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PREME COURT OF INDIA

R Nariman, J., Vineet Saran, J.

Icomm Tele Ltd. v. Punjab State Water Supply And & Sewerage Board

CIVIL APPEAL NO. 2713 of 2019 (Arising out of SLP (Civil) No.3307 of 2018)

11 March, 2019

Arbitration – Deterring a party to an arbitration from invoking this alternative dispute resolution process by a pre-deposit of 10% would discourage arbitration, contrary to the object of de-clogging the Court system, and would render the arbitral process ineffective and expensive. [Para 27]

JUDGMENT

R.F. NARIMAN, J.

1. Leave granted.

2. In 2008, the Punjab State Water Supply & Sewerage Board, Bhatinda issued notice inviting tender for extension and augmentation of water supply, sewerage scheme, pumping station and sewerage treatment plant for various towns mentioned therein on a turnkey basis. On 25.9.2008, the appellant company, which is Signature Not Verified involved in civil/electrical works in India, was awarded the said Digitally signed by tender after having been found to be the best suited for the task. On 16.1.2009, a formal contract was entered into between the appellant and respondent No. 2. It may be mentioned that the notice inviting tender formed part and parcel of the formal agreement. Contained in the notice inviting tender is a detailed arbitration clause. In this matter, we are concerned with clause 25(viii) which is set out as follows:-

> "viii. It shall be an essential term of this contract that in order to avoid frivolous claims the party invoking arbitration shall specify the dispute based on facts and calculations stating the amount claimed under each claim and shall furnish a "deposit-at-call" for ten percent of the amount claimed, on a schedule bank in the name of the Arbitrator by his official designation who shall keep the amount in deposit till the announcement of the award. In the event of an award in favour of the claimant, the deposit shall be refunded to him in proportion to the amount awarded w.r.t the amount claimed and the balance, if any, shall be forfeited and paid to the other party."

3. The appellant had entered into similar contracts with respondent No. 2 which contained the same arbitration clause. It had therefore addressed letters to respondent No. 2 with regard to appointment of arbitrator in those matters and sought for waiving the 10% deposit fee. After having received no response, the appellant had filed a writ petition, being Civil Writ Petition No. 18917 of 2016, before the High Court of Punjab and Haryana. This writ petition was dismissed by a judgment dated 14.9.2016 stating that such tender condition can in no way be said to be arbitrary or unreasonable.

4. On 8.3.2017, the appellant approached the High Court of Punjab and Haryana challenging the validity of this part of the arbitration clause by filing Civil Writ Petition No. 4882 of 2017. The High Court in the impugned judgment merely followed its earlier judgment and dismissed this writ petition as well.

5. Learned counsel appearing on behalf of the appellant has argued that the arbitration clause contained in the tender condition amounts to a contract of adhesion, and since there is unfair bargaining strength between respondent No. 2 and the appellant, this clause ought

to be struck down following the judgment in Central Inland Water Transport Corpn. v. Brojo Nath Ganguly, (1986) 3 SCC 156. He has also argued that arbitration being an alternative dispute resolution process, a 10% deposit would amount to a clog on entering the aforesaid process. Further, claims may ultimately be found to be untenable but need not be frivolous. Also, frivolous claims can be compensated by heavy costs. Further, even in the event that the award is in favour of the claimant, what can be refunded to him is only in proportion to the amount awarded and the rest is to be forfeited. This would also be a further arbitrary and highhanded action on the part of respondent No. 2.

6. Learned counsel appearing on behalf of the respondents has argued that there is no infraction of Article 14 in the present case. It is clear that clause 25(viii) would apply to both the parties equally, and as this is so, the said sub-clause cannot be struck down as being discriminatory. Further, the principle contained in Central Inland Water Transport Corpn. (supra) cannot possibly be applied to commercial contracts. Also, in similar cases, this Court has not entertained this kind of a challenge.

