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Award of Damages in Arbitration- State of Rajasthan Case

Tannishtha Singh,
Partner, MCO Legals
BSL LLB, ILS Law College, Pune
Expertise: Civil Litigation, Commercial Arbitration,
Legal Due Diligence, Statutory Compliances

Shivangi Pathak,
Research Partner
B.A., LLB (Hons), Calcutta University

1. Introduction

1.1 Sections 73 and 74 of the Indian Contract Act, 1872, provide for compensation for loss or damage caused by breach of contract, i.e., payment of damages by the party who has caused the breach to the party who has suffered a loss by reason of such breach.

1.2 A claim for damages cannot be granted simply for the asking, such claim must be backed by evidence of actual loss or injury. A mere breach cannot support a claim for damages.

1.3 The provisions contemplate both liquidated as well as unliquidated damages implying that damages can be claimed and granted even when the same are not quantified. In such cases, the courts are authorised to quantify the damages on an application being made by the concerned party.

1.4 Similar principles in relation to damages apply when a claim for such is made in arbitral proceedings.

1.5 In *Raheja Universal Pvt. Ltd. v. B.E. Bilimoria & Co. Ltd. (2016) 3 AIR Bom R 637,* the Bombay High Court set aside an award granting liquidated damages on the ground that no evidence had been led for proof of any loss or damage.

1.6 However, the apex court, in *Oil and Natural Gas Corporation Limitedvs SAW Pipes Ltd.*, *(2003) 5 SCC 705*, held that terms of the contracts should be taken into account to determine whetherthe claim for liquidated damages can be allowed. It was also clarified that the court has the authority to award reasonable compensation to the aggrieved party even if the actual loss suffered is not proved or a fair estimation/assessment of the same is not possible. This principle was also laid down in *Maula Bux Vs Union of India (1969)2 SCC 554.*

1.7 As far as computation of damages is concerned, tribunals may exercise their discretion in adopting the formula for computation unless provided for in the underlying contract (Ref: *McDermott International Inc. v. Burn Standard Co. Ltd.; (2006) 11 SCC 181.*)

1.8 In *AT Brij Paul Singh vs. State of Gujarat, AIR 1984 SC 1703,* the Supreme Court held that tribunals may apply the exercise of "honest guess work" based on the evidence on record is determination of damages especially in the nature of loss of profits.

2. Issue

2.1 In view of the decisions of the courts, it is amply clear that arbitral tribunals have the competence and power to award damages in arbitration proceedings.

2.2 The issue being discussed in this article is the law in relation to award of damages in arbitration proceedings and additionally, the relevance of claim for interest on damages.

3. Award of damages in arbitration

3.1 In *State of Rajasthan vs. Ferro Concrete Construction Private Limited, (2009) 12 SCC 1*, the Supreme Court dealt with the question of award of damages in the arbitration.

3.2 The brief facts of the case are that the parties entered into a contract for laying and commission of water pipeline. Disputes arose between the parties when the contractor abandoned the work and the employer took steps for having the balance work completed by an alternate agency.

3.3 The parties referred the dispute to arbitration.

3.4 In the facts of that case, the contract between the parties provided for imposition of liquidated damages in the terms of the contract, in case the work is left incomplete.

3.5 Before the arbitrator, the claimant made a claim for certain amount as damages which was allowed by the arbitrator.

3.6 The award was challenged under the Arbitration Act, 1940 and continuing litigations and appeals brought the challenge before the Supreme Court.

3.7 The Supreme Court was of the view that the calculation of how the figure claimed as damages was arrived at was an error apparent on the face of the award. The claim of the claimant for damages was not supported by any evidence at all. In fact, the arbitrator also did not provide any reasons for awarding the damages and the explanation as to the method of reaching the amount.

3.8 The claim for damages related to additional costs incurred in manufacturing pipelines. However, no evidence or documents were produced to prove that such costs were actually incurred or that additional manufacture was required.

3.9 The Supreme Court held that in such circumstances when the claim for damages does not correspond to any proof of actual damages or any evidence as to the manner or formula adopted for the calculation, it was beyond jurisdiction of the arbitrator to award the claim for damages. It was further held that this would render the award illegal and unsustainable.

3.10 It was also held that an award that is not based on any evidence leads to legal misconduct. The arbitrator cannot award damages solely on the basis of the claim statement or considering such statement as the proof or quantum of evidence.

3.11 Thus, the Court set aside the award to the extent of grant of damages at the amount which was claimed by the claimant and allowed by the arbitrator.

4. Interest on amount awarded as damages

4.1 In *State of Rajasthan vs. Ferro Concrete*, the award was also challenged on the ground that interest on damages could not have been awarded for the pre-award time period.

4.2 The Court relied on *Secretary, Irrigation Department, Government of Orissa vs. G. C. Roy - 1992 (1) SCC 508*, *Dhenkanal Minor Irrigation Division vs. N. C. Budharaj - 2001 (2) SCC 721* and *Bhagawati Oxygen Ltd. vs. Hindustan Copper Ltd - 2005 (6) SCC 462* where the unanimous view has been that the arbitrator has jurisdiction and authority to award pre-reference, *pendente lite* and future interest.

4.3 It was argued that unlike in the case of sums due being an ascertained amount, in case of damages, interest becomes payable only from the date of quantification of the amount payable as damages, hence, award of interest for pre-award period was illegal.

4.4 On such point, the Court relied on Section 3 of the Interest Act, 1978 and explained the position regarding award of interest.

4.5 It observed that interest can be awarded even in a claim for damages for the pre-award period or the period before the quantification of damages where the contract between the parties specifically provides for the same or a written demand for interest had been made for payment of interest on damages before the initiation of action.

4.6 Thus, the Court found that grant of interest on damages from the date when parties entered reference in arbitration and appointed the arbitrator, was justified.

4.7 However, the Court also clarified that the rate of interest awarded should not exceed the "current rate of interest" as provided under the Interest Act.

4.8 In such considerations, the Court modified the interest component in the award.

5. Conclusion

5.1 The adjudication on claim for damages in an arbitration proceeding is well within the domain of an arbitrator.

5.2 However, in light of the decisions of the courts and the reliance placed on sections 73 and 74 of the ICA in such decisions, it may be concluded that such claims may only be allowed on sufficient proof being shown by the party as to the existence of actual loss incurred.

5.3 In cases where the amount is unquantifiable, but the existence of loss has been proved, the tribunal may grant a fair estimate on account of damages. Further, the reasons and manner for arriving at such quantification shall also be disclosed.

5.4 The tribunal may only award damages after the party claiming such having proved the existence by adducing evidence or producing documents in relation to the claim.

5.5 The issue of interest on damages may be settled by the tribunal with due regard to the relevant provisions of the Interest Act.

A copy of the judgment is annexed hereto at **page 3 to 28.**

THE
SUPREME COURT CASES
(2009) 12 SCC

(2009) 12 Supreme Court Cases 1

(BEFORE R.V. RAVEENDRAN AND L.S. PANTA, JJ.)

STATE OF RAJASTHAN AND ANOTHER . . Appellants;

Versus

FERRO CONCRETE CONSTRUCTION PRIVATE LIMITED . . Respondent.

Civil Appeals No. 2764 of 2009† with No. 2767 of 2009‡, decided on April 22, 2009

A. **Arbitration Act, 1940 — S. 30 — Award not based on any evidence, if, amounts to legal misconduct — Quantum of evidence required — Arbitrator making award solely on the basis of claim statement considering claim itself as proof — Impermissibility — Held, arbitrator awarding claim equating it as proof without looking for or insisting on proof, held, is legal misconduct and error apparent on face of the award — Arbitration and Conciliation Act, 1996, S. 34**

B. **Contract and Specific Relief — Remedies for breach of contract — Damages — Measure/Quantification of Damages — Compensation for loss of profit — Evidence to be led and facts to be proved, discussed — Contract Act, 1872, S. 73**

Held :

An agreement was entered into between the employer and the contractor for the manufacture, laying, testing and commissioning of water pipeline of a length of about 38 km under a water supply scheme in Ajmer District. The value of the work as per the work order was about Rs 9.9 crores. 10% of the value of work (Rs 99.19 lakhs) agreed to be released as mobilisation advance, was released to the contractor. The contractor created an equitable mortgage over its plant by depositing its title deeds thereto as security for the mobilisation advance and agreed to keep the original title deeds in deposit with the employer till the entire

† Arising out of SLP (C) No. 10818 of 2007. From the Judgment and Order dated 5-2-2007 of the High Court of Rajasthan, Jaipur Bench, Jaipur in SB Civil Misc. Appeal No. 872 of 2003

‡ Arising out of SLP (C) No. 22565 of 2007

amount of advance was repaid in full with interest. The contractor stopped the work after it had manufactured 15.26 km of pipes and had laid 11.6 km out of them and tested only 1.4 km of pipeline. The employer notified the contractor that if he did not resume the work, the balance of the work would be got executed through an alternative agency in terms of the contract, by treating the contract as having been abandoned, and recover the excess cost from the contractor. As the contractor did not resume the work, the employer initiated steps to get the balance work executed through an alternative agency.

