REPORTABLE

IN THE SUPREME COURT OF INDIA

CIVIL ORIGINAL JURISDICTION

ARBITRATION PETITION NO.11 OF 2011

Denel (Proprietary Limited) ...Petitioner

VERSUS

Govt. of India, Ministry of Defence ...

Respondent

O R D E R

SURINDER SINGH NIJJAR, J.

1. The petitioner has filed the present application under Sections 11(4) and (6) of the Arbitration and Conciliation Act, 1996 (hereinafter referred to as the 'Act') read with paragraph 2 of the appointment of the Arbitrators by the Chief Justice of India Scheme, 1996. It is stated that a contract was entered into between

the parties for the supply of Base Bleed Units. Initially the quantity to be supplied was 42,000 units. Later on, the quantity was increased to 52,000 units as per Clause 20 of the agreement. By 5th January, 2005, the petitioner had supplied substantial quantity of the goods. However, some of the goods supplied by the petitioner were rejected by the respondent. The petitioner, thereafter, informed the respondent that two more lots were ready for discharge on 17th March, 2005. However, Union of India never responded to the letter, hence, loss and damage has been caused to the petitioner. In April, 2005, after various discussions, the petitioner came to know that improper fuzes were used by the Union of India which led to the problem that occurred in the lots which were rejected. Thereafter, on 21st April, 2005, Union of India put on hold all contracts. Further, on 14th May, 2008, Union of India sent a notice seeking refund of amount of US $ 23,20,240, failing which legal action was to issue.

2. The disputes having arisen between the parties, efforts were made to resolve the same. The details of the efforts made are narrated in the petition. Since the disputes could not be resolved through mutual discussions, the DGOF appointed one Mr. A.K. Jain, Additional General Manager, Ordnance Factory, Ambajhari, Nagpur as an arbitrator in terms of Clause 19(F) of the contract, which reads as under:-

> "All the disputes and difference arising out of or in any way touching or concerning the agreement (matters for which the decision of a specific authority as specified in the contract shall be final under this agreement, shall not be subject to arbitration) shall be referred to the sole arbitration of the Director General, Ordnance Fys. Govt. of India for the time being or a Government servant appointed by him. The appointee shall not be a Govt. Servant who had dealt with the matters to which this agreement relates and that in the course of his duties as Govt. Servant has had not expressed views on all or any of the matter is in dispute or difference. In case the appointed Govt. Servant in place of the incumbents."

3. The petitioner objected to the appointment of the Arbitrator. The petitioner apprehended that the arbitrator would be favorably inclined towards the employer. Therefore, on 23rd January, 2009, the petitioner issued a notification under Section 14 of the

Arbitration Act stating that the mandate of the arbitrator had been terminated. Since inspite of the aforesaid notification, the arbitrator continued with the arbitration proceedings, the petitioner moved the Principal District Court, Chandrapur and filed Civil Misc. Application No. 45 of 2009 under Section 14(2) of the Act. On 21st December, 2010, the Principal District Court, Chandrapur terminated the mandate of the Sole Arbitrator with the observation that the arbitrator has been biased in favour of respondent No.1. A direction was also issued in the following terms:-

> "Director General, Ordnance Factory, Government of India, is appointed as an Arbitrator or he may appoint Government servant as an Arbitrator , as per Clause 19(F) of February 2004 contract and 19(E) of November 2004 contract, after following due procedure."

4. It is an admitted fact that pursuant to the aforesaid directions, within 30 days, DGOF did not himself commence the arbitration proceedings; nor did he appoint any Government servant as an arbitrator. The petitioner has, therefore, moved the present petition under Section 11(6) of the Act on 2nd of March, 2011 seeking appointment of an independent arbitrator. The petitioner claims

