Provided that, if the decisions on matters submitted to arbitration can be separated from those not submitted, only that part of the arbitral award which contains decisions on matters not submitted to arbitration may be set aside; or

(v) the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties, unless such agreement was in conflict with a provision of this Part from which the parties cannot derogate, or, failing such agreement, was not in accordance with this Part; or

(b) the Court finds that-----

(i) the subject-matter of the dispute is not capable of settlement by arbitration under the law for the time being in force, or

(ii) the arbitral award is in conflict with the public policy of India.

Explanation.---Without prejudice to the generality of sub-clause (ii), it is hereby declared, for the avoidance of any doubt, that an award is in conflict with the public policy of India if the making of the award was induced or affected by fraud or corruption or was in violation of section 75 or section 81.

(3) An application for setting aside may not be made after three months have elapsed from the date on which the party making that application had received the arbitral award, or, if a request had been made under section 33, from the date on which that request had been disposed of by the arbitral tribunal:

Provided that if the Court is satisfied that the applicant was prevented by sufficient cause from making the application within the said period of three months it may entertain the application within a further period of thirty days, but not thereafter.

(4) On receipt of an application under sub-section (1), the Court may, where it is appropriate and it is so requested by a party, adjourn the proceedings for a period of time determined by it in order to give the arbitral tribunal an opportunity to resume the arbitral proceedings or to take such other action as in the opinion of arbitral tribunal will eliminate the grounds for setting aside the arbitral award.

2 16. Competence of arbitral tribunal to rule on its jurisdiction.- (1) The arbitral tribunal may rule on its own jurisdiction, including ruling on any objections with respect to the existence or validity of the arbitration agreement, and for that purpose,-----

(a) an arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the contract; and

(b) a decision by the arbitral tribunal that the contract is null and void shall not entail ipso jure the invalidity of the arbitration clause.

(2) A plea that the arbitral tribunal does not have jurisdiction shall be raised not later than the submission of the statement of defence; however, a party shall not be precluded from raising such a plea merely because that he has appointed, or participated in the appointment of, an arbitrator.

(3) A plea that the arbitral tribunal is exceeding the scope of its authority shall be raised as soon as the matter alleged to be beyond the scope of its authority is raised during the arbitral proceedings.

(4) The arbitral tribunal may, in either of the cases referred to in sub-section (2) or sub-section (3), admit a later plea if it considers the delay justified.

(5) The arbitral tribunal shall decide on a plea referred to in sub-section (2) or sub-section (3) and, where the arbitral tribunal takes a decision rejecting the plea, continue with the arbitral proceedings and make an arbitral award.

(6) A party aggrieved by such an arbitral award may make an application for setting aside such an arbitral award in accordance with section 34.

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