7. Having heard learned counsel for both parties, it will be seen that the 10% "deposit-at-call" before a party can successfully invoke the arbitration clause is on the basis that this is in order to avoid frivolous claims. Clause 25(xv) is also material and is set out hereinbelow:

> "xv. No question relating to this contract shall be brought before any civil court without first invoking and completing the arbitration proceedings, if the issue is covered by the scope of arbitration under this contract.
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> The pending arbitration proceedings shall not disentitle the Engineer-in-charge to terminate the contract and to make alternate arrangements for completion of the works."

8. From this clause, it also becomes clear that arbitration is considered to be an alternative dispute resolution process and entry to the civil court is sought to be taken away if the disputes between the parties are covered by the arbitration clause.

9. It is well settled that the terms of an invitation to tender are not open to judicial scrutiny, as they are in the realm of contract, unless they are arbitrary, discriminatory, or actuated by malice. Thus, in Directorate of Education v. Educomp Datamatics Ltd., (2004) 4 SCC 19, this Court held:

> "9. It is well settled now that the courts can scrutinise the award of the contracts by the Government or its agencies in exercise of their powers of judicial review to prevent arbitrariness or favouritism. However, there are inherent limitations in the exercise of the power of judicial review in such matters. The point as to the extent of judicial review permissible in contractual matters while inviting bids by issuing tenders has been examined in depth by this Court in Tata Cellular v. Union of India [(1994) 6 SCC 651]. After examining the entire case-law the following principles have been deduced:
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> "94. The principles deducible from the above are:
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> (1) The modern trend points to judicial restraint in administrative action.
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> (2) The court does not sit as a court of appeal but merely reviews the manner in which the decision was made.
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> (3) The court does not have the expertise to correct the administrative decision. If a review of the administrative decision is permitted it will be substituting its own decision, without the necessary expertise which itself may be fallible.
>
> (4) The terms of the invitation to tender cannot be open to judicial scrutiny because the invitation to tender is in the realm of contract. Normally speaking, the decision to accept the tender or award the contract is reached by process of negotiations through several tiers. More often than not, such decisions are made qualitatively by experts.
>
> (5) The Government must have freedom of contract. In other words, a fair play in the joints is a necessary concomitant for an administrative body functioning in an administrative sphere or quasi-administrative sphere. However, the decision must

not only be tested by the application of Wednesbury principle of reasonableness (including its other facts pointed out above) but must be free from arbitrariness not affected by bias or actuated by mala fides.

(6) Quashing decisions may impose heavy administrative burden on the administration and lead to increased and unbudgeted expenditure."" (emphasis in original) "12. It has clearly been held in these decisions that the terms of the invitation to tender are not open to judicial scrutiny, the same being in the realm of contract. That the Government must have a free hand in setting the terms of the tender. It must have reasonable play in its joints as a necessary concomitant for an administrative body in an administrative sphere. The courts would interfere with the administrative policy decision only if it is arbitrary, discriminatory, mala fide or actuated by bias. It is entitled to pragmatic adjustments which may be called for by the particular circumstances. The courts cannot strike down the terms of the tender prescribed by the Government because it feels that some other terms in the tender would have been fair, wiser or logical. The courts can interfere only if the policy decision is arbitrary, discriminatory or mala fide."

10. To similar effect is the decision in Global Energy Ltd. v. Adani Exports Ltd., (2005) 4 SCC 435, where this Court held:

"10. The principle is, therefore, well settled that the terms of the invitation to tender are not open to judicial scrutiny and the courts cannot whittle down the terms of the tender as they are in the realm of contract unless they are wholly arbitrary, discriminatory or actuated by malice. This being the position of law, settled by a catena of decisions of this Court, it is rather surprising that the learned Single Judge passed an interim direction on the very first day of admission hearing of the writ petition and allowed the appellants to deposit the earnest money by furnishing a bank guarantee or a bankers' cheque till three days after the actual date of opening of the tender. The order of the learned Single Judge being wholly illegal, was, therefore, rightly set aside by the Division Bench."