that the directions issued by the District Court are without any authority or jurisdiction and as such *void ab initio*. According to the petitioner, the direction of the learned District Judge is based upon an incorrect interpretation of Section 15 of the Act, whereby the learned Judge assumed the authority to appoint an arbitrator, which is beyond her jurisdiction. The Act does not make provision for the appointment of an arbitrator other than in accordance with the arbitration agreement and in the limited circumstances provided for in Section 11. The petitioner also claims that the DGOF would be disqualified to act as an arbitrator as the dispute is against the Government of India and particularly against the Ordnance Factory, Ministry of Defence. If the Director General, Ordnance Factory, Government of India (DGOF) or a Government servant is appointed as an arbitrator, he shall always be bound by the directions/instructions issued by his superior authorities and, therefore, such an arbitrator would not be in a position to independently decide the dispute between the parties. According to the petitioner, such an appointment would be contrary to the

provisions of Section 12 of the Act. The petitioner further claims that the DGOF has already through his actions in the dispute between the parties demonstrated his lack of independence and impartiality. The learned District Judge in her judgment alluded to the fact that the DGOF without receiving any request for referral of the dispute between the petitioner and the respondent colluded with the previous arbitrator to appoint him as an arbitrator without any notice to the petitioner. The petitioner further claims that the DGOF has been directly involved in the dispute as would be evident from the correspondence between the petitioner and the respondent. The petitioner thereafter makes a reference to the letter dated 30th June, 2008 wherein the DGOF took the view that the petitioner is liable to replace the rejected Base Bleed units, as alleged by the respondent, making specific reference to the correspondence in which respondent stated its claim against the petitioner and cancelled the contract with the petitioner. The petitioner further claims that the DGOF has failed to appoint the arbitrator either as directed by the learned District Judge or in

accordance with Section 15 of the Act within 30 days of the order dated 21st December, 2010. Therefore, the respondent has forfeited the right to make an appointment from the date of the filing of the petition.

5. The respondent has controverted the plea put forward by the petitioner by way of a detailed counter affidavit. It is claimed by the respondent that the petition under Section 11(6) of the Act is not maintainable, as Mr.Satyanarayana has been appointed as a substitute arbitrator on 16th March, 2011. The petitioner was duly notified about the appointment of the arbitrator in its letter dated 26th March, 2011. The petitioner was requested to forward its claim within 10 days. The petitioner was informed that if such a claim does not reach by 8th April, 2011, the arbitrator will presume that the petitioner did not have any further claim. Upon receipt of that letter, the petitioner objected to the appointment of a new arbitrator by its letter dated 15th April, 2011, as being contrary to clause 19(F). The petitioner has wrongly claimed that since the

appointment of the arbitrator was not made prior to the filing of the petition under Section 11(6), the respondent has forfeited the right to make the appointment.

6. I have heard the learned counsel for the parties.

7. On the basis of facts narrated above, Mr. Naphade submits that the petitioner has forfeited its right to appoint the arbitrator. In support of the submission, he relied on the judgments of this Court in the case of **Datar Switchgears Ltd.** Vs. **Tata Finance Ltd. & Anr.**[1], **Punj Lloyd Ltd.** Vs. **Petronet MHB Ltd.**[2] and **Yashwith Constructions (P) Ltd.** Vs. **Simplex Concrete Piles India Ltd. & Anr.**[3]

8. On the other hand, Mr. Raval, appearing for the Union of India has submitted that the petitioner has failed to make out a case for not appearing before the arbitrator appointed pursuant to the order

[1] 2000 (8) SCC 151
[2] 2006 (2) SCC 638
[3] 2006 (6) SCC 204

of the Principal District Court, Chandrapur on 21st December, 2010. He submits that the respondents have willingly accepted the appointment of the earlier arbitrator in accordance with the arbitration clause. Therefore, they can have no justification to challenge the appointment of the present arbitrator, who has only been appointed as the mandate of the earlier arbitrator had been terminated by the orders of the Court. The petitioner was duly informed about the appointment of the arbitrator on 16th March, 2011. The arbitrator had intimated both the parties about the appointment and had requested them to submit their respective claims within a period of 10 days. It was only at that stage that the petitioner wrote a letter dated 15th April, 2011 stating that the appointment of the arbitrator was in violation of arbitration clause. Mr. Raval further submitted that in the present circumstances, the matter is squarely covered against the petitioner by the judgment in the case of **Indian Oil Corporation Limited & Ors.** Vs. **Raja Transport Private Limited**[4]. On the basis of the aforesaid judgment, the learned counsel submitted that the present petition

[4] (2009) 8 SCC 520

under Section 11(6) is misconceived, as the Sole Arbitrator has been appointed in terms of the agreed procedure contained in Clause 19 (F) and (E).