On the matter being referred to arbitration, after considering the claims and counterclaims, the arbitrator inter alia in regard to Claim 37-A, directed the employer to pay Rs 12,072 per day from the date of award. In regard to Counterclaim 3 (Rs 79,87,846 towards refund of mobilisation advance with interest), the arbitrator awarded a sum of Rs 59,42,275 with interest at 18% per annum from 18-9-1990 up to the date or decree and directed that the amount be adjusted from the amounts awarded to the contractor and release title documents of plant and machinery. The arbitrator further directed the employer that in case of failure to release documents, the employer is liable to pay Rs 12,072 per day from the date of award.

The District Judge made the award a rule of court despite objections from the employer with a modification of Claim 37-A directing the employer to return the original title deeds to the contractor and pay the amounts awarded to the contractor after deducting the amount awarded by way of counterclaim (that is Rs 59,42,275 towards refund of mobilisation advance due with 18% interest) within 30 days from the date of decree.

The employer filed an appeal against the said judgment and decree. The contractor also filed an appeal aggrieved by the modification. The High Court dismissed the appeal filed by the employer but allowed the appeal filed by the contractor and restored the direction of the arbitrator that the payment of compensation at Rs 12,072 per day should be from the date of the award itself. The High Court also granted interest at 18% per annum from the date of the award. Feeling aggrieved the employer filed the present appeals by special leave.

Partially allowing the appeals, the Supreme Court

Held :

A sum of Rs 12,072 per day was claimed as damages by the contractor for loss of profits on the basis that the contractor would have manufactured 15 pipes per day of the value of Rs 1,20,000 and that the profit and overhead element out of it would have been 15% or Rs 18,000 per day. By taking the working days as 306 in a year and deducting 20% of labour component, the loss of profit per day was calculated to be Rs 12,072 per day. There is no evidence to show that the contractor was at any point of time manufacturing 15 pipes a day of the value of Rs 8000 each or that he would have made a profit of 15% on the cost thereof. The claim is made on the ground that it is disabled from manufacturing that many number of pipes elsewhere. (Para 52)

There is no evidence that the contractor had other contracts where it was required to manufacture that number of pipes or that it could not manufacture the required pipes for want of plant and machinery. Nor is there any evidence as to the value of the plant and machinery that had been mortgaged to the employer and what would be the cost of an alternative plant with a capacity to manufacture

15 pipes per day. If the plant and machinery was of the value of say Rs 25 lakhs, or if the contractor could install another similar plant at a cost of Rs 25 lakhs, then the loss at best would be interest on Rs 25 lakhs and not anything more. (Para 53)

In fact even though there is no evidence, while making Claims 36 and 37 the contractor has given value of the plant and machinery as Rs 36,84,161. Even assuming the said figure to be true, at best the blocked up investment was only Rs 36,84,161 and the loss would be around 1% thereon per month by way of interest which would be Rs 36,841 per month. What is more strange is that nowhere in the award the arbitrator considers the validity of the claim of Rs 12,072 per day nor accepts the said claim as valid or correct. In a reasoned award if the claim of a contractor is equated to proof of the claim, then it is obviously a legal misconduct and an error apparent on the face of the award. (Para 54)

While the quantum of evidence required to accept a claim may be a matter within the exclusive jurisdiction of the arbitrator to decide, if there was no evidence at all and if the arbitrator makes an award of the amount claimed in the claim statement, merely on the basis of the claim statement without anything more, it has to be held that the award on that account would be invalid. The entire award under this head is wholly illegal and beyond the jurisdiction of the arbitrator, and wholly unsustainable. (Para 55)

C. **Arbitration Act, 1940 — Ss. 33, 30 and 14 — Wrong conclusion of arbitrator, if ground for setting aside award — Reappreciation of evidence by court — Permissibility — Arbitrator reaching a wrong conclusion or failing to appreciate facts while making award, held, is not ground for setting aside of award — Court while considering challenge to award does not sit in appeal over the findings of arbitrator nor reappreciate evidence — When there is no allegation of moral misconduct against the arbitrator with reference to the award, award can be challenged only on grounds of legal misconduct of arbitrator and on error apparent on face of the award — Arbitration and Conciliation Act, 1996, Ss. 34 and 35**

(Paras 18, 20, 68, 69 and 72)

Champsey Bhara & Co. v. *Jivraj Balloo Spg. & Wvg. Co. Ltd.*, (1922-23) 50 IA 324 : AIR 1923 PC 66; *State of Rajasthan* v. *Puri Construction Co. Ltd.*, (1994) 6 SCC 485, *relied on*

D. **Arbitration Act, 1940 — S. 30 — Award of arbitrator — Legal misconduct — Terms of agreement — Overlooking of, by arbitrator, if constitutes legal misconduct — Bilateral agreement between parties providing for release of mobilisation advance in instalments subject to submission of guarantee bond and certificate of utilisation of previous instalment — Arbitrator awarding claim based on delay in release on part of employer, overlooking bilateral agreement — Held, arbitrator committed legal misconduct — On facts, there was no breach on part of employer and contractor himself was responsible for the delay — Hence question of compensating does not arise — Contract Act, 1872 — S. 73 — Arbitration and Conciliation Act, 1996, S. 34** **(Paras 39 and 40)**

E. **Contract and Specific Relief — Remedies for breach of contract — Damages for anticipatory breach — Pleading and proof necessary — Arbitrator suo motu building up a case for and awarding such damages —**

Impermissibility — Award for "breach, if made in future" — Tenability — Held, in present case reasoning for directing such payment was strange — Awarding payment was not because of breach by employer but for "breach if made in future" — There was no such claim — Hence the award was beyond reference — Further, award and interest for mortgaged plant and machinery in favour of employer was given till date of award, whereas damages for non-utilisation of the same were awarded to contractor till release of documents — Hence, making of such an award is error apparent on face of the award and legal misconduct of arbitrator or proceedings — Arbitration and Conciliation Act, 1996 — S. 34 — Arbitration Act, 1940, S. 30

F. **Contract and Specific Relief — Remedies/Relief — Arbitration award — Adjustment of claims for ascertained sum against claims for unascertained sum — Tenability — Arbitration Act, 1940 — S. 30 — Arbitration and Conciliation Act, 1996 — S. 34 — Contract Act, 1872, S. 73**

Held :

The award under Claim 37-A i.e. a claim for compensation for loss of production in the factory from 13-1-1992 was made, not on account of any breach committed by the employer, but in respect of *a breach* if *made in future* after the date of the award. There was no such claim and the award was therefore beyond the reference. (Paras 48 and 46)

The reasoning of the arbitrator is very strange and is a classic case of an error apparent on the face of the award and a legal misconduct. The arbitrator rejected Claim 37-A for payment of Rs 12,072 as compensation for loss of production from 13-1-1992 (which was the subject-matter of the claim) on the ground that the plant had been mortgaged in favour of the employer by the contractor and therefore there was no justification for the contractor to claim that it should be permitted to remove and take away the plant when the mortgage subsisted. Having rejected the claim, the arbitrator evolved a strange reasoning that though there was a subsisting valid mortgage in respect of the mobilisation advance with interest in favour of the employer, because he had made an award in favour of the employer for Rs 59,42,275 plus interest, the mortgage came to an end and the employer became liable to return the documents and if it failed to return the documents, the contractor was entitled to damages of Rs 12,072 per day from the date of award. However, evidently, until the amount of Rs 59,42,275 with interest was paid by the contractor to the employer, the mortgage would continue. If the mortgage continued, there was no obligation on the part of the employer to return the documents; and if there was no obligation on the part of the employer to return the documents, the contractor could not complain that the documents were wrongly held by the employer nor could it claim loss of production as a result of the employer wrongly withholding the documents. This to say the least is legal misconduct and an error apparent on the face of the award. (Paras 49, 50, 51 and 41)

Moreover, the mobilisation advance amount was an ascertained sum due to the employer from the contractor, with a specific provision for interest. There was a specific contract for continuation of the mortgage until the said amount was paid. On the other hand the amounts that allegedly became due to the contractor under the award were mostly towards damages and escalation in prices, validity of which were under challenge and there was no provision in the

contract for payment of interest thereon. At best the arbitrator could have directed return of the documents of title to the contractor and could not have directed payment of damages at the rate of Rs 12,072 per day. (Paras 56 and 57)

[**Ed.**: It is interesting to note that one can make a claim for damages for anticipatory breach: *see Jawahar Lal Wadhwa* v. *Haripada Chakroborty*, (1989) 1 SCC 76; though it would seem that it would be a sine qua non for the award of such of damages that a claim is brought by the promisee and the court or arbitrator cannot suo motu build up a case for and award such damages. *See also* **Avtar Singh: *Contract & Specific Relief*, 10th Edn.**, Eastern Book Company, pp. 448 et seq.; Treitel, G.H: *The Law of Contract*, 10th Edn., pp. 798-99; *Anson's Law of Contract*, 28th Edn. pp. 572-73.]