11. As has correctly been argued by learned counsel appearing on behalf of the respondents, this court's judgment in Central Inland Water Transport Corpn. (supra), which lays down that contracts of adhesion, i.e., contracts in which there is unequal bargaining power, between private persons and the State are liable to be set aside on the ground that they are unconscionable, does not apply where both parties are businessmen and the contract is a commercial transaction (see paragraph 89 of the said judgment). In this view of the matter, the argument of the appellant based on this judgment must fail.

12. In S.K. Jain v. State of Haryana, (2009) 4 SCC 357, this Court dealt with an arbitration clause in an agreement which read as follows:-

"11. Sub-clause (7) of Clause 25-A of the agreement reads as follows:

"25-A. (7) It is also a term of this contract agreement that where the party invoking arbitration is the contractor, no reference for arbitration shall be maintainable unless the contractor furnishes to the satisfaction of the Executive Engineer in charge of the work, a security deposit of a sum determined according to details given below and the sum so deposited shall, on the termination of the arbitration proceedings be adjusted against the costs, if any, awarded by the arbitrator against the claimant party and the balance remaining after such adjustment in the absence of any such costs being awarded, the whole of the sum will be refunded to him within one month from the date of the award—

Amount of claim Rate of security deposit 1For claims below Rs 2% of amount . 10,000 claimed 2For claims of Rs 10,000 5% of amount . and above and below Rs claimed 1,00,000 and 3For claims of Rs 1,00,000 7% of amount . and above claimed."

13. In upholding such a clause, this Court referred to the judgment in Central Inland Water Transport Corpn. (supra) and distinguished this judgment, stating that the concept of unequal bargaining power has no application in the case of commercial contracts. It then went on to hold:-

"14. It has been submitted by learned counsel for the appellant that there

should be a cap in the quantum payable in terms of sub-clause (7) of Clause 25-A. This plea is clearly without substance. It is to be noted that it is structured on the basis of the quantum involved. Higher the claim, the higher is the amount of fee chargeable. There is a logic in it. It is the balancing factor to prevent frivolous and inflated claims. If the appellants' plea is accepted that there should be a cap in the figure, a claimant who is making higher claim stands on a better pedestal than one who makes a claim of a lesser amount."

14. It will be noticed that in this judgment there was no plea that the aforesaid condition contained in an arbitration clause was violative of Article 14 of the Constitution of India as such clause is arbitrary. The only pleas taken were that the ratio of Central Inland Water Transport Corpn. (supra) would apply and that there should be a cap in the quantum payable by way of security deposit, both of which pleas were turned down by this court. Also, the security deposit made would, on the termination of the arbitration proceedings, first be adjusted against costs if any awarded by the arbitrator against the claimant party, and the balance remaining after such adjustment then be refunded to the party making the deposit. This clause is materially different from clause 25(viii), which, as we have seen, makes it clear that in all cases the deposit is to be 10% of the amount claimed and that refund can only be in proportion to the amount awarded with respect to the amount claimed, the balance being forfeited and paid to the other party, even though that other party may have lost the case. This being so, this judgment is wholly distinguishable and does not apply at all to the facts of the present case.

15. In ABL International Ltd. v. Export Credit Guarantee Corpn. of India Ltd., (2004) 3 SCC 553, this Court has held that even within the contractual sphere, the requirement of Article 14 to act fairly, justly and reasonably by persons who are "state" authorities or instrumentalities continues. Thus, this Court held:

"23. It is clear from the above observations of this Court, once the State or an instrumentality of the State is a party of the contract, it has an obligation in law to act fairly, justly and reasonably which is the requirement of Article 14 of the Constitution of India. Therefore, if by the impugned repudiation of the claim of the appellants the first respondent as an instrumentality of the State has acted in contravention of the abovesaid requirement of Article 14, then we have no hesitation in holding that a writ court can issue suitable directions to set right the arbitrary actions of the first respondent... xxx xxx xxx

27. From the above discussion of ours, the following legal principles emerge as to the maintainability of a writ petition:

(a) In an appropriate case, a writ petition as against a State or an instrumentality of a State arising out of a contractual obligation is maintainable.