9. I have considered the submissions made by the learned counsel. In my opinion, Mr. Naphade is correct in his submission that the matter is squarely covered by the judgment in **Datar Switchgears Ltd. (supra)**, wherein this Court has observed as follows:-

> "**19.** So far as cases falling under Section 11(6) are concerned — such as the one before us — no time limit has been prescribed under the Act, whereas a period of 30 days has been prescribed under Section 11(4) and Section 11(5) of the Act. In our view, therefore, *so far as Section 11(6) is concerned*, if one party demands the opposite party to appoint an arbitrator and the opposite party does not make an appointment within 30 days of the demand, the right to appointment does not get automatically forfeited after expiry of 30 days. If the opposite party makes an appointment even after 30 days of the demand, but *before the first party has moved the court under Section 11*, that would be sufficient. In other words, in cases arising under Section 11(6), if the opposite party has not made an appointment within 30 days of demand, the right to make appointment is not forfeited but continues, but an appointment has to be made before the former files application under Section 11

seeking appointment of an arbitrator. Only then the right of the opposite party ceases. We do not, therefore, agree with the observation in the above judgments that if the appointment is not made within 30 days of demand, the right to appoint an arbitrator under Section 11(6) is forfeited."

The aforesaid ratio has been reiterated in **Punj Lloyd Ltd. (supra).**

10. In the facts and circumstances of this case, it would not be possible to accept the submission of Mr. Raval that the present petition filed by the petitioner under Section 11(6) of the Act is not maintainable. On the admitted facts, it is evident that the mandate of the earlier arbitrator Mr. Arun Kumar Jain was terminated by the orders passed by the Principal District Court, Chandrapur in Civil Misc. Application No. 45 of 2009 by order dated 21st December, 2010. A perusal of the aforesaid order would show that the petitioner had challenged the validity of Clause 19(F). The aforesaid submission was rejected by the Court with the observation that the same cannot be the subject matter which could be resolved in a

petition under Section 14(2) of the Act. The petitioner was given an opportunity to challenge the clauses in an appropriate forum. The District Judge, however, accepted the submission of the petitioner that there are justifiable reasons to indicate that the arbitrator has not acted fairly. Hence the mandate of Mr. A.K. Jain as the Sole Arbitrator was terminated. In accordance with Section 15(2) of the Act, DGOF was appointed as an arbitrator. He was also given an option to appoint Government servant as an arbitrator as per the arbitration clause. It is a matter of record that DGOF did not act himself as an arbitrator, pursuant to the aforesaid order of the Principal District Judge, Chandrapur dated 21st December, 2010. Mr. Satyanarayana, the subsequent arbitrator, had not been appointed till 16th March, 2011. The present petition was moved on 2nd March, 2011. Therefore, the respondents had clearly forfeited their right to make the appointment of an arbitrator. Consequently, the appointment of Mr. Satyanarayana, as an arbitrator, by letter dated 16th March, 2011 cannot be sustained.

11. Mr. Naphade then submits that in the peculiar facts and circumstances of this case, the respondent cannot now be permitted to insist that the Court should appoint an arbitrator only in terms of the agreed procedure. In support of this submission, he emphasised that DGOF can not act as an arbitrator as the same will be against the principles of natural justice, as no one can be a judge in his own cause. He further submitted that even if any government employee is appointed as an arbitrator, he will not be in a position to act against the Union of India as he will be obliged to follow the instructions of the superiors. He placed reliance on **Bharat Sanchar Nigam Limited & Anr.** Vs. **Motorola India Private Limited**[5]**.** It is not possible to accept the submissions of Mr. Naphade. This Court in the case of **Indian Oil Corporation Limited (supra)** has considered such a submission and observed that :-

> "Arbitration is a binding voluntary alternative dispute resolution process by a private forum chosen by the parties. If a party, with open eyes and full knowledge and comprehension of the relevant provision enters into a contract with a Government/statutory

[5] 2009 (2) SCC 337

corporation/public sector undertaking containing an arbitration agreement providing that one of its Secretaries/Directors shall be the arbitrator, he cannot subsequently turn around and contend that he is agreeable for settlement of the disputes by arbitration, but not by the named arbitrator who is an employee of the other party.

