

SUPREME COURT OF INDIA

Vedanta Ltd

Vs.

Shenzhen Shandong Nuclear Power Construction Co. Ltd.

C.A.No.10394 of 2018

(R.F.Narinam and Indu Malhotra,JJ.,)

11.10.2018

JUDGMENT

Indu Malhotra,J.,

SLP(Civil)No.25819 of 2018

1. Leave granted.

2. The present Special Leave Petition has been filed to challenge the judgment and order dated 30th August, 2018 passed by the Delhi High Court in an Appeal filed by under Section 37 of the Arbitration & Conciliation Act, 1996 [hereinafter referred to as “the said Act”].

2. The factual matrix of the present case, briefly stated, is as under:

2.1 On 22nd May 2008, the Appellant and the Respondent-Company entered into four interrelated contracts for the construction of a 210-MW Co-Generation Power Plant, viz.: -

i. Offshore Engineering and Technical Services Contract

ii. Offshore Supply Contract

iii. Onshore Services and Construction Contract

iv. Onshore Supply Contract These contracts are hereinafter collectively referred to as the ‘EPC Contracts’.

2.2 Each of the four contracts contained an Arbitration Clause which is identically worded, which reads as under:

“Article 10 ARBITRATION

10.1 The parties hereto shall endeavor to settle all disputes and difference relating to and/or arising out of the Contract amicably.

10.2 In the event of the parties failing to resolve any dispute amicably the same shall be referred to Arbitration in accordance with the Arbitration & Conciliation Act 1996 with all modifications and re-enactments thereto, as is prevalent in India. Each party shall be entitled to nominate an Arbitrator and the two Arbitrators so nominated shall jointly nominate a third presiding Arbitrator. The Arbitrators shall give a reasoned award.

10.3 The place of arbitration shall be Mumbai and the language of the arbitration shall be English.

10.4 The parties further agree that any arbitration award shall be final and binding upon the parties.

10.5 The parties hereto agree that the Supplier shall be obliged to carry out its obligations under the Contract even in the event a dispute is referred to Arbitration. It is clarified that the purchaser shall be entitled to retain any sum or portion of Contract Price which has become due and payable, for any unfinished works or any subject matter under arbitration. ”

2.3 The Governing law of the Contracts is the Law of India. The relevant Clause is set out herein below for ready reference:

“ Article 12

GOVERNING LAW AND JURISDICTION

12.1 This contract shall be construed in accordance with and governed by the laws of India and in the event of any litigation the courts in India shall be exclusive jurisdiction. ”

2.4 The EPC Contracts contained a termination clause which reads as under :

“35.2.1- The Purchaser may suspend the work in whole or in part at any time by giving Supplier notice in writing to such effect stating the nature, the date and the anticipated duration of such suspension. On receiving the notice of suspension, the Supplier shall stop all such work which the Purchaser has directed to be suspended with immediate effect.

The Supplier shall continue to perform other work in terms of the Contract which the Purchaser has not suspended. The Supplier shall resume the suspended work as expeditiously as possible after receipt of such withdrawal of suspension notice.

35.2.2-During suspension, the Supplier shall be entitled to receive from the Purchaser a Variation Order covering reasonable costs if any due to suspension and appropriate adjustment for Completion Schedule, and other terms and conditions of this Contract.

35.2.3-If such suspension continues for more than 180 (one hundred and eighty) days, at the end of the period, the Supplier shall be by a further 30 (thirty) days prior notice, entitled to terminate the Contract and Purchaser shall pay to the Supplier 105% (one hundred and five percent) of the cost incurred by the Supplier till the date of termination

a. s compensation after adjusting payments already made till the termination. No consequential damages shall be payable by the Purchaser to the Supplier in the event of such suspension. ”

(Emphasis supplied)

2.5 The EPC Contracts are entered into between the Petitioner herein an Indian Company, and a company incorporated in the People's Republic of China. The arbitration between these parties is an international commercial arbitration, having its seat in India, which would be governed by Part I of the 1996 Act. The termination clause provided that in the event of termination, the Purchaser shall pay 105% of the cost incurred by the Supplier as compensation. The EPC contracts did not contain any provision on payment of Interest.

2.6 Disputes arose between the parties, which resulted in the termination of the EPC Contracts by the Respondent vide notice dated 25.02.2011. The Respondent called upon the Petitioner herein to pay the outstanding dues as mentioned in the said notice.

2.7 The Respondent-Claimants invoked the Arbitration Clause vide Notice dated 18.04.2012. The disputes emanating out of the EPC contracts were referred to arbitration by a three-member tribunal in terms of the agreement between the parties. At the first sitting of the arbitral tribunal on 17.10.2012, the parties mutually agreed to a change of the seat/place of arbitration from Mumbai to New Delhi.

2.8 The Claimant-Respondent herein raised various Claims in multiple currencies amounting to Rs. 4,472,106,315; US \$ 2,380,000; and EUR 121,723,214 along with pendent lite and future Interest @ 18% p.a.