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53. From the above, it is clear that when an instrumentality of the State acts contrary to public good and public interest, unfairly, unjustly and unreasonably, in its contractual, constitutional or statutory obligations, it really acts contrary to the constitutional guarantee found in Article 14 of the Constitution..."

16. Thus, it must be seen as to whether the aforesaid clause 25(viii) can be said to be arbitrary or discriminatory and violative of Article 14 of the Constitution of India.

17. We agree with the learned counsel for the respondents that the aforesaid clause cannot be said to be discriminatory in that it applies equally to both respondent No. 2 and the appellant. However, arbitrariness is a separate and distinct facet of Article 14. In A.L. Kalra v. The Project & Equipment Corporation of India Limited, [1984] 3 S.C.R. 646, this Court turned down a submission that arbitrariness is only a facet of discrimination. The contention of Shri Lal Narain Sinha was recorded thus (at page 661):-

"It was urged that in the absence of any specific pleading pointing out whether any one else was either similarly situated as the appellant or dissimilarly treated the charge of discrimination cannot be entertained and no relief can be claimed on the allegation of contravention of Art. 14 or Art. 16 of the Constitution. It was submitted that the expression discrimination imports the concept of comparison between

equals and if the resultant inequality is pointed out in the treatment so meted out the charge of discrimination can be entertained and one can say that equal protection of law has been denied.

Expanding the submission, it was urged that the use of the expression 'equality' in Art. 14 imports duality and comparison which is predicated upon more than one person of situation and in the absence of available material for comparison, the plea of discrimination must fail. As a corollary, it was urged that in the absence of material for comparative evaluation not only the charge of discrimination cannot be sustained but the executive action cannot be struck down on the ground that the action is per se arbitrary."

18. This contention was negatived stating (at pages 662-663):-

"It thus appears well settled that Art. 14 strikes at arbitrariness in executive/administrative action because any action that is arbitrary must necessarily involve the negation of equality. One need not confine the denial of equality to a comparative evaluation between two persons to arrive at a conclusion of discriminatory treatment. An action per se arbitrary itself denies equal of protection by law. The Constitution Bench pertinently observed in Ajay Hasia's case [[1981] 2 S.C.R. 79] and put the matter beyond controversy when it said 'wherever therefore, there is arbitrariness in State action whether it be of the legislature or of the executive or of an "authority" under Article 12, Article 14 immediately springs into action and strikes down such State action.' This view was further elaborated and affirmed in D.S. Nakara v. Union of India [[1983] 1 SCC 305]. In Maneka Gandhi v. Union of India [[1978] 2 S.C.R. 621] it was observed that Art. 14 strikes at arbitrariness in State action and ensure fairness and equality of treatment. It is thus too late in the day to contend that an executive action shown to be arbitrary is not either judicially reviewable or within the reach of Article 14."

19. We have thus to see whether clause 25(viii) can be said to be arbitrary and violative of Article 14 of the Constitution of India.

20. The first important thing to notice is that the 10% "deposit-at- call" of the amount claimed is in order to avoid frivolous claims by the party invoking arbitration. It is well settled that a frivolous claim can be dismissed with exemplary costs. Thus, in Dnyandeo Sabaji Naik v. Pradnya Prakash Khadekar, (2017) 5 SCC 496, this Court held:

"14. Courts across the legal system—this Court not being an exception—are choked with litigation. Frivolous and groundless filings constitute a serious menace to the administration of justice. They consume time and clog the infrastructure. Productive resources which should be deployed in the handling of genuine causes are dissipated in attending to cases filed only to benefit from delay, by prolonging dead issues and pursuing worthless causes. No litigant can have a vested interest in delay. Unfortunately, as the present case exemplifies, the process of dispensing justice is misused by the unscrupulous to the detriment of the legitimate. The present case is an illustration of how a simple issue has occupied the time of the courts and of how successive applications have been filed to prolong the inevitable. The person in whose favour the balance of justice lies has in the process been left in the lurch by repeated attempts to revive a stale issue. This tendency can be curbed only if courts across the system adopt an institutional approach which penalises such behaviour.