It is now well settled by a series of decisions that arbitration agreements in government contracts providing that an employee of the Department (usually a high official unconnected with the work of the contract) will be the arbitrator, are neither void nor unenforceable. All the decisions proceed on the basis that when senior officers of Government/statutory corporations/public sector undertakings are appointed as arbitrators, they will function independently and impartially, even though they are employees of such institutions/organizations."

In my opinion, the aforesaid observations are a complete answer to the submission made by Mr. Naphade.

12. Learned senior counsel then submitted that even if the arbitration clause is held to be valid, Mr. Satyanarayana still can not be permitted to continue with arbitration as the petitioner has a strong apprehension that he is biased in favour of the respondents. In support of the submission, the learned senior counsel has relied on the various notices issued by the arbitrator which were

invariably received after the expiry of the time fixed by the arbitrator. In support of his submission, he relied on a judgment of this Court in the case of **Denel (Proprietary) Limited** Vs. **Bharat Electronics Limited & Anr.**[6].

13. Replying to the apprehension of bias pleaded by Mr. Naphade, it is submitted by Mr. Raval that non-receipt of the letters in time can not possibly give rise to an apprehension that Mr. Satyanarayana is in any manner biased against the petitioner. He submits that the reliance of the petitioner on the judgment in **Denel (Proprietary) Limited (supra)** is also misconceived as the aforesaid judgment was confined to the facts of that particular matter. He, therefore, submits that the Court ought to follow the agreed procedure and not to interfere with the appointment of Mr. Satyanarayana as the arbitrator. In the alternative, he submits that even if the appointment of Mr. Satyanarayana is held to be invalid, the matter has to be left to the DGOF to either act as an arbitrator himself or to appoint an officer appointed by him.

[6] 2010 (6) SCC 394

14. It is true that in normal circumstances while exercising jurisdiction under Section 11(6), the Court would adhere to the terms of the agreement as closely as possible. But if the circumstances warrant, the Chief Justice or the nominee of the Chief Justice is not debarred from appointing an independent arbitrator other then the named arbitrator.

15. A Three Judge Bench of this Court in the case of **Northern Railway Administration, Ministry of Railway, New Delhi** Vs. **Patel Engineering Company Limited**[7], considered the scope and ambit of Section 11(6) of the Act, as divergent views were taken in two decisions of this Court in **Ace Pipeline Contracts (P) Ltd.** Vs. **Bharat Petroleum Corpn. Ltd.**[8] and **Union of India** Vs. **Bharat Battery Manufacturing Co. (P) Ltd. (supra).** Upon consideration of the relevant provisions it was inter-alia observed as follows:-

> "A bare reading of the scheme of Section 11 shows that the emphasis is on the terms of the agreement being

[7] 2008 (10) SCC 240
[8] 2007 (5) SCC 304

adhered to and/or given effect as closely as possible. In other words, the Court may ask to do what has not been done. The Court must first ensure that the remedies provided for are exhausted. It is true as contended by Mr. Desai, that it is not mandatory for the Chief Justice or any person or institution designated by him to appoint the named arbitrator or arbitrators. But at the same time, due regard has to be given to the qualifications required by the agreement and other considerations."

16. Keeping in view the observations made above, I have examined the facts pleaded in this case. I am of the opinion that in the peculiar facts and circumstances of this case, it would be necessary and advisable to appoint an independent arbitrator. In this case, the contract is with Ministry of Defence. The arbitrator Mr. Satyanarayana has been nominated by DGOF, who is bound to accept the directions issued by the Union of India. Mr. Satyanarayana is an employee within the same organization. The attitude of the respondents towards the proceeding is not indicative of an impartial approach. In fact, the mandate of the earlier arbitrator was terminated on the material produced before the Court, which indicated that the arbitrator was biased in favour of the Union of India. In the present case also, Mr. Naphade has

made a reference to various notices issued by the arbitrator, none of which were received by the petitioner within time. Therefore, the petitioner was effectively denied the opportunity to present his case before the Sole Arbitrator. Therefore, the apprehensions of the petitioner can not be said to be without any basis.

