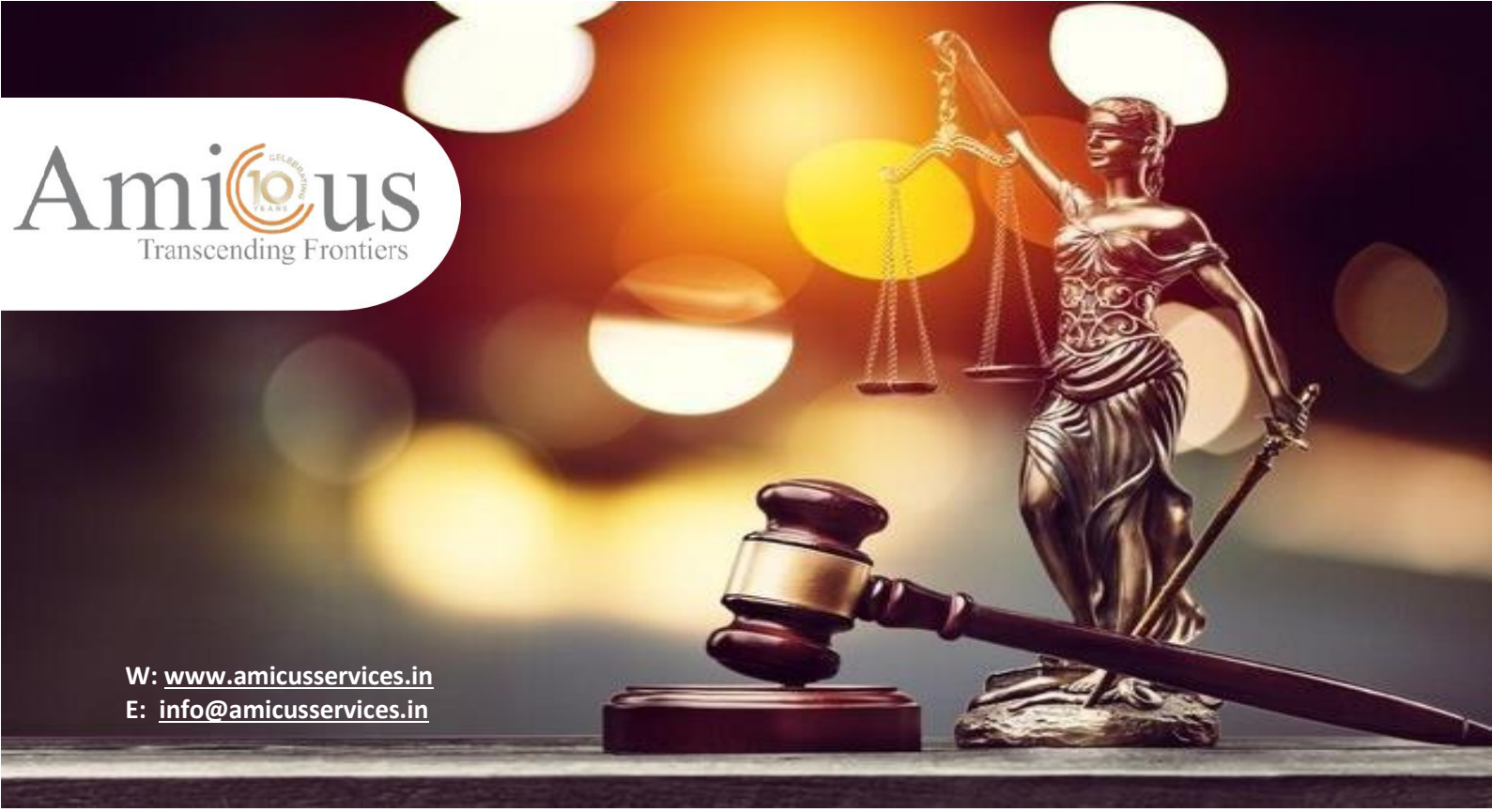

APPROPRIATE STAGE TO CHALLENGE UNILATERAL APPOINTMENT OF A SOLE ARBITRATOR

01 March 2022

On 8 November 2021, in the case of *M/s Kanodia Infratech Limited v. M/s Dalmia Cement (Bharat) Limited*[1], the Single Bench of the Hon'ble High Court of Delhi ("**High Court**") held that unilateral appointment of a sole arbitrator by a party is not open to challenge under Section 34 of the Arbitration and Conciliation Act, 1996 ("**the Act**") after an arbitral award has been passed, where such challenge was not made during the course of arbitration proceedings.

