

(1996) 03 BOM CK 0042
In the Bombay High Court
Case No : Arbitration Suit No. 4458 of 1995

Indian Oil Corporation Ltd.	Vs	APPELLANT
Raaj Unocal Lubricants Ltd.		RESPONDENT

Date of Decision : 26-03-1996

Acts Referred:

Arbitration Act, 1940 — Section 20
Contract Act, 1872 — Section 10, 19, 19A, 23

Citation : (1997) 1 BomCR 292 : (1997) 2 MhLj 281

Hon'ble Judges : S.M. Jhunjhunwala, J

Bench : Single Bench

Advocate : G.H. Vahanvati and P.H. Modi, instructed by Mulla and Mulla and Craigie and Blunt and Caroe, for the Appellant; K.L. Bhatt and R.J. Majra, instructed by Wadia Ghandy and Co., for the Respondent

Final Decision : Allowed

Judgement

S.M. Jhunjhunwala, J.—BY this application numbered and registered as suit under the provisions of section 20 of The Arbitration Act, 1940 (for short, "the Act") the plaintiff seeks to have the arbitration agreement filed in this Court and an order of reference to arbitration in accordance therewith.

2. The plaintiff carries on business inter alia of marketing lubricants produced by blending base oil with adhesives. The defendant owns an oil blending plant at village Jharsaintly, 40th road, Ballabgrah, Haryana (for short, "the said plant"). The plaintiff, being desirous of obtaining the services of oil blending facilities in Northern India on a contract basis, on 22nd February, 1994 entered into an agreement with the defendant for blending, packaging and loading of SERVO/I.O.C. brand lubricants at the said plant on the terms and conditions mentioned therein (for short, "the said Agreement"). The said agreement was executed at Bombay and Clause 34 thereof records an agreement by and between the plaintiff and the defendant to refer the disputes to arbitration as provided therein. The said Clause 34 reads as under:--

"34 Arbitration:

In case of any dispute or difference arising out of this contract, the matter shall be referred to the sole arbitration of an officer of the Corporation nominated by the Director (Marketing) of the Corporation whose decision will be final and binding on both the parties (Details as per Annexure-VI)"

Annexure (VI) mentioned in Clause 34 read as under:---

"ARBITRATION CLAUSE:

a) Any dispute or difference of any nature whatsoever any claim, cross-claim, counter-claim or set-off or regarding any right, liability, act, omission or account of any of the parties hereto arising out of or in relation to this agreement shall be referred to the sole arbitration of the Director (Marketing) of the Corporation who may either himself act as the arbitrator or nominate some other officer of the Corporation to act as the arbitrator. The contractor will not be entitled to raise any objection to any such arbitrator on the ground that the arbitrator is an officer of the Corporation.

b) In the event of the arbitrator to whom the matter is originally referred being transferred, he shall be entitled to continue the arbitration proceedings notwithstanding his transfer unless the Director (Marketing) at the time of such transfer or at any time thereafter, designates another person to act as arbitrator in his place in accordance with the terms of this agreement.

c) In the event of the arbitrator, to whom the matter is originally referred vacating his office or being unable or refusing to act for any reasons, the Director (Marketing) at the time of vacation of office or inability or refusal to act, shall designate another person to act as arbitrator in accordance with the terms of this agreement.

d) An arbitrator newly appointed by the Director (Marketing) under Clause (b) or under Clause (c) above shall be entitled to proceed with the reference from the point at which it was left by his predecessor.

e) It is an express term of this contract that no person other than the Director (Marketing) is a person nominated by such Director (Marketing) of the Corporation as aforesaid shall act as arbitrator hereunder. If for any reason Director (Marketing) is unable or unwilling or refuses or fails to act as arbitrator or nominate an arbitrator then the matter shall not be referred to arbitration at all.

f) The Award of the arbitrator so appointed shall be final, conclusive and binding on all parties to the agreement subject to the provisions of the Arbitration Act, 1940 or any statutory modification or re-enactment thereof and the rules made thereunder for the time being in force shall apply to the arbitration proceedings under this clause.

g) The Award shall be made in writing and published by the arbitrator within two

years after entering upon the reference or within such extended time not exceeding one further year as the parties shall by writing agreement. The parties hereto shall be deemed to have irrevocably given their consent to the arbitrator to make and publish the Award within the period referred to hereinabove and shall not be entitled to raise any objection or protest thereto under any circumstances whatsoever.