G. **Contract and Specific Relief — Performance of contract — Modes and order of performance — Binding effect of terms of contract — Breach of contract when made out — Claimant complying with terms of agreement for release of mobilisation advance in instalments but claiming damages for delay in release of mobilisation advance in instalments and not in single instalment — Delay in releasing of mobilisation advance, on facts, if could be fastened on employer and if amounted to a breach — Held, conduct of claimant suggests that terms in bilateral agreement were binding on parties and mobilisation advance was to be released in instalments — Hence, there was no delay or breach on part of employer — Evidence Act, 1872 — S. 115 — Contract Act, 1872, Ss. 50, 51 and 8** (Paras 36 to 38)

H. **Contract and Specific Relief — Variation, Rectification and Novation of Contract — Expressly/by renegotiation, etc. — Instances — Later bilateral agreement specifically incorporating modifications, held, would be binding — Contract Act, 1872, S. 62** (Paras 32 to 34)

I. **Arbitration Act, 1940 — S. 30 — Arbitral award — Awarding a claim which was not pleaded — Impermissibility — Arbitration and Conciliation Act, 1996, S. 34** (Paras 41 and 52)

J. **Arbitration and Conciliation Act, 1996 — S. 31(7) — Award of interest by arbitrator — Reiterated, in absence of any express bar in the contract in regard to interest, the arbitrator can award interest — Arbitration Act, 1940, S. 29** (Para 60)

Irrigation Deptt., Govt. of Orissa v. *G.C. Roy*, (1992) 1 SCC 508; *Dhenkanal Minor Irrigation Division* v. *N.C. Budharaj*, (2001) 2 SCC 721; *Bhagawati Oxygen Ltd.* v. *Hindustan Copper Ltd.*, (2005) 6 SCC 462, *relied on*

K. **Arbitration and Conciliation Act, 1996 — S. 31 — Award of interest by arbitrator — Pre-reference period (i.e. from due date up to date of reference) — Held, arbitrator empowered to allow interest if contract is silent as to payment of interest in regard to pre-reference period in terms of Interest Act, 1978 — Where contract provides for interest, it shall be paid in accordance with the contract and in case of express barring of payment of interest by contract, no interest shall be awarded — Arbitration Act, 1940 — S. 29 — Interest Act, 1978, S. 3** (Paras 63 to 65)

L. **Arbitration and Conciliation Act, 1996 — S. 31(7) — Award of interest — Pendente lite (date of institution of proceedings to date of award) and future interest (from the date of award to date of payment) — Held, award of interest for pendente lite and future periods will be governed by S. 34 CPC or law governing arbitration — Interest Act, 1978 is not**

applicable — Arbitration Act, 1940 — S. 29 — Interest Act, 1978 — S. 3 — Applicability (Para 65)

M. **Arbitration Act, 1940 — S. 29 — Award of interest on damages — Permissibility — Conditions prerequisite — Change effected in the law by Interest Act, 1978 — Held, interest on damages can be awarded if: (i) contract specifically provides for it, or (ii) a written demand had been made for payment of interest on the damages before initiation of action — In case of unascertained or unquantified amounts, interest should be from date of demand or future date and for ascertained sums due, interest will be from date when they became due — In present case, interest awarded only from date of petition for appointment of arbitrator — Hence, no reason to interfere as to date of commencement of interest — Contract and Specific Relief — Remedies/Relief — Remedies for breach of contract — Interest — Interest Act, 1978 — S. 3 — Arbitration and Conciliation Act, 1996, S. 31(7) (Para 66)**

Iron & Hardware (India) Co. v. *Firm Shamlal & Bros.*, AIR 1954 Bom 423, *held, legislatively superseded*

N. **Arbitration Act, 1940 — S. 29 — Rate of interest — Pre-reference, pendente lite and future period — Appropriate rate of interest — Interest at 18% p.a. — Permissibility — Held, award of interest at 18% p.a. under Arbitration Act, 1940 was an error apparent on the face of the award — Pre-reference interest should be 9% in terms of Interest Act, 1978 — Thus, in present case, held, same rate appropriate for pendente lite and future interest — Arbitration and Conciliation Act, 1996, S. 31(7) (Para 67)**

N-D/43310/S

Advocates who appeared in this case :

Vijay Hansaria, Senior Advocate (Jatinder Kr. Bhatia, B.N. Jha and Ms Sneh Kalita, Advocates) for the Appellants;

Dushyant Dave, Ravindra Shrivastava and Kishore Shrivastava, Senior Advocates (Kunal Verma, Rajul Shrivastava, Aniruddh Rajput, Manish Chaudhary and C.G. Solshe, Advocates) for the Respondent.

Chronological list of cases cited ***on page(s)***

1. (2005) 6 SCC 462, *Bhagawati Oxygen Ltd.* v. *Hindustan Copper Ltd.* 22*f*
2. (2001) 2 SCC 721, *Executive Engineer, Dhenkanal Minor Irrigation Division* v. *N.C. Budharaj* 22*e-f*
3. (1994) 6 SCC 485, *State of Rajasthan* v. *Puri Construction Co. Ltd.* 11*f-g*
4. (1992) 1 SCC 508, *Irrigation Deptt., Govt. of Orissa* v. *G.C. Roy* 22*e-f*
5. AIR 1954 Bom 423, *Iron & Hardware (India) Co.* v. *Firm Shamlal & Bros.* 22*h*
6. (1922-23) 50 IA 324 : AIR 1923 PC 66, *Champsey Bhara & Co.* v. *Jivraj Balloo Spg. & Wvg. Co. Ltd.* 11*c*

The Judgment of the Court was delivered by

R.V. RAVEENDRAN, J.— Leave granted. Heard learned counsel. The appellants (also referred to as "the employer") invited tenders for the manufacture, laying, testing and commissioning of water pipeline of a length of 37.41 km under a water supply scheme in Ajmer District. Tenders were received from various tenderers including the respondent (hereinafter referred to as "the contractor").

2. As different tenderers had stipulated different terms and conditions, the tenderers were invited for discussions, and Common Terms of Reference (for short "CTR") were formulated on 22-2-1988 and the original tender conditions stood modified to the extent of the alterations in CTR. Thereafter the offer of the respondent was accepted and a work order dated 23-8-1988 was issued to him stipulating the period for completing the contract as two years from that date. There was an amendment to the work order on 8-11-1988.

3. The employer and the contractor entered into an agreement dated 11-1-1989 enumerating and stipulating the documents which will form part of the contract and the modifications agreed to in regard to certain terms. The value of the work as per the work order was Rs 9,91,94,602.50. Ten per cent of the value of work (Rs 99.19 lakhs) which was agreed to be released as mobilisation advance, was released to the contractor between 25-1-1989 and 5-5-1989. The contractor created an equitable mortgage over its plant by depositing its title deeds thereto as security for the mobilisation advance. By letter dated 15-12-1990, the contractor confirmed that the original title deeds will remain in deposit with the employer till the entire amount of advance was repaid in full with interest.

4. The contract (Clause 23 of the General Conditions of Contract) provided for settlement of disputes by arbitration. By letter dated 18-6-1990 the respondent invoked the provision for arbitration and sought appointment of an arbitrator to decide its claims aggregating to Rs 2,01,66,547 arising on account of certain alleged omissions and commissions of the employer. Another dispute was raised in respect of the rate payable for work done subsequent to the due date of completion (22-8-1990).

5. On 22-8-1990 the contractor stopped the work. By that date it had manufactured 15.26 km of pipes and had laid 11.6 km out of them and tested only 1.4 km of pipeline as against the total contracted quantity of 37.41 km. On 13-9-1990 the employer notified the contractor that if he did not resume the work, the balance of the work would be got executed through an alternative agency in terms of the contract, by treating the contract as having been abandoned on 22-8-1990, and recover the excess cost from the contractor.

6. The respondent contractor sent a reply dated 3-11-1990 stating its efforts to complete the work were rendered futile on account of the delays and breaches on the part of the employer; and it was necessary to enter into a fresh agreement as the tender was not accepted in the manner in which it ought to have been accepted. The contractor did not resume the work. The contractor's stand was that in the absence of an extension of time for completion by mutual consent before the stipulated date for completion, it was not liable to continue the work on the tendered rates.

7. The employer on 30-3-1991 made a final demand calling upon the contractor to state whether it was ready to restart and complete the remaining

work and if so to submit a revised time schedule for such completion. As the contractor did not resume the work, the employer initiated steps to get the balance work executed through an alternative agency.