Facts

M/s Kanodia Infratech Limited ("**Kanodia**") entered into multiple agreements with M/s Dalmia Cement (Bharat) Limited ("**Dalmia**") for use and subsequent purchase of a cement manufacturing plant owned by Dalmia. Certain disputes arose between the parties and the agreements between them were terminated. Dalmia sought certain monetary claims which were rejected by Kanodia. Hence, Dalmia invoked arbitration on 10.10.2018. In accordance with the terms of the arbitration clause, Dalmia unilaterally appointed a sole arbitrator for adjudication of disputes who then passed the final award on 09.03.2021 ("**Award**") in favour of Dalmia. During the arbitral process, Kanodia did not challenge the unilateral appointment of the sole arbitrator by Dalmia.

[1] OMP (COMM) 297/2021

High Court Proceedings

It was only after conclusion of the arbitral proceedings, that Kanodia assailed the Award by primarily placing reliance on *Perkins Eastman Architects DPC & Anr. Vs HSCC (India) Ltd.*[2] ("**Perkins Eastman**") and *TRF Limited v. Energo Engineering Projects Limited*[3] ("**TRF Limited**"), wherein it was held that a party who has interest in the outcome or the decision of the dispute must not have the power to appoint a sole arbitrator. Kanodia submitted that the sole arbitrator lacked inherent jurisdiction to entertain and try the disputes as unilateral appointment of the sole arbitrator by Dalmia was contrary to the law settled by Perkins Eastman and TRF Limited. These submissions were countered by Dalmia. They argued that having submitted to the jurisdiction of the arbitrator and actively participated in the arbitration proceedings, Kanodia could not now impugn the Award for the reason that the appointment of the sole arbitrator was made unilaterally, more so at a post-arbitral stage under Section 34 of the Act, when such objection was never raised during the course of the arbitration proceedings.

High Court Decision

Although the Award was partly modified by the High Court on certain other grounds, Kanodia's plea with respect to the unilateral appointment of the arbitrator was rejected. The High Court opined that the facts under both Perkins Eastman and TRF Limited were distinct from the present case as in those cases, the challenge to the unilateral appointment was made at a Section 11 stage, i.e., at the stage of appointment of an arbitrator. Whereas, the present case was a petition under Section 34[4] of the Act. Accepting Dalmia's submissions, the High

[2] AIR 2020 SC 59

[3] AIR 2017 SC 3889

[4] *"34. Application for setting aside arbitral awards.–*
(1) Recourse to a Court against an arbitral award may be made only by an application for setting aside such award in accordance with sub-section (2) and sub-section (3).
(2) An arbitral award may be set aside by the Court only if –
(a) the party making the application 1[establishes on the basis of the record of the arbitral tribunal that] –
(i) a party was under some incapacity, or
(ii) the arbitration agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law for the time being in force; or
(iii) the party making the application was not given proper notice of the appointment of an arbitrator or of the arbitral proceedings or was otherwise unable to present his case; or
(iv) the arbitral award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration:
Provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, only that part of the arbitral award which contains decisions on matters not submitted to arbitration may be set aside; or
(v) the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties, unless such agreement was in conflict with a provision of this Part from which the parties cannot derogate, or, failing such agreement, was not in accordance with this Part; or
(b) the Court finds that--
(i) the subject-matter of the dispute is not capable of settlement by arbitration under the law for the time being in force, or
(ii) the arbitral award is in conflict with the public policy of India.
1[Explanation 1. – For the avoidance of any doubt, it is clarified that an award is in conflict with the public policy of India, only if, –
(i) the making of the award was induced or affected by fraud or corruption or was in violation of section 75 or section 81; or
(ii) it is in contravention with the fundamental policy of Indian law; or
(iii) it is in conflict with the most basic notions of morality or justice.