h) The arbitrator shall have power to order and direct either of the parties to abide by, observe and perform all such directions as the arbitrator may think fit having regard to the matters in difference i.e. dispute before him. The arbitrator shall have all summary powers and may take such evidence oral and/or documentary as the arbitrator in his absolute discretion thinks fit and shall be entitled to exercise all powers under the Indian Arbitration Act, 1974 including admission of any affidavit as evidence concerning the matter in difference i.e. dispute before him.

i) The parties against whom the arbitration proceedings have been initiated, that is to say, the respondents in the proceedings shall be entitled to prefer a cross-claim, counter-claim or set off before the arbitrator in respect of any matter in issue out of or in relation to the agreement without seeking a formal reference of arbitration in the Director (Marketing) for such counter-claim, cross-claim or set off and the arbitrator shall be entitled to consider and deal with the same as if the matters arising therefrom has been referred to him originally and deemed to form part of the reference made by the Director (Marketing).

j) The arbitrator shall be at liberty to appoint, if necessary, any accountant or engineer or other technical person to assist him and to act on the opinion taken from such person.

k) The arbitrator shall have power to make one or more Awards whether interim or otherwise in respect of the dispute and difference and in particular will be entitled to make separate Awards in respect of claims or cross-claims of the parties.

l) The arbitrator shall be entitled to direct any one of the parties to pay the costs of the other party in such manner and to such extent as the arbitrator may in his discretion determine and shall also be entitled to require one or both the parties to deposit funds in such proportion to meet the arbitrator's fees and expenses as and when called upon to do so."

3. Pursuant to Clause 9 of the said agreement, the defendant, on 22nd February, 1994 itself, also executed a Secrecy Agreement to ensure that plaintiff's proprietary information/technology would remain confidential and secret. The said plant was commissioned on 11th July, 1994. According to the plaintiff, from the very inception the functioning of the said plant was far from satisfactory and the defendant failed and neglected to comply with and/or committed breach of various terms and conditions of the said agreement. Correspondence ensued between the plaintiff and the defendant. Ultimately, by its advocates' letter

dated 22nd November 1995, the plaintiff terminated the said agreement with immediate effect and called upon the defendant to forthwith return to the plaintiff the stocks of base oil, adhesives, barrels, packing and other materials belonging to the plaintiff and lying with the defendant as also all documents provided by the plaintiff. Since the disputes and differences have arisen by and between the plaintiff and the defendant under or in respect of or relating to the said agreement, instead of proceeding under Chapter (II) of the Act, the plaintiff has filed the present application for filing the arbitration agreement in this Court and for order of reference to arbitration in accordance therewith. Both the learned Counsel have agreed that the parties hereto are governed by the provisions of the Act and not by the provisions of The Arbitration and Conciliation Ordinance, 1996 and as such, section 20 of the Act applies. Though in the affidavit filed in reply on behalf of the defendant it is contended that this Court has no jurisdiction to entertain and try this application of the plaintiff. Mr. Bhatt, the learned Counsel appearing for the defendant, has fairly conceded that the defendant is not raising the issue of jurisdiction of this Court.

4. Section 20 of the Act, relevant for deciding the controversy involved reads as under:-

"20. Application to file in Court arbitration agreement

1) Where any persons have entered into an arbitration agreement before the institution of any suit with respect to the subject matter of the agreement or any part of it, and where a difference has arisen to which the agreement applies, they or any of them, instead of proceeding under Chapter (II), may apply to a Court having jurisdiction in the matter to which the agreement relates, that the agreement be filed in Court.

2) The application shall be in writing and shall be numbered and registered as suit between one or more of the parties interested or claiming to be interested as plaintiff or plaintiffs and the remainder as defendant or defendants, if the application has been presented by all the parties, or if otherwise, between the applicant as plaintiff and the other parties as defendants.

3) On such application being made, the Court shall direct notice thereof to be given to all parties to the agreement other than the applicants, requiring them to show cause within the time specified in the notice why the agreement should not be filed.

4) Where no sufficient cause is shown, the Court shall order the agreement to be filed, and shall make an order of reference to the arbitrator appointed by the parties, whether in the agreement or otherwise, or where the parties cannot agree upon an arbitrator, to an arbitrator appointed by the Court.

5) Thereafter the arbitration shall proceed in accordance with, and shall be governed by the other provisions of this Act so far as they can be made applicable".

As per section 20, all or any of the parties to arbitration agreement may apply to have it filed in Court and a reference made to arbitration. However, there are certain essential conditions necessary to make this section applicable. They are-

- a) the parties must have entered into an arbitration agreement;
- b) the agreement must have been entered into before a suit with respect to its subject matter is filed in Court;
- c) a difference or dispute, contemplated in the agreement, must have arisen; and
- d) the Court had jurisdiction in the matter.