8. In the meanwhile the contractor filed a suit against the appellant in the District Court, Ajmer and obtained a temporary injunction restraining the employer from imposing liquidated damages. The contractor made an application to the District Court, Ajmer, under Section 20 read with Section 8 of the Arbitration Act, 1940 ("the Act", for short) for filing the arbitration agreement into the court and seeking appointment of an arbitrator.

9. The District Court, Ajmer by an order dated 27-4-1991 held that it had the jurisdiction to appoint an arbitrator but deferred the actual appointment to a future date. The contractor revised its claim to Rs 5,51,90,306 in the notice of appointment of an arbitrator. The employer challenged the order of the District Judge and the High Court allowed the appeal on 9-8-1991 and set aside the order of the District Judge. The contractor in turn approached this Court.

10. On 12-11-1991, this Court recorded the consent of parties for appointment of Mr B.L. Mathur as the sole arbitrator and directed the employer (Chief Engineer, Public Health Engineering Department, State of Rajasthan) to appoint him as the arbitrator. On being appointed, the arbitrator entered upon the reference and the contractor filed a claim statement before the arbitrator on 13-1-1992 making 43 claims aggregating to Rs 6,21,29,626. The employer filed its reply to the claim statement, and also made five counterclaims aggregating to Rs 8,63,46,505 before the arbitrator.

11. In the meanwhile, the employer having concluded the arrangements to get the work completed through an alternative agency, on the contractor's failure to resume the work, awarded the work to M/s Indian Hume Pipes Co. Ltd. on 10-8-1992. On the basis of the contract value in regard to the balance work, the employer revised its Counterclaim 2 relating to extra cost to Rs 6,66,62,000 and consequently the total of the counterclaims stood increased to Rs 11,55,98,388.

12. After considering the claims and counterclaims, the learned arbitrator made an award dated 21-9-1994. He rejected Claims 4, 7, 8, 10, 14, 21, 22, 23, 26, 36, 36-A, 37, 38, 39, 40, 41 & 41-A, 42 & 42-A and 43 of the contractor. He awarded the following amounts to the contractor in regard to the remaining claims:

Sl. Nos.	*Claim*	*Description of claim*	*Amount claimed Rs*	*Amount awarded Rs*
1.	1	Loss of profitability due to late release of mobilisation advance	83,49,913	33,06,500
2.	2 and 16	Refund of excess sales tax deducted	2,94,142	2,94,142

a	*3.*	3 and 15	5% amount withheld for testing of pipeline	14,70,956	14,70,956
	4.	5 and 18	Excess recovery of security deposit	13,28,457	13,28,457
	5.	6 and 17	Price escalation	58,83,854	43,47,520
b	*6.*	9 and 19	Refusal of employer for redesigning pressure pipes from higher into lower	10,11,354	6,95,910
	7.	11 and 20	Slow progress due to reduction of width of trench	21,32,496	21,07,195
	8.	24	Refund of deduction for want of BG renewal	4,31,926	4,31,926
c	*9.*	27 and 28	Gas pipes fitted	2,60,200	67,098
	10.	29	Payment for 8 kg pipes but paid for 6 kg pipes	1,17,150	1,12,294
	11.	30	Refunds for paint of specials	9759	9759
	12.	31	Deduction from running bill for pipes	22,385	22,385
d	*13.*	32	Refund for deduction for insufficient refilling	46,569	46,569
	14.	33	Less measurement of pipe	1,15,738	1,15,738
	15.	35 with 25	Difference in final bill Less payment re: sand bedding	1,47,00,000 7,31,676	23,74,458
e		34	Payment for excavation	2,50,740	
	16.	37-A	Idle charges for machinery, staff, etc.	12,072 per day from 13-1-1992	12,072 per day from date of award, if the factory was not released from mortgage security within 30 days.
f					
g	*17.*	12 and 13	Interest (pre-reference, pendente lite and future)	18% per annum	18% per annum

The arbitrator rejected Counterclaims 1, 2, 4 and 5 of the employer. In regard to Counterclaim 3 (Rs 79,87,846 towards refund of mobilisation advance with interest), the arbitrator awarded a sum of Rs 59,42,275 with interest at 18% per annum from 18-9-1990 up to the date or decree or payment, whichever was earlier.

h

13. The contractor made an application for making the award, a rule of the court. The employer challenged the award by filing objections under Section 30 read with Section 33 of the Act. By an order dated 17-2-2003, the District Judge, Ajmer allowed the application of the contractor and made the award a rule of the court subject to a modification in regard to the award made on Claim 37-A.

14. In place of the award made by the arbitrator (direction to employer to pay Rs 12,072 per day from the date of the award), the District Judge directed that the employer shall return the original title deeds to the contractor and pay the amounts awarded to the contractor after deducting the amount awarded by way of counterclaim (that is Rs 59,42,275 towards refund of mobilisation advance due with 18% interest) within 30 days from the date of decree, failing which, the employer shall pay Rs 12,072 per day from the date of decree. The employer filed an appeal (Civil Miscellaneous Appeal No. 872 of 2003) against the said judgment and decree contending that the award ought to have been set aside. The contractor also filed an appeal (Civil Miscellaneous Appeal No. 910 of 2003) aggrieved by the modification by the learned District Judge directing compensation of Rs 12,072 per day only from the date of decree (instead of the date of award).

15. The High Court dismissed the appeal filed by the employer by judgment dated 5-2-2007. The High Court allowed the appeal filed by the contractor by judgment dated 30-5-2007 and restored the direction of the arbitrator that the payment of compensation at Rs 12,072 per day should be from the date of the award itself (21-9-1994). The High Court also granted interest at 18% per annum from the date of the award. Thus the High Court upheld the award. Feeling aggrieved, the employer has filed these two appeals by special leave. The first of the appeals [arising out of SLP (C) No. 10818 of 2007] is against the dismissal of its appeal on 5-2-2007. The second of the appeals [arising out of SLP (C) No. 22565 of 2007] is against the judgment dated 30-5-2007 allowing the contractor's appeal.

16. One of the contentions urged by the appellants before the court below was that the arbitrator did not have the jurisdiction to enter upon the reference and make an award, as the appointing authority under the arbitration clause had merely appointed the arbitrator, but had not *referred* any dispute to him for arbitration. The said contention was rejected by both the courts on the ground that when the authority competent to appoint the arbitrator appointed the arbitrator, in pursuance of the agreement reached before this Court to have the pending disputes of both parties settled by arbitration, the employer could not be permitted to raise a technical plea that the arbitrator had no jurisdiction to proceed with the arbitration, in the absence of a further specific reference by the employer. Realising the unsoundness of the said contention, the appellants did not press it before us.

17. On the contentions urged, the question that arises for consideration is whether there is any legal misconduct or error apparent on the face of the award, in regard to the award of the arbitrator in respect of:

(*i*) Claims 1 and 37-A;

(*ii*) Claims 12 and 13;

(*iii*) Claims 2 and 16, 3 and 15, 5 and 18, 6 and 17, 9 and 19, 11 and 20, 24, 27 and 28, 29, 30, 31, 32, 33, 35 (with Claims 25, 34); and

(*iv*) Counterclaims 1, 2, 4 and 5.

18. Section 30 of the Act inter alia provides that an award can be set aside on the ground that an arbitrator had misconducted himself or the proceedings, or that the award had been improperly procured or is otherwise invalid. An error apparent on the face of the award, is a ground for setting aside the award under Section 30 or for remitting the award to the arbitrator under Section 16(1)(*c*) of the Act.

19. In *Champsey Bhara & Co.* v. *Jivraj Balloo Spg. & Wvg. Co. Ltd.*[1] the Privy Council explained the term "an error of law on the face of the award" thus: (IA p. 331)

> "... An error in law on the face of the award means ... that you can find in the award or a document actually incorporated thereto, as for instance, a note appended by the arbitrator stating the reasons for his judgment, some legal proposition which is the basis of the award and which you can then say is erroneous."

20. It was well settled that under the Arbitration Act, 1940, an award was not open to challenge on the ground that the arbitrator has reached a wrong conclusion or failed to appreciate facts, as under the law, the arbitrator is made the final arbiter of the dispute between the parties. While considering the challenge to an award, the court will not sit in appeal over the award nor reappreciate the evidence for the purpose of finding whether on the facts and circumstances, the award in question could have been made. When there is no allegation of moral misconduct against the arbitrator with reference to the award, and where the arbitration has not been superseded, there were only two grounds of attack. First was that there was legal misconduct on the part of the arbitrator in making the award. Second was that there was an error apparent on the face of the award.