Liberal access to justice does not mean access to chaos and indiscipline. A strong message must be conveyed that courts of justice will not be allowed to be disrupted by litigative strategies designed to profit from the delays of the law. Unless remedial action is taken by all courts here and now our society will breed a legal culture based on evasion instead of abidance. It is the duty of every court to firmly deal with such situations. The imposition of exemplary costs is a necessary instrument which has to be deployed to weed out, as well as to prevent the filing of frivolous cases. It is only then that the courts can set apart time to resolve genuine causes and answer the concerns of those who are in need of justice. Imposition of real time costs is also necessary to ensure that access to courts is available to citizens with genuine grievances. Otherwise, the doors would be shut to legitimate

> causes simply by the weight of undeserving cases which flood the system. Such a situation cannot be allowed to come to pass. Hence it is not merely a matter of discretion but a duty and obligation cast upon all courts to ensure that the legal system is not exploited by those who use the forms of the law to defeat or delay justice. We commend all courts to deal with frivolous filings in the same manner." (Emphasis supplied)

21. It is therefore always open to the party who has succeeded before the arbitrator to invoke this principle and it is open to the arbitrator to dismiss a claim as frivolous on imposition of exemplary costs.

22. We may also notice this Court's judgment in General Motors (I) (P) Ltd. v. Ashok Ramnik Lal Tolat, (2015) 1 SCC 429, that punitive damages follow when a court is approached with a frivolous litigation. This court held:-

"16. We proceed to deal with the issue of correctness of finding recorded by the National Commission for awarding punitive damages. Before doing so, we may notice that the respondent complainant appearing in person, in his written submissions has raised various questions, including the question that the appellant should be asked to account for the proceeds of the vehicles sold by it. Admittedly, the vehicle in question has been ordered to be handed back to the appellant against which the respondent complainant has no claim. Thus, the plea raised is without any merit. The other issue raised for further punitive damages of Rs. 100 crores and also damages for dragging him in this Court, merits no consideration being beyond the claim of the complainant in the complaint filed by him. Moreover, no litigant can be punished by way of punitive damages for merely approaching this Court, unless its case is found to be frivolous."

23. The important principle established by this case is that unless it is first found that the litigation that has been embarked upon is frivolous, exemplary costs or punitive damages do not follow. Clearly, therefore, a "deposit-at-call" of 10% of the amount claimed, which can amount to large sums of money, is obviously without any direct nexus to the filing of frivolous claims, as it applies to all claims (frivolous or otherwise) made at the very threshold. A 10% deposit has to be made before any determination that a claim made by the party invoking arbitration is frivolous. This is also one important aspect of the matter to be kept in mind in deciding that such a clause would be arbitrary in the sense of being something which would be unfair and unjust and which no reasonable man would agree to. Indeed, a claim may be dismissed but need not be frivolous, as is obvious from the fact that where three arbitrators are appointed, there have been known to be majority and minority awards, making it clear that there may be two possible or even plausible views which would indicate that the claim is dismissed or allowed on merits and not because it is frivolous. Further, even where a claim is found to be justified and correct, the amount that is deposited need not be refunded to the successful claimant. Take for example a claim based on a termination of a contract being illegal and consequent damages thereto. If the claim succeeds and the termination is set aside as being illegal and a damages claim of one crore is finally granted by the learned arbitrator at only ten lakhs, only one tenth of the deposit made will be liable to be returned to the successful party. The party who has lost in the arbitration proceedings will be entitled to forfeit nine tenths of the deposit made despite the fact that the aforesaid party has an award against it. This would render the entire clause wholly arbitrary, being not only excessive or disproportionate but leading to the wholly unjust result of a party who has lost an arbitration being entitled to forfeit such part of the deposit as falls proportionately short of the amount awarded as compared to what is claimed.