If these conditions are satisfied, the parties to the agreement may either avail of the procedure prescribed by Chapter (II) of the Act i.e. refer the dispute to arbitration without the intervention of the Court, or have the agreement filed in Court u/s 20 of the Act. Sub-section (2) to (4) lay down the procedure to be followed by Court, when an application is filed u/s 20 and sub-section (5) makes the provisions of the remaining sections of the Act applicable to proceedings u/s 20. The plaintiff has opted to have the arbitration agreement filed in this Court u/s 20 of the Act.

Besides the present application filed by the plaintiff, which is numbered and registered as suit under the provisions of section 20 of the Act, no other suit with regard to the subject matter of dispute between the plaintiff and the defendant has been filed in Court by either party. The correspondence ensued between the parties hereto prior to the filing of the present application amply establish that disputes or differences within the ambit and scope of the arbitration agreement contained in Clause 34 of the said agreement have arisen between the parties. This Court has jurisdiction in the matter. Hence, three out of the aforesaid four essential conditions necessary to make section 20 applicable are admittedly complied with. Though the fact of entering into the arbitration agreement as contained in Clause 34 of the said agreement has not been denied by the defendant, according to the defendant, the agreement being arbitrary and opposed to the principles to natural justice is illegal, invalid and bad in law and as such, cannot be enforced.

Mr. Bhatt has submitted that the plaintiff, being an instrumentality of the State, is a "State" within the meaning of Article 12 of the Constitution of India and even in the field of entering into contract the plaintiff, as an instrumentality of State, is neither to act arbitrarily nor in violation of the principles of natural justice. Mr. Bhatt has further submitted that the arbitration agreement as contained in Clause 34 of the said agreement is arbitrary and opposed to the principles of natural justice inasmuch as the sole arbitrator to be appointed has to be an officer of the plaintiff to be nominated by none other than the Director (Marketing) of the plaintiff. Mr. Bhatt has further submitted that since the plaintiff is made a judge in its own cause, such an arbitration is farce and violative of the principles of natural justice and the arbitration agreement as contained in Clause

34 of the said agreement read with Annexure VI thereto being wholly opposed to the letter and spirit of section 23 of the Indian Contract Act, 1872 is void and unenforceable. On merits of the claims of the plaintiff against the defendant, Mr. Bhatt has submitted that the plaintiff is not entitled to any claim from the defendant but is liable to pay the amount claimed by the defendant. It may be mentioned here that so far as the merits of the claims of the plaintiff against the defendant or of the defendant, against the plaintiff are concerned, in the present proceedings, it is neither necessary nor desirable to consider the same and as such, the same is not been considered.

5. In support of his submissions, Mr. Bhatt has put reliance on the judgments of the Supreme Court in the case of Central Coal Fields Ltd. and Another Vs. Jaiswal Coal Co. and Others, ; Central Inland Water Transport Corporation Limited and Another Vs. Brojo Nath Ganguly and Another, ; Kumari Srilekha Vidhyarthi & others v. State of U.P. & others, reported in 19941(1) S.C.C. 213; Gullapalli Nageswara Rao etc. Vs. The State of Andhra Pradesh and Others, ; Mineral Development Ltd. Vs. The State of Bihar and Another, ; Ranjit Thakur Vs. Union of India (UOI) and Others, and International Airports Authority of India Vs. K.D. Bali and Anr, . 1099. In the case of Central Coal Fields Ltd. & another, (supra), the Supreme Court has held that effective access to justice is the most basic requirement.

6. In the case of Central Inland Water Transport Corporation Ltd., (supra), the Supreme Court has held that unconscionable terms in contract are void u/s 23 of the Indian Contract Act, 1872 as also violative of Article 14 of the Constitution of India. In the case of Kumari Srilekha Vidhyarthi & others, (supra), the Supreme Court has held that State's actions are required to be non-arbitrary and justified on the touchstone of Article 14 of the Constitution of India. In the case of Gullappalli Nageswararao & others, (supra), the Supreme Court has held that the principles governing the doctrine of bias vis-a-vis judicial tribunals are well settled and they are: (i) no man shall be a Judge in his own cause; (ii) Justice should not only be done but manifestly and undoubtedly seem to be done. In the case of Mineral Development Ltd. (supra), the Supreme Court has held that the test to reasonableness, wherever prescribed, should be applied to each individual statute impugned, and no abstract standard, or general pattern of reasonableness can be laid down as applicable to all cases. In the case of Ranjit Thakur (supra), the Supreme Court has held that it is the essence of a judgment that it is made after due observance of the judicial process; that the Court or Tribunal passing it observes, at least the minimal requirements of natural justice is composed of impartial persons acting fairly and without bias and in good faith. A judgment which is the result of bias or want of impartiality is a nullity and the trial "Coram non judice". In the case of International Airport Authority of India, (supra), the Supreme Court has held that the purity of administration requires that the party to the proceedings should not have apprehension that the authority is biased and is likely to decide against the party. But it is not easy suspicion felt by a party which must lead to the conclusion that the authority