21. This Court explained the principles relating to interference with awards under the 1940 Act in *State of Rajasthan* v. *Puri Construction Co. Ltd.*[2] thus: (SCC pp. 502-03, para 31)

> "*31.* ... Similarly, an award rendered by an arbitrator is open to challenge within the parameters of several provisions of the Arbitration Act. Since the arbitrator is a Judge by choice of the parties, and more often than not, a person with little or no legal background, the adjudication of disputes by an arbitration by way of an award can be challenged only within the limited scope of several provisions of the Arbitration Act and the legislature in its wisdom has limited the scope

1 (1922-23) 50 IA 324 : AIR 1923 PC 66
2 (1994) 6 SCC 485

and ambit of challenge to an award in the Arbitration Act. Over the decades, judicial decisions have indicated the parameters of such challenge consistent with the provisions of the Arbitration Act. By and large the courts have disfavoured interference with arbitration award on account of error of law and fact on the score of misappreciation and misreading of the materials on record and have shown definite inclination to preserve the award as far as possible. As reference to arbitration of disputes in commercial and other transactions involving substantial amount has increased in recent times, the courts were impelled to have fresh look on the ambit of challenge to an award by the arbitrator so that the award does not get undesirable immunity. In recent times, error in law and fact in basing an award has not been given the wide immunity as enjoyed earlier, by expanding the import and implication of 'legal misconduct' of an arbitrator so that award by the arbitrator does not perpetrate gross miscarriage of justice and the same is not reduced to mockery of a fair decision of the lis between the parties to arbitration. Precisely for the aforesaid reasons, the erroneous application of law constituting the very basis of the award and improper and incorrect findings of fact, which without closer and intrinsic scrutiny, are demonstrable on the face of the materials on record, have been held, very rightly, as legal misconduct rendering the award as invalid. It is necessary, however, to put a note of caution that in the anxiety to render justice to the party to arbitration, the court should not reappraise the evidence intrinsically with a close scrutiny for finding out that the conclusion drawn from some facts, by the arbitrator is, according to the understanding of the court, erroneous. Such exercise of power which can be exercised by an appellate court with power to reverse the finding of fact, is alien to the scope and ambit of challenge of an award under the Arbitration Act. Where the error of finding of facts having a bearing on the award is patent and is easily demonstrable without the necessity of carefully weighing the various possible viewpoints, the interference with award based on erroneous finding of fact is permissible. Similarly, if an award is based by applying a principle of law which is patently erroneous, and but for such erroneous application of legal principle, the award could not have been made, such award is liable to be set aside by holding that there has been a legal misconduct on the part of the arbitrator. In ultimate analysis, it is a question of delicate balancing between the permissible limit of error of law and fact and patently erroneous finding easily demonstrable from the materials on record and application of principle of law forming the basis of the award which is patently erroneous."

22. Keeping the said principles in mind let us examine the various claims.

Re: Claim 1

23. The contractor claimed that the mobilisation advance had to be released to it immediately on entrustment of work, to enable it to set up the factory for manufacturing the pipes. It was contended that prompt release of mobilisation advance was crucial and fundamental to the contract as manufacture of pipes depended upon setting up a factory for that purpose. Even assuming that the mobilisation advance could be released in three instalments, as per the modified terms and conditions, the contractor contended that there was inordinate delay on the part of the employer in releasing the instalments, that too, in five instalments.

24. The contractor further contended that if the mobilisation advance had been released immediately on award of the work, it would have set up a factory and commenced production within three months; that in view of the delay, it lost production for a period of eight months, that is, nearly one-third of the contract period, and that as a consequence they were not able to execute the work of the value of Rs 5,56,66,086 and the loss of profits and overheads on the said amount at a standard 15% was Rs 83,49,913 and it was entitled to that amount as compensation for the breach by the employer.

25. The calculation of the said loss of profit and overheads in Claim 1 was as follows:

Amount of contract (with ZVV)	Rs	9,91,94,602.00
Payment already received from the Department	Rs	2,88,28,516.00
Balance	Rs	7,03,66,086.00
Amount due to contractor against work done	Rs	1,47,00,000.00
Balance	Rs	5,56,66,086.00
Loss of profitability and overheads @ 15% (0.15 x 5,56,66,086)	Rs	83,49,913.00

26. The employer resisted the said claim contending that having regard to the relevant conditions in the work order and the contract agreement, the mobilisation advance had to be released in three instalments against bank guarantees; that the second and third instalments had to be released only on production of the certificate of a chartered accountant on the utilisation of the previously paid amount and on verification by the Department of the progress; and that the mobilisation advance was released in instalments in terms of the contract and there was no delay and no breach on their part.

27. We may refer to the relevant provisions of the contract in this behalf. Clause 8 of the Special Conditions relating to the establishment of factory at site provided thus:

"*Establishment of factory at site*

The contractor, if he so desires, may establish the pipe factory at site to avoid transportation of pipes. All material and equipment and land required for the purpose shall be arranged by the contractor at his own cost. The Department may assist him in acquisition of land. However, the work should not be delayed on this account. The firm should commence and continue to supply the pipes, etc. from their existing set-up till the factory at site is established. As already stated, the supply of pipes, etc. should commence within 30 days, from the award of contract."

28. Clause 8 was superseded by Clause 3 of the Common Terms of Reference which is extracted below:

"*Mobilisation advance (for PSC pipes only)*

10% of the contract value shall be given against bank guarantee as mobilisation advance at a simple interest rate of 18%. Recovery of mobilisation advance shall be effected from 1st Running Bill on pro rata basis in a way that complete mobilisation advance is recovered by the time 75% work is complete. Interest shall also be recovered along with recovery of capital mobilisation advance. The assets built by the contractor out of mobilisation advance so made will be mortgaged to the Department. In case work is left incomplete, liquidated damages will be imposed as per the terms of the document and the assets built by the contractor for manufacturing pipes will become the property of the Department. Such assets can be used by the Department for the purpose of completing the remaining work."

In the subsequent work order issued on 23-8-1988, Clause 5.1 relates to mobilisation advance.

29. While Para (*a*) of Clause 5.1 was a reproduction of Clause 3 of the Common Terms of Reference, the following was added as Para (*b*) in Clause 5.1 of the work order:

"The mobilisation advance is being given for the establishment of factory at site. In case the factory is not established in 3 months' period the mobilisation advance shall be recovered by way of the bank guarantee given in lieu of the mobilisation advance."

30. By letter of amendment dated 8-11-1988 issued by the employer, several clauses of the work order including Clause 5.1(*b*) were amended/replaced. Clause 5.1(*b*) as replaced is extracted below:

"The mobilisation advance is being given for establishment of factory at site. The mobilisation advance shall be paid in three instalments of which the second and third instalments shall be paid on production of a certificate of the chartered accountant about utilisation of the previously paid amount and on verification by the Department of the progress towards setting up of the factory."

31. This was followed by an agreement executed by both the parties on 11-1-1989 and Clause 7 thereof extracted below dealt with mobilisation advance:

"*Mobilisation advance*

(*a*) 10% of the contract value shall be given as mobilisation advance @ 18% simple interest subject to production of bank guarantee from any

nationalised bank equal to the amount of such advance. The recovery of such advance shall be effected from 1st Running Bill on pro rata basis in such a way that recovery of this advance is made by the time when 75% of the work is completed. Amount of interest is recoverable along with the recovery of principal amount.

(*b*) The assets built by the contractor out of the mobilisation advance shall be mortgaged with the Government. Such assets will not be mortgaged with any other agency for any purposes.

(*c*) In case the contractor fails to complete the work in specified time, the contractor shall pay the compensation as liquidated damages as per the terms and conditions of the contract and the assets built by the contractor for manufacturing of pipes will be the property of the Government and the Department will have right to use it as government property for completion of remaining work."

32. The arbitrator held that Clause 8 of the Special Conditions of Contract stood superseded by Clause 3 of the Common Terms of Reference which required the mobilisation advance to be released in one instalment and not in three instalments. He held that Clause 5.1(*b*) inserted by the amendment to the work order dated 8-11-1988 was an unilateral incorporation by the employer and was not binding on the contractor. He further held that the employer ought to have released the mobilisation advance along with the work order dated 23-8-1988, and the employer had abnormally delayed the release of mobilisation advance by a total period of 8.5 months by releasing it in instalments. He held that there was a clear delay of about 8 months and during that period the contractor could have executed one-third of the work of the value of Rs 3,30,64,867.50, and as the contractor was prevented from executing the said work on account of the delay, the contractor was entitled to 10% of the said amount, that is, Rs 33,06,500 as loss of profit. The said sum was therefore awarded to the contractor under Claim 1.

33. There is no doubt that Clause 8 of the Special Conditions of Contract has to be read with Clause 3 of CTR. It is true that Clause 3 of CTR did not contemplate the mobilisation advance being released in three instalments. But CTR was followed by the work order dated 23-8-1988 which was followed by an amendment dated 8-11-1988 which specifically stated that the mobilisation advance shall be paid in three instalments of which the second and third instalments shall be paid on production of a certificate of the chartered accountant about utilisation of the previously paid amounts and on verification by the Department towards progress of the factory. The arbitrator has held that the said clause was unilaterally introduced and therefore is not binding on the contractor. On the face of it this is erroneous.