Court observed that permissible grounds of interference with an arbitral award were prescribed under Section 34 and unilateral appointment of an arbitrator was not one such ground available to a party to seek the relief of setting aside of an arbitral award. The High Court observed that the scope of interference by the courts while considering a petition under Section 34 of the Act is limited and demands interference only when the arbitrator has acted beyond the scope of the contract/agreement or exceeded the jurisdiction which has not taken place in the present case. The High Court rejected Kanodia's challenge to the unilateral appointment for the reason that it was raised at a belated stage after pronouncement of the Award. The High Court observed that the ratios of Perkins Eastman and TRF Limited could not be applied to petitions under Section 34 of the Act as the grounds available under this provision to set aside an arbitral award were limited and exhaustive, and unilateral appointment of an arbitrator by a party was not a ground available under Section 34 for setting aside the Award.

Analysis & Conclusion

The decision of the High Court rejecting Kanodia's challenge to the jurisdiction of the sole arbitrator is erroneous. Primarily, from a joint reading of the judgments in TRF Limited and Perkins Eastman and Section 12(5) read with the Seventh Schedule[5] , of the Act, it emerges that where a party has a direct interest in the dispute, such party cannot act as an arbitrator or unilaterally appoint the arbitrator without the consensus of the other contracting party. For ease of reference, Section 12(5) of the Act is reproduced below –

> *"12. Grounds for challenge.—*
>
> *XXX*
>
> *(5) Notwithstanding any prior agreement to the contrary, any person whose relationship, with the parties or counsel or the subject-matter of the dispute, falls under any of the categories specified in the Seventh Schedule shall be ineligible to be appointed as an arbitrator:*
>
> *Provided that parties may, subsequent to disputes having arisen between them, waive the applicability of this sub-section by an express agreement in writing."*

In TRF Limited and Perkins Eastman, the Supreme Court was cognizant of the risks that a unilateral appointment of an arbitrator could pose insofar as bias by such arbitrator inasmuch as this arbitrator could have an interest in

Explanation 2. – For the avoidance of doubt, the test as to whether there is a contravention with the fundamental policy of Indian law shall not entail a review on the merits of the dispute.]

2[(2A) An arbitral award arising out of arbitrations other than international commercial arbitrations, may also be set aside by the Court, if the Court finds that the award is vitiated by patent illegality appearing on the face of the award:

Provided that an award shall not be set aside merely on the ground of an erroneous application of the law or by reappreciation of evidence.]"

[5] List detailing arbitrator's relationship with the parties or counsel; arbitrator's relationship to the dispute; arbitrator's relationship direct or indirect interest in the dispute.

the result of the arbitration and invariably determine the course of the arbitration proceedings. This in turn, would make the appointment susceptible to challenge on grounds of independence and impartiality. This principle is an extension of Section 12(5) which was introduced in the Act to ensure neutrality of the arbitrator and fairness in arbitration proceedings.

Although, the proviso to Section 12(5) carves out an exception to the rule but in *Bharat Broadband Network Limited v. United Telecoms Limited*[6] ("**Bharat Broadband**"), the Supreme Court has clarified that this proviso is applicable only in certain exceptional situations which arise in family arbitrations or other arbitrations where a person subjectively commands blind faith and trust of the parties to the dispute, despite the existence of objective justifiable doubts regarding his independence and impartiality. Therefore, it would not be incorrect to say that in a commercial arbitration such as the one between Kanodia and Dalmia, unilateral appointment of the arbitrator by a party is out of question as the objectivity of the arbitrator is placed at a higher pedestal than party autonomy in arbitration proceedings.

In Perkins Eastman, the Supreme Court was of the view that if 'interest that the arbitrator would be said to be having in the outcome or result of the dispute' forms the test to determine the validity of his appointment, the possibility of bias would be present in all cases of unilateral appointment of an arbitrator. While observing so, the Supreme Court was conscious of the repercussions its decision would have on all similarly worded arbitration agreements as a party to the agreement would be disentitled to appoint the sole arbitrator. Notwithstanding such repercussions, the Supreme Court held that any person with an interest in the outcome of the dispute must not have the power to appoint a sole arbitrator. This establishes that the Supreme Court's decision in Perkins Eastman was to render all such arbitration agreements invalid which allowed one party to the contract to unilaterally appoint a sole arbitrator in order to eliminate the possibility of justifiable doubts regarding the neutrality and fairness of the arbitrator. Hence, the arbitration agreement between Kanodia and Dalmia that provided for appointment of the arbitrator by Dalmia, ought to have been declared void and non-enforceable.