17. It must also be remembered that even while exercising the jurisdiction under Section 11(6), the Court is required to have due regard to the provisions contained in Section 11(8) of the Act. The aforesaid section provides that apart from ensuring that the arbitrator possesses the necessary qualifications required of the arbitrator by the agreement of the parties, the Court shall have due regard to other considerations as are likely to ensure the appointment of an independent and impartial arbitrator. Keeping in view the aforesaid provision, this Court in the case of **Indian Oil Corporation Limited (supra)**, whilst emphasizing that normally the Court shall make the appointment in terms of the agreed procedure has observed that the Chief Justice or his designate may deviate

from the same after recording reasons for the same. In paragraph 45 of the aforesaid judgment, it is observed as follows:-

> "**45.** If the arbitration agreement provides for arbitration by a named arbitrator, the courts should normally give effect to the provisions of the arbitration agreement. But as clarified by Northern Railway Admn.10, where there is material to create a reasonable apprehension that the person mentioned in the arbitration agreement as the arbitrator is not likely to act independently or impartially, or if the named person is not available, then the Chief Justice or his designate may, after recording reasons for not following the agreed procedure of referring the dispute to the named arbitrator, appoint an independent arbitrator in accordance with Section 11(8) of the Act. In other words, referring the disputes to the named arbitrator shall be the rule. The Chief Justice or his designate will have to merely reiterate the arbitration agreement by referring the parties to the named arbitrator or named Arbitral Tribunal. Ignoring the named arbitrator/Arbitral Tribunal and nominating an independent arbitrator shall be the exception to the rule, to be resorted for valid reasons."
>
> (emphasis supplied)

18. The material placed before the Court by the petitioner would indicate that it would not be unreasonable to entertain the belief that the arbitrator appointed by the respondent would not be

independent. That being so, the appointment of Mr. Satyanarayana can not pass the test under Section 11(8) of the Act.

19. Similarly, applying the test laid down in **Indian Oil Corporation Ltd. (supra**), this Court in the case of **Denel (Proprietary) Limited (supra)** also observed that the Managing Director, Bharat Electronics Limited, which is a Government company is bound by the directions/instructions issued by his superior authority. The Court also observed that according to the pleaded case of the respondents, though it was liable to pay the amount due under the purchase order, it was not in a position to supply the dues only because of the direction issued by the Ministry of Defence, Government of India. Therefore, the Court concluded that the Managing Director may not be in a position to independently decide the dispute between the parties. Consequently, the Court proceeded to appoint an independent arbitrator.

20. In my opinion, the circumstances in the present case are similar and a similar course needs to be adopted. In view of the above, the petition is allowed.

21. In exercise of my powers under Section 11(4) and (6) of the Arbitration and Conciliation Act, 1996 read with Paragraph 2 of the Appointment of Arbitrator by the Chief Justice of India Scheme, 1996, I hereby appoint Hon. Mr. Justice Ashok C. Agarwal, Retd. Chief Justice of the Madras High Court, R/o No. 20, Usha Kiran, 2nd Pasta Lane, Colaba, Mumbai-400 005, as the Sole Arbitrator, to adjudicate the disputes that have arisen between the parties, on such terms and conditions as the learned Sole Arbitrator deems fit and proper. Undoubtedly, the learned Sole Arbitrator shall decide all the disputes arising between the parties without being influenced by any prima facie opinion expressed in this order, with regard to the respective claims of the parties.

22. The registry is directed to communicate this order to the Sole Arbitrator forthwith to enable him to enter upon the reference and decide the matter as expeditiously as possible.

.....J.
[Surinder Singh Nijjar]

New Delhi;
January 09, 2012.