

# Dispute Resolution Hotline

December 22, 2014

## SUPREME COURT: ARBITRATORS CAN AWARD POST AWARD INTEREST ON INTEREST PENDENTE LITE

The Supreme Court has:

- Held that post-award interest under **Section 31(7)(b)** of the Arbitration and Conciliation Act, 1996 would also be awarded on the amount of interest *pendente lite*, if any, and not merely on the principal sum
- Interpreted the word 'sum' used in **Section 31(7)**, sub-clauses (a) and (b) of the Act to be an amount of money that could include principal or interest or both.
- The Supreme Court's judgment in *State of Haryana and Others vs S.L. Arora & Co.* was pronounced as incorrect and overruled

### INTRODUCTION

In its recent judgment of *M/s Hyder Consulting (UK) Ltd v. Governor State Of Orissa through Chief Engineer*, the Supreme Court has considered the much debated question of whether post-award interest can be awarded by an arbitral tribunal on *pendente lite* interest under **Section 31(7)** of the Arbitration and Conciliation Act, 1996 ("Act"). The majority decision has held in the affirmative.

### FACTS

An arbitral award of Rs.2,30,59,802 was made in favour of the appellant. During execution proceedings, the District Judge ordered payment of Rs.8,92,15,993 taking into account interest payable on the principal amount and the interest *pendente lite* thereon for the calculation of post award interest.

The High Court of Orissa, quashed the order of the District Judge on the basis of the judgment of the Supreme Court in the case of *State of Haryana v. SL Arora and Co.*<sup>1</sup> ("**SL Arora Case**") which stated that "interest on interest" in the post award phase could not be awarded. This order was set aside by the High Court of Orissa and the District Judge was instructed to calculate the total amount payable without considering interest on interest *pendente lite*.

The High Court's order was appealed in the Supreme Court.

### ISSUE

- Whether, under **Section 31(7)** of the Act, interest *pendente lite* is included within the "sum" payable as per the arbitral award, for the purposes of awarding post-award interest.
- Whether the judgment in the *SL Arora Case* contained any infirmity, *inter alia*, in its interpretation of the *McDermott*<sup>2</sup> and the *Three Circles*<sup>3</sup> cases.

### JUDGMENT

#### Majority Decision (A Bobde and AM Sapre J.J)

Contrary to the view taken by the Hon'ble CJI, the majority decision disagreed with the judgment in the *SL Arora Case* whereby it had been held that unless stated in the contract, the tribunal did not have the power to provide for interest on pre-award interest. The Hon'ble Court stated that post award interest, as prescribed under **Section 31(7)(a)** of the Act, would also be applicable to the interest *pendente lite* and not merely the principal amount awarded by an arbitral tribunal.

In this regard, the Hon'ble Court reasoned and held as follows:

- **Section 31(7)(a)** of the Act contemplated that the term "sum" would include interest for the pre-award period on the entire sum awarded by an Arbitral Tribunal. Only if no interest is awarded would "sum" comprise only the principal. This was evident from the language of **Section 31(7)(a)** of the Act which stated that "...the arbitral tribunal may include in the sum for which the award is made interest..." The Court, thus, concluded that this line in the Act itself suggested that the term "sum" could include interest.
- On a comparison with **Section 34** of the Code of Civil Procedure, 1908 ("**CPC**") (which concerned interest in civil suits), the language of **Section 31(7)** of the Act was different and evidently intended to have a different effect.
- It was held that since **Section 34** of CPC empowered the Court to award interest "on the principal sum" and not merely the "sum" as provided under **Section 31(7)** of the Act. Thus, clearly the ambit of **Section 31(7)** of the Act was to include the pre-award interest awarded along with the principal sum. Had that not been the case **Section 31(7)** of the Act would have the same language as the **Section 34** of the CPC.