2.9 The present Appellant filed a Counter Claim amounting to Rs. 2458,34,89,367 along with Interest @18% p.a. for determination before the arbitral tribunal.

2.10 The arbitral tribunal passed a detailed Award dated 09.11.2017, wherein the Tribunal awarded the following amounts:

“ 134. Thus, in light of the aforesaid, the following amounts are awarded in favour of the Claimant and the Respondent is liable to pay the same to the Claimant within a period of 120 days from the date of this award:

I. Under the First Claim:

a) Rs. 46,71,41,942/- and Euro 23,717,437; and

b) Rs. 12,19,69,047

II. Under the Second claim:

a) Rs. 25,47,325/-; and

b) Rs. 6,06,707/-c) Rs. 1,31,10,990/-

135. The aforesaid amount shall be payable along with interest at the rate of 9% from the date of institution of the present arbitration proceedings provided the amount is paid/deposited within 120 days of the award.

136. In case the respondent fails to pay the aforesaid amounts within 120 days from the date of the Award, the claimant shall be entitled to further interest at the rate of 15% till the date of realization of the amount.

137. Considering the overall facts and circumstances of the case and the expenditure incurred in the arbitration proceedings, we consider it appropriate to award Rs. 50,0,000.00/- (Rupees Fifty Lakh) towards costs and legal expenses to the claimant, which according to us would meet the ends of justice. The claim of payment of cost of the Respondent is rejected.”

The arbitral tribunal in the Award granted a part of the First Claim in INR, while the other component was awarded in EUR. The claim made in US \$ was rejected. The arbitral tribunal adopted a dual rate of Interest. If the amounts awarded were paid within 120 days’ from the passing of the Award, the awarded sum would carry a 9% rate of Interest on both the components of the Award i.e. the amounts payable in INR and EUR. However, if the awarded amounts were not paid within 120 days’, the arbitral tribunal imposed a higher rate of further Interest @ 15% till the date of realization of the amount. The arbitral tribunal also awarded Rs. 50,0,000 (Fifty Lakhs Rupees) towards Costs and Legal Expenses to the Claimant/Respondent herein. The arbitral tribunal rejected the Counter-Claims filed by the Appellant/Award-Debtor.

2.11 Aggrieved by the said Award, the present Appellant filed Objections under Section 34 before the Delhi High Court which came to be rejected vide Order dt. 12.02.2018.

2.12 Aggrieved by the judgment of the Single Judge, the Appellant award-debtor filed an Appeal before a Division Bench of the Delhi High Court under Section 37 of the said Act. The Division Bench dismissed the Appeal vide Order dt. 30.08.2018.

2.13 Aggrieved by the judgment of the Division Bench, the Appellant has preferred the present Special Leave Petition. At the time of arguments, the Appellant restricted the challenge to the rate of Interest awarded by the arbitral tribunal. The challenge on the Interest awarded by the Tribunal is being considered in the peculiar facts and circumstances of the present case, and the specific clauses of the Contracts in question.

3. 'Interest' is defined as "the return or compensation for the use or retention by one person for a sum of money belonging to or owned by any reason to another". In essence, an award of Interest compensates a party for its forgone return on investment, or for money withheld without a justifiable cause. The current practice of awarding Interest in international commercial arbitrations is riddled with inconsistencies, and is criticized for lack of uniformity. In international contracts, there is no consensus on the method or rate of awarding Interest.

4. In an international commercial arbitration, in the absence of an agreement between the parties on Interest, the rate of Interest awarded would be governed by the law of the Seat of arbitration. The rate of interest awarded must correspond to the currency in which the award is given, and must be in conformity with the laws in force in the *lex fori*.

5. In the present case, the international commercial arbitration having its seat in India, the rate of interest to be awarded must be in accordance with the Arbitration and Conciliation Act, 1996. Section 31(7) of the 1996 Act which provides for Interest, is set out herein below for ready reference:

"31. Form and content of arbitral award—
(7)...

(a) Unless otherwise agreed by the parties, where and in so far as an arbitral award is for the payment of money, the arbitral tribunal may include in the sum for which the award is made interest, at such rate as it deems reasonable, on the whole or any part of the money, for the whole or any part of the period between the date on which the cause of action arose and the date on which the award is made.

[(b) A sum directed to be paid by an arbitral award shall, unless the award otherwise directs, carry interest at the rate of two per cent, higher than the current rate of interest prevalent on the date of award, from the date of award to the date of payment.

Explanation - The expression "current rate of interest" shall have the same meaning as assigned to it under clause (b) of section 2 of the Interest Act, 1978 (14 of 1978).]

(Emphasis supplied)

Section 31(7) is in two parts: sub-section (a) pertains to the award of Interest for the pre-reference and pendente lite period, which is subject to the agreement between the parties. This would be evident from the opening words of Section 31(7)(a) - ‘ unless otherwise agreed by the parties’. Absent an agreement between the parties, the arbitral tribunal has the discretion to award interest; as it deems reasonable.