hearing the proceeding is biased. The apprehension must be judged from a wealthy, reasonable and average point of view and not on mere apprehension of any whimsical person.

7. There is not and there cannot be any dispute as regards the principles laid down by the Supreme Court in the context of facts involved in above referred decisions. However, the nature of the said agreement entered by and between the plaintiff and the defendant and the applicability of the said principles thereto are required to be considered. The said agreement constitutes a "commercial contract" between the plaintiff and the defendant. There is nothing to show and in the facts of the case it cannot be said that the terms of the contract were imposed by the plaintiff upon the defendant. There is nothing to show that at the time of entering into the contract the plaintiff and the defendant were not equal or almost equal in bargaining power. The terms of the contract mutually agreed by and between the plaintiff and the defendant as contained in the said agreement executed on 22nd February 1994 are usually contained in a commercial contract of the nature entered by and between the plaintiff and the defendant.

8. u/s 19 of the Indian Contract Act, when consent to an agreement is caused by coercion, fraud or misrepresentation, the agreement is a contract voidable at the option of the party whose consent was so caused. It is not the case of the defendant that there was any coercion brought to bear upon it or that any fraud or misrepresentation has been practised upon it. u/s 19-A, when consent to an agreement is caused by undue influence, the agreement is a contract voidable at the option of the party whose consent was so caused and the Court may set aside any such contract. Section 23 states that the consideration or object of an agreement is lawful unless inter alia the Court regards it as opposed to public policy. It further provides that every agreement of which the object or consideration is unlawful is void. It is not a case where object or consideration of the said agreement can be said to be unlawful. Though expression "public policy" has not been defined by the Indian Contract Act, it connotes some matter which concerns the public good and the public interest. Applying the test, the said agreement cannot be said to be "opposed to public policy" or "contrary to public policy". An unconscionable bargain would be one which is irreconcilable with what is right or reasonable. In the facts of the case, the said agreement cannot be considered as unconscionable bargain".

9. There is no doubt that under the arbitration agreement incorporated in the said agreement the Director (Marketing) of the plaintiff is to appoint the sole arbitrator who is to be an officer of the plaintiff. However, the fact remains that knowing the nature and contents of the said arbitration agreement, the plaintiff and the defendant voluntarily and with mutual consent entered into the same. It is not the case of the defendant that the defendant had not read the contents of the said arbitration agreement or had not understood the implications thereof prior to execution of the said agreement. When the defendant had knowingly and

of its free will and consent agreed to constitution of domestic tribunal by the Director (Marketing) of the plaintiff from amongst officers of the plaintiff for adjudication of disputes arising out of the said agreement or reference to arbitration being made, it is no more open for the defendant now to contend that the said arbitration agreement is bad or enforceable unless the defendant establishes a case of bias and not mere apprehension of bias. No case of bias has been established by the defendant except alleging that Director (Marketing) of the plaintiff is to nominate an officer of the plaintiff to act as sole arbitrator, such officer may have a bias against the defendant. As held by the Supreme Court in the case of International Airport Authority of India, (supra), it is not every suspicion felt by a party which must lead to the conclusion that the authority hearing the proceedings is biased. The apprehension must be judged from a healthy, reasonable and average point of view and not on mere apprehension of any whimsical person. In most of such contracts entered by Corporations constituting "State" within the meaning of Article 12 of the Constitution of India, such arbitration agreements are incorporated and the experience shows that the arbitrator/s so nominated had/have conducted the arbitration proceedings fairly and in impartial manner. As held by the Supreme Court in case of Bareilly Development Authority and Another Vs. Ajay Pal Singh and Others, , on which reliance has been placed by Mr. Vahanvati, the learned Counsel appearing for the plaintiff, when the contract entered into by the State is non-statutory and purely contractual, the relations are no longer governed by the constitutional provisions but by the legally valid contract which determines the rights and obligations of the parties inter se.

