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NEWSALERT

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Supreme court judgment: Arbitrator can award interest on interest

A three Judge Bench of the Supreme Court, in a recent judgment dated November 25, 2014, in the case of **Hyder Consulting (UK) Ltd., vs Governor, State of Orissa**, has held that it is within the powers of an arbitral tribunal to grant interest from the date of its award not only on the sum that is found principally due by a party but also on the interest that is payable on such principal sum from the date on which cause of action arose till the date on which the award is made, that is to say, that the arbitral tribunal can grant future interest, i.e. interest from the date of the award, even on the interest which has accrued during the pendency of the arbitration proceedings between the parties.

While holding so, the Supreme Court overruled its earlier judgment rendered in 2010 by a Division Bench in **State of Haryana & Ors. Vs S. L. Arora & Co., (2010) SCC 619**. In S. L. Arora case (Supra), the Supreme Court had held that the arbitrator could grant future interest, i.e. interest from the date of the award, only on the principal amount or the amount that may be found due and payable by a party in respect of the main claim against it but not on the interest on such claim that may have accrued during the pendency of the arbitration proceeding.

The three-Judge Bench while overruling the decision in S. L. Arora case (Supra) found that Section 31(7) of the Arbitration & Conciliation Act, 1996 (the “Act”) was quite clear in its wording. Section 31(7)(a) provided that arbitration tribunal could include in the sum for which the award is made, interest on the money found due from the date on which the cause of action arose till the date on which the award is made, unless there is an agreement between the parties to the contrary. Section 31(7)(b) provided that the sum directed to be paid by the arbitral award shall, unless the award otherwise directs, carry an interest @ 18% per annum from the date on which the award is made till the date of payment and/or realisation. The three-Judge Bench held that “the sum directed to be paid by the arbitral award” would therefore include not only money found due on the main claim but also the interest that is ordered to be paid on such money from the date on which the cause of action arose till the date on which the award is made. Interestingly, out of the three judges, the Chief Justice was in the minority and dissented. According to him the decision in S. L. Arora case (Supra) was correct and the intention of the Parliament was not to allow interest on interest to be made payable post the award. However, the majority held that the intention of the Parliament was clearly to discourage people from not complying with awards and thus, provided for interest to be made payable even on the interest post the award.

The Supreme Court has however clarified that the arbitrator has the *discretion* in awarding the future interest for the period post the date of the award in the event of non-payment and that only if the arbitrator does not specify anything about the future interest and has not rejected the claim for future interest, then only would interest @ 18% per annum be payable from the date of the award on the sum directed to be paid by the arbitral award which may include any interest that has accrued and been directed to be paid for the period during the pendency of the arbitration proceeding.

IndusLaw Quick View:

In the absence of any contract providing for interest on interest or compound interest to be charged or paid, it does seem harsh that the Act has been interpreted to allow the victor in arbitral proceedings to recover more than what he would have lost or suffered by non-payment of the award amount, by allowing compound interest to be recovered from the date of the award. But the majority of the judges felt that the wording of the Act did not give scope for any different interpretation. It must also be noted that the future rate of interest specified by the Section itself, i.e. 18% per annum, is quite high in comparison to the present interest rate scenario. However, just prior to this judgement, the Law Commission has recommended certain amendments to the Act - inter-alia to limit the future interest to 2% above the current rate of interest. It has also recommended an amendment to clarify that future interest can be awarded on both the principal claim awarded as well as the interest pendent lite if any merged therein, which is in tune with the present judgement.

The Supreme Court did note that there could be a case where the principal claim in the arbitration itself is only for interest. However, it did not consider one possible absurd situation resulting as a consequence of its interpretation. There could be a case where the main claim could be only of unpaid interest on some amount (which has already been paid), and when such a claim for interest is allowed, S. 31(7)(a) allows the arbitrator to award interest on this interest claim for the period when the arbitration proceedings would be pending and then there could be further interest awarded on the main interest claim + pendent lite interest from the date on which the award is made, which would be a situation of interest being payable on compounded interest! Such a scenario does not seem to have been considered by the Law Commission also. However, though the provisions have been interpreted to allow such awarding of interest, since there is discretion vested in the arbitrators, it is hoped that they will be reasonable in their approach when considering grant of both pendent lite interest as well as future interest. It would do a lot of good for the party, who fears that he may lose the arbitration proceedings, to ensure that the arbitrator issues a positive direction fixing a rate of future interest in the award, which would be reasonable and be confined to the principal claim, than leave it to the provisions to take effect. Nonetheless, this judgment and the recommended amendment should have the effect of making the parties, who lose in arbitral proceedings, seriously rethink challenging awards mechanically on frivolous grounds, given the risk of mounting interest becoming payable in the event of them losing in their challenge to the award.

* Authors- V. Srinivasa Raghavan, Partner & Avinaash Singh Gautama, Senior Associate

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