34. After the work order, the parties have executed a bilateral agreement dated 11-1-1989 which specifically states at Para 2 and Para 6 that the work order dated 23-8-1988 and subsequent amendment to the work order dated 8-11-1988 shall be deemed to be a part of the contract and will bind both the

parties. The agreement dated 11-1-1989 itself contains a detailed clause (Clause 7) relating to mobilisation advance in addition to what was earlier agreed in regard to mobilisation advance. Therefore obviously the clauses relating to mobilisation advance in the amendment to the work order dated 8-11-1988 and the agreement dated 11-1-1989 had to be read in addition to the earlier provision relating to mobilisation advance contained in CTR.

35. Clause 5.1(*b*) of the work order, as amended, specifically provided that the contractor had to provide a bank guarantee for the mobilisation advance. Sub-clause (*b*) of Clause 7 of the agreement dated 11-1-1989 provided that assets built by the contractor by utilising the mobilisation advance should be mortgaged to the employer. Sub-clause (*c*) of Clause 7 provided that if the contractor fails to complete the work, the assets built by the contractor would become the property of the employer and the Department could use it as government property for completion of the remaining work. Sub-clause (*d*) of Clause 7 provided that if the contractor failed to establish the factory within three months of payment of the mobilisation advance, the said advance would be recovered by enforcing the bank guarantee given in lieu of the mobilisation advance. Thus it is evident that the mobilisation advance had to be released only against a bank guarantee to be furnished by the contractor.

36. If according to the contractor, the mobilisation advance had to be released in a single instalment and if the contractor wanted the entire mobilisation money to be released in one lump sum instead of in three instalments, it ought to have given a single bank guarantee for the entire sum. But strangely the contractor did not give such a bank guarantee. It gave four bank guarantees for Rs 40 lakhs on 21-5-1989, Rs 25 lakhs on 1-2-1989, Rs 15 lakhs on 17-2-1989 and Rs 25 lakhs on 23-3-1989. It is thus evident that the contractor had also proceeded on the basis that the condition in Clause 5.1(*b*) of the work order amendment letter dated 8-11-1988 governed the payment of mobilisation advance.

37. We find that the mobilisation amount corresponding to first bank guarantee was released within two days; mobilisation amount corresponding to second guarantee was released in seven days; and mobilisation amount corresponding to third guarantee, was partly released in 12 days and the balance in two months. The amount corresponding to the second and third bank guarantees had to be released only after the contractor produced a certificate in regard to the utilisation of the earlier advance.

38. It is seen that in regard to the first mobilisation advance the certificate was produced on 7-2-1989 and on the same day the second instalment was released. Insofar as the third instalment is concerned, the certificate was only received on 4-4-1989. Therefore it cannot be said that there was delay or breach on the part of the employer in releasing the mobilisation advance. If at all there was any delay, the delay was on the part of the contractor.

39. The fact that release of the mobilisation advance was governed by Clause 5.1(*b*) of the work order (as amended on 8-11-1988) and Clause 7 of the agreement dated 11-1-1989 was totally overlooked by the arbitrator by proceeding on the basis that mobilisation advance was governed by CTR alone. The arbitrator committed a legal misconduct by ignoring the terms of contract, that is, the agreement dated 11-1-1989, which specifically provided that in addition to CTR, the work order and amendment to work order dated 8-11-1988 would also form part of the contract.

40. The arbitrator also overlooked the fact that the additional provision regarding mobilisation advance was introduced in the agreement itself. Therefore the mobilisation advance was governed by the terms in CTR, the work order, the amendment to the work order dated 8-11-1988 and the agreement dated 11-1-1989 read together. If so read, it was clear that there was no breach on the part of the employer and the contractor was itself responsible for the delay. If so, the question of compensating the contractor on that score does not arise.

41. There is yet another aspect. The contractor claimed compensation on the basis that he could not do work of the value of Rs 5,56,66,086 in view of the delay and he was entitled to 15% thereof, namely, Rs 83,49,913 as compensation. But the arbitrator made an award in respect of the claim on the ground that there was delay in releasing the mobilisation advance and during that period of delay, one-third of the contract work could have been done and the value of the work that could have been done was Rs 3,30,64,867, and 10% thereof was the loss of profit. Firstly, there was no such plea. Secondly, we have already held that the delay relating to mobilisation advance was not on the part of the employer. Thirdly, even if there was delay, it was nobody's case that no work was done or that the contractor had suffered loss for non-execution of the work during the contract period. Therefore we are of the view that the award of compensation of Rs 33,03,500 towards Claim 1 is liable to be set aside.

Re: Claim 37-A

42. Claim 37-A was linked to mobilisation advance. The contractor claimed that it had mortgaged its pipe manufacturing unit in favour of the employer by deposit of title deeds as security for repayment of the mobilisation advance; that the machinery installed in the said factory had not been released by the employer in its favour and as a consequence, it could not be shifted to another place to enable it to start the manufacturing process elsewhere; and that on account of the failure on the part of the employer to release the plant, it had to keep the machinery idle and the employer was therefore liable to reimburse to the contractor the loss of production from 13-1-1992 at the rate of Rs 12,072 per day.

43. The contractor contended that if it had been permitted to shift its plant and machinery, it would have produced 15 pipes per day valued at Rs 1,20,000, that out of which the overhead and profit element was 15% (that is Rs 18,000 per day); that as there were 306 working days in a year, the loss of profits/overheads would be 18,000 x 306/365 = Rs 15,090 per day; and that if 20% thereof (Rs 3018) was deducted therefrom towards labour component, the loss of profit per day on account of non-availability of plant and machinery was Rs 12,072 per day.

44. The employer resisted the claim by contending that there was no obligation to release the plant and its title deeds until the mobilisation advance was repaid with interest; that the contractor had not repaid the mobilisation advance and interest thereon in spite of the award; and therefore the question of compensating any "daily loss" on that account did not arise. The employer also contested the correctness of the assumptions made for calculating the loss.

45. The contractor deposited the title deeds relating to the plant by way of mortgage of deposit of title deeds, in terms of the contract and specifically agreed that the original deeds will remain in deposit with the employer till the entire mobilisation advance was repaid with interest. It is also not in dispute that though a mortgage security was created on the plant, it continued to be in the possession, enjoyment and control of the contractor, as the employer did not take over physical possession of the plant at any point of time.

46. The arbitrator considered Claim 37-A with three other Claims (36, 36-A and 37). The particulars of the said claims are:

Claim 36	
Compensation for idling machinery, labour, staff due to delay and wrong decisions (for the period up to 12-1-1992)	Rs 48.21 lakhs
Claim 36-A	
Compensation for idling machinery, staff and labour, etc. from 13-1-1992	Rs 6370 per day
Claim 37	
Compensation for loss of production in the factory (for the period up to 12-1-1992)	Rs 61.48 lakhs
Claim 37-A	
Compensation for loss of production in the factory from 13-1-1992	Rs 12,072 per day

The arbitrator held that none of the four claims were maintainable as the factory built out of the mobilisation advance had been mortgaged in favour of the employer. As a consequence he did not award any amount in respect of the four claims.

47. But strangely the arbitrator directed payment of Rs 12,072 per day from the date of the award not because he held that there was any loss of production as a consequence of any breach by the employer, but on the following reasoning:

> "After perusal of the arguments of the parties and the evidence on record, I come to the finding that it is a case of real hardship to the claimants for having been denied the use of the factory and machinery elsewhere in their business venture, but *because of legalities involved, such as mortgage, the claimants cannot be given the benefit of any award*. Had the assets of the factory built out of mobilisation advance not being (*sic* been) mortgaged in favour of the respondent, I would have considered making an award in favour of the claimants. In view of the fact that I have allowed Counterclaim 3 of the respondent for balance amount of mobilisation advance in full along with interest, there is no reason why the assets built out of mobilisation advance should continue to remain mortgaged with the respondents. I therefore direct the respondent to release the documents relating to mortgage as mentioned above within a period of 30 days from the date of this award failing which the claimants shall be entitled to an award of Rs 12,072 per day from the date of this award till the date of release of mortgage. No award in favour of the claimants for the period I entered upon reference to the date of the publication of the award." (emphasis supplied)

48. Thus we find that the award under Claim 37-A was not made on account of any finding of breach on the part of the employer. It was made because the arbitrator had made an award against the contractor in favour of the employer for Rs 59,42,275 with interest. The arbitrator was of the view that if that sum was adjusted against the amounts due by the employer, there was no need for the mortgage of the plant to continue and therefore the employer should release the documents of title deposited by way of equitable mortgage, within 30 days from the date of the award; and that if the employer failed to do so, the employer should pay to the contractor Rs 12,072 per day from the date of the award till the date of release of the mortgage. Therefore, the said award under Claim 37-A was made, not on account of any breach committed by the employer, but in respect of *a breach* if *made in future* after the date of the award. There was no such claim and the award was therefore beyond the reference.