10. Mr. Vahanvati has submitted that the arbitration agreement incorporated in the said agreement is valid, legal and enforceable in law and merely because the Director (Marketing) of the plaintiff has been empowered to nominate an officer of the plaintiff to act as sole arbitrator, it cannot be said to be illegal, invalid or unenforceable in law. In support of his submission, Mr. Vahanvati has put reliance on the judgment in the case of M/s Mc. Kenzies Ltd. v. M/s Sulleman & Company, reported in AIR 1933 Sind 75 where it had been held that the fact that the Chief Engineer of one of the parties to the contract, who was nominated as arbitrator in the contract, had a duty to which the works in respect of which contract was given and might already have formed an opinion upon matters in dispute is not enough, in the absence of any evidence that he would not act fairly, to prevent him from being the proper person to decide the dispute. This judgment has stood the test of time. In the case of J. Chamber of Commerce v. Amrit Shah, reported in AIR 1940 Lah 180 on which reliance has been placed by Mr. Vahanvati, an application for stay of the suit in view of existence of arbitration agreement was opposed on the ground that the directors of the defendant company who had to be the arbitrators under the submission clause had personal and private interest in the subject matter of the suit and therefore were not fit persons to act as arbitrators. The learned Counsel appearing for the defendant Company in that case made the statement to the Court that the defendant company would not

object to the interested directors being excluded to act as arbitrators. The Court held that the fact that the arbitrators had to be chosen from the directors of the defendant company was perfectly legal. Even in the case of *President of India v. Kesar Singh*, reported in AIR 1966 J&k 113, on which also reliance has been placed by Mr. Vahanvati, the agreement gave the power to the Chief Engineer to appoint anybody as the arbitrator. The Chief Engineer exercised the option without consultation with the contractor. It was held that where the arbitration agreement gives power to one party to appoint anybody as arbitrator, the other party need not be consulted before any person is appointed arbitrator and the fact that the arbitrator is a servant of that party cannot vitiate proceedings.

11. In the case of *Indian Oil Corporation Ltd. v. Kesar Singh Mohan Singh*, reported in 1984 Mh.L.J. 903, the relevant portion of the arbitration clause contained in the agreement between the parties reads as under:---

"Any dispute or difference of any nature whatsoever or regarding any right, liability, act, omission or account of any of the parties hereto arising out of or in relation to this agreement shall be referred to the sole arbitration of the Managing Director of the Corporation or of some officer of the Corporation, who may be nominated by the Managing Director. The dealer will not be entitled to raise any objection to any such arbitrator on the ground that the arbitrator is an officer of the Corporation or that he has to deal with the matters to which the contract relates or that in the course of his duties as an officer of the Corporation he had expressed view on all or any other matters in dispute of difference....It is also a term of this contract that no person other than the Managing Director or a person nominated by such Managing Director of the Corporation as aforesaid shall act as arbitrator hereunder...."

The arbitration agreement provided that any dispute or difference of any nature whatsoever could be referred to a sole arbitrator who was to be an officer functioning with one of the parties thereto. This Court held that merely because an arbitrator was one of the officers with one of the parties to the dispute that did not affect the validity of the decision of the dispute by such person.

12. In the facts of the case, merely because the plaintiff as instrumentality of State is "State" within the meaning of Article 12 of the Constitution of India and under the agreement power is vested with the Director (Marketing) of the plaintiff to nominate an officer of the plaintiff as sole arbitrator for adjudication of any dispute or difference arising out of the said agreement, in my view, the arbitration agreement is neither arbitrary nor opposed to the principles of natural justice nor illegal nor invalid nor unenforceable in law nor opposed to public policy nor the arbitrator to be said to be biased. Though in the matter of arbitration persons who command mutual confidence of both sides should act as arbitrators, when a party agrees to the acting of an employee of the other party as arbitrator it has to be taken that the former fully understanding the implication thereof displayed confidence in such arbitrator. It cannot later turn round and seek setting at nought such mutually agreed arbitration agreement. I

hold the arbitration agreement incorporated in the said agreement in terms of Clause 34 as valid, legal, enforceable in law and binding on the parties thereto.

13. In the circumstances, the fourth essential condition necessary to make section 20 of the Act applicable also being complied with, the suit is decreed in terms of prayers (a) and (b). The Director (Marketing) of the plaintiff is directed to appoint arbitrator in accordance with the arbitration agreement within four weeks from today. In the event of arbitrator not being appointed within the period of four weeks from today either party is at liberty to apply to this Court for appointment of arbitrator without filing fresh petition and merely on precipe. There shall, however, be no order as to costs of the suit.