In Bharat Broadband, the Supreme Court held that the appointment of an arbitrator is rendered *de jure* ineligible where the person so appointed is hit by one or the other conditions under Section 12(5) of the Act. This position is set in stone and is sacrosanct to the extent that party autonomy cannot disturb the position. Therefore, where a person appointed as an arbitrator is, (a) related either to one of the parties, or; (b) related to their counsel, or; (c) related to the subject matter of the dispute, such appointment shall be hit by the rigours of Section 12(5) and acquiescence by a party shall not regularize such appointment. The Court also observed that where any arbitrator

[6] AIR 2019 SC 2434

has become *de jure* ineligible to perform their functions due to applicability of Section 12(5), such arbitrator would not even be competent to rule on its own jurisdiction under Section 16 of the Act.

Further, the Supreme Court has also laid down that where the appointment of an arbitrator, unilateral or not, is redundant and such an arbitrator is no longer capacitated to perform the duties and functions of an arbitrator, the appointment of such arbitrator becomes *de jure* ineligible and their mandate stands terminated by virtue of Section 14(1)(a) of the Act. Therefore, the Award passed in the present case cannot be said to be valid in law as it was passed by an arbitrator whose mandate stood automatically terminated from the date of commencement of the arbitration by virtue of Section 14(1)(a) of the Act irrespective of the fact whether any party had raised such concerns or not.

Besides the aforesaid, the High Court decision as well as the Award passed by the arbitrator is violative of the fundamental policy of India because it completely ignores the law laid down by Supreme Court in Perkins Eastman, which states that unilateral appointment of a sole arbitrator is invalid in law. It is a well settled position that the law laid down by superior courts cannot be disregarded[7] irrespective of whether such objection was taken during the course of arbitration proceeding or not.

Considering the Kanodia-Dalmia arbitration was invoked before the ratio in Perkins Eastman was laid down by the Supreme Court, it does not take away from the fact that the independence and impartiality of the arbitrator is the essence of any arbitration proceeding. In TRF Limited, the Supreme Court has clearly pointed out that the element of invalidity to act or appoint an arbitrator is directly related to the interest a person would have in the outcome of the proceedings. Therefore, it held that a person having interest in the dispute or decision thereof must not be eligible to act as an arbitrator and that such person cannot and should not have any role in charting out any course to the dispute resolution by having the power to appoint an arbitrator.

By simple deduction and application of the ratio of TRF Limited, it would not be wrong to state that where any individual associated with Dalmia itself was not eligible to act as an arbitrator, it could not have appointed an arbitrator as well. Thus, in both a pre-Perkins Eastman and a post-Perkins Eastman scenario, the Award contradicted the provisions of the Act inasmuch as the appointment of the arbitrator became *de jure* ineligible from the date of commencement of the arbitration and the mandate of the arbitrator stood terminated. In view of the aforesaid, the challenge to the Award was squarely governed by Section 34(2)(b)(ii) of the Act.

[7] Renusagar Power Co. Ltd. v. General Electric Co AIR 1994 SC 860

Lastly, there is nothing to preclude a party from raising an objection regarding jurisdiction of an arbitrator under Section 34 of the Act post pronouncement of an arbitral award, even if no such objection was raised under Section 16[8] Therefore, under law, it was open to Kanodia to assail the Award on the grounds of jurisdiction even if it is not one of the prescribed grounds of challenge to an arbitral award under Section 34 of the Act and the Court could have interfered with the Award as the arbitrator never had the appropriate jurisdiction to adjudicate the Kanodia-Dalmia arbitration.

Basis the provisions of the Act and various precedents laid down by the Supreme Court, in our view, unilateral appointment of a sole arbitrator can be challenge at the stage of Section 34 of the Act and the decision of the High Court in the present case requires reconsideration.

Present Status

It so appears that the Division Bench of the High Court may be of the same opinion as the order of the Single Bench of the High Court, i.e., 8 November 2021, is being reevaluated in the appeal titled *M/s Kanodia Infratech Limited v. M/s Dalmia Cement (Bharat) Limited*[9] under Section 37 of the Act. This appeal was last heard on 28 February 2022 where the parties have been directed to file written submissions before the High Court and the matter will now come up on 7 September 2022. It will be interesting to see how the Division Bench addresses the issue of unilateral appointment of a sole arbitrator.

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[8] Lion Engineering Consultants v. State of Madhya Pradesh AIR 2018 SC 1895
[9] FAO(OS) (COMM.) 163/20210