Interest may be awarded either on the whole, or any part of the sum awarded. section 31(7)(b) pertains to the post-award period i.e. from the date of the award to the date of realization, and is not subject to party autonomy or an agreement between the parties. This would be apparent from the manner in which clause (b) of s. 31(7) is framed. The phrase “unless otherwise agreed by the parties” is absent from this provision. The statutory rate of Interest is 2% higher than the current rate of Interest prevalent on the date of the award.

6. The discretion of the arbitrator to award interest must be exercised reasonably. An arbitral tribunal while making an award for Interest must take into consideration a host of factors, such as: (i) the ‘loss of use’ of the principal sum; (ii) the types of sums to which the Interest must apply; (iii) the time period over which interest should be awarded; (iv) the internationally prevailing rates of interest; (v) whether simple or compound rate of interest is to be applied (vi) whether the rate of interest awarded is commercially prudent from an economic stand-point;

(vii) the rates of inflation, (viii) proportionality of the count awarded as Interest to the principal sums awarded. On the one hand, the rate of Interest must be compensatory as it is a form of reparation granted to the award-holder; while on the other it must not be punitive, unconscionable or usurious in nature. Courts may reduce the Interest rate awarded by an arbitral tribunal where such Interest rate does not reflect the prevailing economic conditions or where it is nor found reasonable , or promotes the interests of justice .

7. During the course of hearing, a suggestion was made to apply Interest in accordance with LIBOR plus a margin (between 1 to 3%). LIBOR is an average interest rate calculated from time to time, based on inputs given by major banks in London as to their interest rates. Under the LIBOR regime, banks give details vis-a-vis actual interest rate that they are paying, or would be required to pay for borrowing from other banks. LIBOR is a 3-month rate which has been adopted in some cases of a breach of contract (or other obligation) .

8. In the present case, the arbitral tribunal has adopted a dual rate of Interest in the Award. The Award directs payment of Interest @ 9% for 120 days post award; if the amount awarded is not paid within 120 days’, the rate of Interest is scaled up to 15% on the sum awarded. The dual rate of Interest awarded seems to be unjustified. The award of a much higher rate of Interest after 120 days’ is arbitrary, since the Award- debtor is entitled to challenge the award within a maximum period of 120 days’ as provided by Section

34(3) of the 1996 Act . If the award-debtor is made liable to pay a higher rate of Interest after 120 days, it would foreclose or seriously affect his statutory right to challenge the Award by filing objections under section 34 of the said Act.

9. The imposition of a high rate of interest @ 15% post- 120 days is exorbitant, from an economic standpoint, and has no co-relation with the prevailing contemporary international rates of Interest. The Award-debtor cannot be subjected to a penal rate of interest, either during the period when he is entitled to exercise the statutory right to challenge the Award, before a Court of law, or later. Furthermore, the arbitral tribunal has not given any reason for imposing a 15% rate of Interest post 120-days.

10. The Petitioner in his written submissions submitted a chart which shows that the Interest component of the Award amounts to almost 50% of the sum awarded. The grant of 15% Interest is excessive and contrary to the principle of proportionality and reasonableness.

11. It is also relevant to note that as per Clause 35.2.3 (supra) of the Conditions of Contract, it was expressly provided that there would be no consequential damages payable by the Purchaser to the Supplier in the event of termination of the contract, as the supplier would get 105% of the costs incurred. The Claimant/Respondent has, in fact been awarded 105% of the costs incurred under the EPC Contracts by the arbitral tribunal. The award of Interest @ 9% on the Euro component of the Claim is unjustified and unwarranted. The levy of such a high rate of Interest on a claim made in a foreign currency, would result in the Claimant being awarded compensation, contrary to the conditions stipulated in the Contract.

12. The Award has granted a uniform rate of 9% S.I. on both the INR and the EUR component. However, when the parties do not operate in the same currency, it is necessary to take into account the complications caused by differential interest rates. Interest rates differ depending upon the currency. It is necessary for the arbitral tribunal to co-ordinate the choice of currency with the interest rate. A uniform rate of Interest for INR and EUR would therefore not be justified. The rate of 9% Interest on the INR component awarded by the arbitral tribunal will remain undisturbed. However, with respect to the EUR component, the award-debtor will be liable to pay Interest at the LIBOR rate + 3 percentage points, prevailing on the date of the Award.

13. In light of the above-mentioned discussion, the Interest awarded by the arbitral tribunal is modified only to the extent mentioned hereinbelow :-

(i) The Interest rate of 15% post 120 days granted on the entire sum awarded stands deleted. A uniform rate of Interest @ 9% will be applicable for the INR component in entirety till the date of realization.

(ii) The Interest payable on the EUR component of the Award will be as per LIBOR + 3 percentage points on the date of Award, till the date of realization.

The Appeal is disposed of accordingly.