49. Further, the reasoning of the arbitrator is very strange and is a classic case of an error apparent on the face of the award and a legal misconduct. The arbitrator rejected Claim 37-A for payment of Rs 12,072 as compensation for loss of production from 13-1-1992 (which was the subject-matter of the claim) on the ground that the plant had been mortgaged in favour of the employer and therefore there was no justification for the contractor to claim that it should be permitted to remove and take away the plant when the mortgage subsisted. Having rejected the claim, the arbitrator

evolved a strange reasoning that though there was a subsisting valid mortgage in respect of the mobilisation advance with interest in favour of the employer, because he had made an award in favour of the employer for Rs 59,42,275 plus interest, the mortgage came to an end and the employer became liable to return the documents and if it failed to return the documents, the contractor was entitled to damages of Rs 12,072 per day from the date of award.

50. The arbitrator noticed the fact that the plant and machinery was mortgaged by deposit of title deeds in favour of the employer and that the contract was that "the original documents will remain in deposit with the employer till the amount of advance is repaid with full interest". The arbitrator in fact makes an award for return of Rs 59,42,276 in favour of the employer with interest at 18% per annum from 1-9-1990 to 17-9-1990 and interest at 18% per annum on Rs 59,42,275 from 18-9-1990 till date of decree or payment, whichever was earlier. Therefore evidently until the amount of Rs 59,42,275 with interest was paid by the contractor to the employer, the mortgage would continue. If the mortgage continued, there was no obligation on the part of the employer to return the documents; and if there was no obligation on the part of the employer to return the documents, the contractor could not complain that the documents were wrongly held by the employer nor could it claim loss of production as a result of the employer wrongly withholding the documents.

51. It is of some interest to note that as per the award of the arbitrator, made under Claim 37-A, on a claim that was never made, the amount that would become due at Rs 12,072 from 21-9-1994 to date will be approximately Rs 6,42,70,000. We have a strange situation where the arbitrator makes an award in favour of an employer directing the contractor to refund to the employer Rs 59,42,275 with interest at 18% per annum from 18-9-1990 up to the date of decree/payment and then even though the said payment was not made, awards damages to the contractor which works out to Rs 6,42,70,000 to the contractor. This to say the least is legal misconduct and an error apparent on the face of the award.

52. We may also refer to another aspect. A sum of Rs 12,072 per day was claimed as damages by the contractor in a two-line calculation without any supporting evidence or document. As noticed above, the claim was on the basis that the contractor would have manufactured 15 pipes per day of the value of Rs 1,20,000 and that the profit and overhead element out of it would have been 15% or Rs 18,000 per day. By taking the working days as 306 in a year and deducting 20% of labour component, the loss of profit per day was calculated to be Rs 12,072 per day. There is no evidence to show that the contractor was at any point of time manufacturing 15 pipes a day of the value of Rs 8000 each or that he would have made a profit of 15% on the cost thereof. The claim is made on the ground that it is disabled from manufacturing that many number of pipes elsewhere.

53. There is no evidence that the contractor had other contracts where it was required to manufacture that number of pipes or that it could not manufacture the required pipes for want of plant and machinery. Nor is there any evidence as to the value of the plant and machinery that had been mortgaged to the employer and what would be the cost of an alternative plant with a capacity to manufacture 15 pipes per day. If the plant and machinery was of the value of say Rs 25 lakhs, or if the contractor could install another similar plant at a cost of Rs 25 lakhs, then the loss at best would be interest on Rs 25 lakhs and not anything more.

54. In fact even though there is no evidence, while making Claims 36 and 37 the contractor has given value of the plant and machinery as Rs 36,84,161. Even assuming the said figure to be true, at best the blocked up investment was only Rs 36,84,161 and the loss would be around 1% thereon per month by way of interest which would be Rs 36,841 per month. What is more strange is nowhere in the award the arbitrator considers the validity of the claim of Rs 12,072 per day nor accepts the said claim as valid or correct. In a reasoned award if the claim of a contractor is equated to proof of the claim, then it is obviously a legal misconduct and an error apparent on the face of the award.

55. While the quantum of evidence required to accept a claim may be a matter within the exclusive jurisdiction of the arbitrator to decide, if there was no evidence at all and if the arbitrator makes an award of the amount claimed in the claim statement, merely on the basis of the claim statement without anything more, it has to be held that the award on that account would be invalid. Suffice it to say that the entire award under this head is wholly illegal and beyond the jurisdiction of the arbitrator, and wholly unsustainable.

56. Learned counsel for the contractor submitted that though there was an award in favour of the employer for refund of mobilisation advance of Rs 59,42,275 with interest, there was a larger award in its favour aggregating to about Rs 1.67 crores and interest and it was legitimately entitled to adjust the sum of Rs 59,42,275 with interest towards the amount due by the employer under the award, namely, Rs 1.67 crores with interest and therefore as on the date of the award the liability towards mobilisation advance stood wiped out on account of the same being adjusted towards the amount claimed by him and therefore as on the date of the award, the liability to refund the mobilisation advance ceased. This contention is not sound.

57. The mobilisation advance amount was an ascertained sum due to the employer from the contractor, with a specific provision for interest. There was a specific contract for continuation of the mortgage until the said amount was paid. On the other hand the amounts that allegedly became due to the contractor under the award were mostly towards damages and escalation in prices, validity of which were under challenge and there was no provision in the contract for payment of interest thereon. As noticed above, at best the arbitrator could have directed return of the documents of title to the

contractor and could not have directed payment of damages at the rate of Rs 12,072 per day.

58. We therefore hold that viewed from any angle, awarding Rs 12,072 per day as damages, from the date of award under Claim 37-A cannot be sustained and the same is liable to be set aside.

Re: Claims 12 and 13

59. The contractor claimed pre-reference interest at 18% per annum on all its claims from the date of the claim to the date of the arbitrator entering upon the reference (18-6-1990 to 15-12-1991), as also pendente lite interest from 16-12-1991 to 21-9-1994 and future interest from the date of award till the date of payment or decree, whichever was earlier. The arbitrator awarded the following interest:

(*a*) pre-reference interest on all sums awarded except Claim 1, from 3-9-1990 (date of the contractor's application under Sections 8 and 20 of the Act) to 15-12-1991 at 18% per annum;

(*b*) pendente lite interest on all sums awarded including Claim 1, from 16-12-1991 to 21-9-1994 at 18% per annum; and

(*c*) future interest on all sums awarded from 22-9-1994 till date of decree or payment, whichever is earlier, at the rate of 18% per annum.

The District Court did not award any post-decretal interest, but the High Court, however, granted interest from the date of decree till the date of payment at 18% per annum.

60. The appellants contend that there was no provision in the contract for payment of interest on any of the amounts payable to the contractor and therefore no interest ought to be awarded. But this Court has held that in the absence of an express bar, the arbitrator has the jurisdiction and authority to award interest for all the three periods—pre-reference, pendente lite and future (vide decisions of the Constitution Bench in *Irrigation Deptt., Govt. of Orissa* v. *G.C. Roy*[3], *Dhenkanal Minor Irrigation Division* v. *N.C. Budharaj*[4] and the subsequent decision in *Bhagawati Oxygen Ltd.* v. *Hindustan Copper Ltd.*[5]). In the present case as there was no express bar in the contract in regard to interest, the arbitrator could award interest.

61. The appellant next contended that in regard to the claims in the nature of damages, as contrasted from ascertained sums due, interest becomes payable only on quantification and therefore award of interest prior to the date of the arbitrator's award was illegal.

62. It is no doubt true that the position of law earlier was that in regard to award of damages, interest was not payable before quantification by a court. This was on the assumption that insofar as damages are concerned, there is no liability till determination of the quantum of damages. We may refer to a decision of the Bombay High Court in *Iron & Hardware (India) Co.* v. *Firm*

3 (1992) 1 SCC 508
4 (2001) 2 SCC 721
5 (2005) 6 SCC 462

Shamlal & Bros.[6], where Chagla, C.J., speaking for the Bench, stated the principle thus: (AIR pp. 425-26, para 7)

> "*7.* ... In my opinion it would not be true to say that a person who commits a breach of the contract incurs any pecuniary liability, nor would it be true to say that the other party to the contract who complains of the breach has any amount due to him from the other party.
>
> As already stated, the only right which he has is the right to go to a court of law and recover damages. Now, damages are the compensation which a court of law gives to a party for the injury which he has sustained. But, and this is most important to note, he does not get damages or compensation by reason of any existing obligation on the part of the person who has committed the breach. He gets compensation as a result of the fiat of the court. Therefore, no pecuniary liability arises till the court has determined that the party complaining of the breach is entitled to damages. Therefore, when damages are assessed, it would not be true to say that what the court is doing is ascertaining a pecuniary liability which already existed. The Court in the first place must decide that the defendant is liable and then it proceeds to assess what that liability is. But till that determination there is no liability at all upon the defendant."