24. Further, it is also settled law that arbitration is an important alternative dispute resolution process which is to be encouraged because of high pendency of cases in courts and cost of litigation. Any requirement as to deposit would certainly amount to a clog on this process. Also, it is easy to visualize that often a deposit of 10% of a huge claim would be even greater than court fees that may be charged for filing a suit in a civil court. This Court in State of J&K v. Dev Dutt Pandit, (1999) 7 SCC 339, has held:-

> "23. Arbitration is considered to be an important alternative disputes redressal process which is to be encouraged because of high pendency of cases in the courts and cost of litigation. Arbitration has to be looked up to with all earnestness so that

the litigant public has faith in the speedy process of resolving their disputes by this process. What happened in the present case is certainly a paradoxical situation which should be avoided. Total contract is for Rs. 12,23,500. When the contractor has done less than 50% of the work the contract is terminated. He has been paid Rs 5,71,900. In a Section 20 petition he makes a claim of Rs. 39,47,000 and before the arbitrator the claim is inflated to Rs. 63,61,000. He gets away with Rs. 20,08,000 with interest at the rate of 10% per annum and penal interest at the rate of 18% per annum. Such type of arbitration becomes subject of witticism and do not help the institution of arbitration. Rather it brings a bad name to the arbitration process as a whole. When claims are inflated out of all proportions not only that heavy cost should be awarded to the other party but the party making such inflated claims should be deprived of the cost. We, therefore, set aside the award of cost of Rs. 7500 given in favour of the contractor and against the State of Jammu and Kashmir." (Emphasis supplied)

25. Several judgments of this Court have also reiterated that the primary object of arbitration is to reach a final disposal of disputes in a speedy, effective, inexpensive and expeditious manner. Thus, in Centrotrade Minerals & Metal Inc. v. Hindustan Copper Ltd., (2017) 2 SCC 228, this court held:

> "39. In Union of India v. U.P. State Bridge Corpn. Ltd. [(2015) 2 SCC 52] this Court accepted the view [O.P. Malhotra on the Law and Practice of Arbitration and Conciliation (3rd Edn. revised by Ms Indu Malhotra, Senior Advocate)] that the A&C Act has four foundational pillars and then observed in para 16 of the Report [sic] that:
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> "16. First and paramount principle of the first pillar is 'fair, speedy and inexpensive trial by an Arbitral Tribunal'. Unnecessary delay or expense would frustrate the very purpose of arbitration.
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> Interestingly, the second principle which is recognised in the Act is the party autonomy in the choice of procedure. This means that if a particular procedure is prescribed in the arbitration agreement which the parties have agreed to, that has to be generally resorted to."" (Emphasis in original)

26. Similarly, in Union of India v. Varindera Constructions Ltd., (2018) 7 SCC 794, this Court held:-

> "12. The primary object of the arbitration is to reach a final disposition in a speedy, effective, inexpensive and expeditious manner. In order to regulate the law regarding arbitration, legislature came up with legislation which is known as Arbitration and Conciliation Act, 1996. In order to make arbitration process more effective, the legislature restricted the role of courts in case where matter is subject to the arbitration. Section 5 of the Act specifically restricted the interference of the courts to some extent. In other words, it is only in exceptional circumstances, as provided by this Act, the court is entitled to intervene in the dispute which is the subject- matter of arbitration. Such intervention may be before, at or after the arbitration proceeding, as the case may be. In short, court shall not intervene with the subject-matter of arbitration unless injustice is caused to either of the parties."

27. Deterring a party to an arbitration from invoking this alternative dispute resolution process by a pre-deposit of 10% would discourage arbitration, contrary to the object of de-clogging the Court system, and would render the arbitral process ineffective and expensive.

28. For all these reasons, we strike down clause 25(viii) of the notice inviting tender. This clause being severable from the rest of clause 25 will not affect the remaining parts of clause 25. The judgment of the High Court is set aside and the appeal allowed.