63. The legal position, however, underwent a change after the enactment of the Interest Act, 1978. Sub-section (1) of Section 3 of the said Act provided that a court (as also an arbitrator) can in any proceedings for recovery of any debt or damages, if it thinks fit, allow interest to the person entitled to the debt or damages at a rate not exceeding the *current rate of interest*, for the whole or part of the following period, that is to say,—

> "3. (1)(*a*) if the proceedings relate to a debt payable by virtue of a written instrument at a certain time, then, from the date when the debt is payable to the date of institution of the proceedings;
>
> (*b*) if the proceedings do not relate to any such debt, then, from the date mentioned in this regard in a written notice given by the person entitled or the person making the claim to the person liable that interest will be claimed, to the date of institution of the proceedings:"

64. Sub-section (3) of Section 3 made it clear that nothing in that section shall apply to any debt or damages upon which interest is payable as of right, by virtue of any agreement; or to any debt or damages upon which payment of interest is barred, by virtue of an express agreement. The said sub-section also made it clear that nothing in that section shall empower the court to award interest upon interest. Section 5 of the said Act provides that nothing in the said Act shall affect the provisions of Section 34 of the Code of Civil Procedure, 1908.

65. The position regarding award of interest after the Interest Act, 1978 came into force, can be stated thus:

6 AIR 1954 Bom 423

(*a*) Where a provision has been made in any contract, for interest on any debt or damages, interest shall be paid in accordance with such contract.

(*b*) Where payment of interest on any debt or damages is expressly barred by the contract, no interest shall be awarded.

(*c*) Where there is no express bar in the contract and where there is also no provision for payment of interest then the principles of Section 3 of the Interest Act will apply in regard to the pre-suit or pre-reference period and consequently interest will be payable:

(*i*) where the proceedings relate to a debt (ascertained sum) payable by virtue of a written instrument at a certain time, then from the date when the debt is payable to the date of institution of the proceedings;

(*ii*) where the proceedings is for recovery of damages or for recovery of a debt which is not payable at a certain time, then from the date mentioned in a written notice given by the person making a claim to the person liable for the claim that interest will be claimed, to date of institution of proceedings.

(*d*) Payment of interest pendente lite (date of institution of proceedings to date of decree) and future interest (from the date of decree to date of payment) shall not be governed by the provisions of the Interest Act, 1978 but by the provisions of Section 34 of the Code of Civil Procedure, 1908 or the provisions of the law governing arbitration as the case may be.

66. Therefore, even in regard to the claims for damages, interest can be awarded for a (*sic* period) prior to the date of ascertainment or quantification thereof if (*a*) the contract specifically provides for such payment from the date provided in the contract; or (*b*) a written demand had been made for payment of interest on the amount claimed as damages before initiation of action, from the date mentioned in the notice of demand (that is from the date of demand or any future date mentioned therein). In regard to claims for ascertained sums due, interest will be due from the date when they became due. In the present case, interest has been awarded only from 3-9-1990, the date of the petition under Section 20 of the Act for appointment of arbitrator. We find no reason to alter the date of commencement of interest.

67. In regard to the rate of interest, we are of the view that the award of interest at 18% per annum, in an award governed by the old Act (the Arbitration Act, 1940), was an error apparent on the face of the award. In regard to award of interest governed by the Interest Act, 1978, the rate of interest could not exceed the *current rate of interest* which means the highest of the maximum rates at which interest may be paid on different classes of deposits by different classes of scheduled banks in accordance with the directions given or issued to banking companies generally by Reserve Bank of India under the Banking Regulation Act, 1949. Therefore, we are of the view that pre-reference interest should be only at the rate of 9% per annum. It is appropriate to award the same rate of interest even by way of pendente lite interest and future interest up to the date of payment.

Re: Claims 2 and 16, 3 and 15, 5 and 18, 6 and 17, 9 and 19, 11 and 20, 24, 27, and 28, 29, 30, 31, 32, 33, 35 (with 25 and 34) of the contractor

68. Claims 9 and 19, 27 and 28, 29, 33, 35 (with 25 and 35) are for payment for the work done by the contractor. Claims 2 and 16, 3 and 15, 5 and 18, 24, 30, 31 and 32 are for release/refund of amounts withheld or excess deductions. Claims 6 and 17 are for escalation in prices. Claims 11 and 20 are for compensation for slow progress due to reduction of width of trench. The arbitrator has awarded certain amounts against these claims by examining the material placed before him and the terms of contract. He has also assigned reasons for awarding the amount against these claims. Courts cannot sit in judgment over the award of the arbitrator, nor reappreciate the evidence.

69. The awards on these claims do not suffer from any infirmity which can be the basis for interference either under Section 30 or under Section 16 of the Arbitration Act, 1940. Neither want of jurisdiction, nor legal misconduct, nor any inconsistency nor error apparent on the face of the award are made out in regard to awards made in regard to these claims. The awards in regard to these claims are therefore upheld.

Re: Claims 4, 7, 8, 10 and 21, 14, 22, 23, 26, 38, 39, 40, 41 and 41-A, 42 and 42-A, 43 of the contractor

70. These claims of the contractor have been examined and rejected by the arbitrator and upheld by the courts below. No ground is made out to interfere with the same.

Re: Counterclaims of the employer

71. Out of the five counterclaims of the employer, the arbitrator has allowed only Counterclaim 3. Counterclaim 3 was for refund of mobilisation advance (Rs 79,87,846) with interest and the arbitrator has awarded Rs 59,42,275 with interest at the contract rate of 18% per annum up to the date of decree/payment, whichever was earlier. Counterclaims 1, 2, 4 and 5 made by the appellant against the contractor have been rejected. They are:

Counterclaim	*Brief description of counterclaim*	*Amount of counterclaim*
1.	Liquidated damages	Rs 99,19,460
2.	Extra cost in getting work completed through another agency	Rs 6,66,62,000
3.	* *	*
4.	Interest on payments made to the contractor and not utilised	Rs 2,17,42,168
5.	Costs	Rs 2,50,000

72. Counterclaims 1, 2 and 4 have been considered by the arbitrator and rejected by the arbitrator on the ground that the delays/breaches were on the

part of the appellant and therefore, the question of claiming these amounts does not arise. Rejection of Counterclaim 5 is consequential. As noticed above, the court does not sit in appeal over the award of the arbitrator and cannot reappreciate the evidence to arrive at a different conclusion. The award on these items does not attract any of the grounds on which the award could be set aside. Therefore, rejection of these claims is also not open to interference.

73. We therefore allow these appeals in part and modify the judgments of the courts below as indicated above. Resultantly:

(A) The award of the arbitrator on Claim 1 (Rs 33,06,500) and Claim 37-A (Rs 12,072 per day from 21-9-1994 till date of payment) is set aside.

(B) The award of the arbitrator on Claims 2 and 16, 3 and 15, 5 and 18, 6 and 17, 9 and 19, 11 and 20, 24, 27 and 28, 29, 30, 31, 32, 33, 35 (with 25 and 24) aggregating to Rs 1,34,24,407 is upheld.

(C) Interest shall be payable at 9% p.a. on Rs 1,34,24,407 from 3-9-1990 till date of payment. The award on Claims 12 and 13 is modified accordingly.

(D) Award of Rs 59,42,275 in respect of Counterclaim 3 of the appellant with interest at the rate of 18% per annum from the respective dates of release up to the date of payment is upheld.

(E) The direction for adjustment of the amount due under Counterclaim 3 calculated as on 21-9-1994, against the amounts found due to the contractor calculated as on 21-9-1994 is upheld. Consequently, the appellant shall release the title deeds deposited in regard to the plant/machinery of the contractor. The contractor will be entitled to remove the plant, if it is not already done.

(F) Rejection of Claims 4, 7, 8, 10 and 21, 14, 22, 23, 26, 38, 39, 40, 41 and 41-A, 42 and 42-A and 43 of the contractor and Counterclaims 1, 2, 4, and 5 of the employer is upheld.

(G) Parties to bear their respective costs.

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(BEFORE R.V. RAVEENDRAN AND P. SATHASIVAM, JJ.)

SAYEED AHMED AND COMPANY .. Appellant;

Versus

STATE OF UTTAR PRADESH AND OTHERS .. Respondents.

Civil Appeal No. 4197 of 2009†, decided on July 9, 2009

A. **Arbitration and Conciliation Act, 1996 — S. 31(7) — Interest — Express bar in contract against claim for interest — Arbitrator's power —**

† Arising out of SLP (C) No. 15980 of 2008. From the Judgment and Order dated 27-2-2008 of the High Court of Uttarakhand at Nainital in AO No. 457 of 2006