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- At the post-award stage the “sum directed to be paid by an arbitral tribunal” would include interest, as elucidated above. Thus, any post award interest being granted by the tribunal under **Section 31(7)(b)** of the Act is only on the “sum directed to be paid by an arbitral tribunal” and not on any amount referred to as “interest”. Thus, usage of the term “interest on interest” seems inaccurate.
- The purpose of enacting the provision under **Section 31(7)** was to encourage early payment of the awarded sum. Thus, “sum” could be interpreted to include interest, in line with the purpose of the provision.

### Minority Dissenting Judgment (HL Dattu, CJI)

The Hon'ble Judge considered the decision of the Supreme Court in the *SL Arora Case* and found it to be correct.

The Hon'ble Judge considered the following rationale under the *SL Arora Case*:

- The use of the words “*where and insofar as an arbitral award is for the payment of money*” and use of the words “*the Arbitral Tribunal may include in the sum for which the award is made, interest... on the whole or any part of the money*” in Clause (a) and use of the words “*a sum directed to be paid by an arbitral award shall... carry interest*” in Clause (b) of **Sub-section (7)** of Section 31 clearly indicate that the section contemplates award of only simple interest and not compound interest or interest upon interest.
- The Hon'ble Judge held that the interpretation of **Section 31(7)** of the Act under the *SL Arora Case* was correct and therefore the judgment therein was not *per incuriam*.

It was further held that the interest awarded under **Section 31(7)** of the Act was only towards compensating one party for the other party's withholding of the money which rightfully belonged to the first party and not for withholding the interest. Thus, post-award interest could only be paid towards the principal sum claimed by the party and not towards the interest *pendente lite*.

The word “*sum*” under sub-sections (a) and (b) of **Section 31(7)** of the Act, in this regard, was also interpreted to mean the money directed to be paid as per the award and did not include the interest *pendent lite*. Dattu J. examined a number of legal dictionaries to give the term “sum” its ordinary meaning and in doing so arrived at the conclusion that “sum” could only mean principal sum and not interest.

### ANALYSIS

The majority judgment in this case has used the literal rule of interpretation to read the provisions as they are and give them their plain meaning in order to glean the legislative intent from the words used in the provisions. It has examined the legislative intent to determine that the word “sum” would have to be read as inclusive of the principal and interest *pendent lite*. The implication of this majority judgment would be that parties would avoid unnecessary delays or prolonging of proceedings during the course of arbitration. During the post-award stage, there would be a reduction in frivolous challenges to the enforcement of awards, by the parties since the parties would be paying a hefty interest over a potentially enlarged claim amount.

The judgment is also in line with the Law Commission in its Report on Amendments to Arbitration and Conciliation Act, 1996<sup>4</sup> wherein the inclusion of an explanation to **Section 31(7)(b)** that would legislatively overrule the decision of the Supreme Court in *SL Arora Case* and including interest *pendent lite* as a part of word ‘sum’ has been suggested.

The dissenting judgment does provide food for thought; considering the nature of the term interest, which is compensatory in nature. There could be a legitimate argument that should the dispute have been adjudicated through a suit then post decree interest would only be over the decretal principal and not over the *pendent lite* interest. However, merely because the dispute is adjudicated through an arbitral award, parties become entitled to a post award interest over both the principal and the interest *pendent lite*, it remains to be seen if the legislature intended such a result.

One could also see, as the Hon'ble Chief Justice has held, that in the portion “*the arbitral tribunal may include in the sum for which the award is made interest*” of **Section 31(7)(a)** could be read dichotomously to state that the sum means principal but such principal could also include interest, when the award is being given.

It is important to note that while interest on *pendente lite* interest may be payable in respect of domestic arbitrations, it may not be applicable to international arbitrations seated outside India. This is owing to the non-applicability of **Section 31(7)** of the Act to foreign awards<sup>5</sup> and the absence of a similar provision under Part II of the Act which deals with the execution of foreign awards.

While this judgment has overruled *SL Arora Case* and has reversed the position of law as laid down therein, given the importance of this issue in the realm of arbitration it remains to be seen whether the case would be considered by a constitution bench of the Supreme Court, for further clarity on the issue.

– **Varuna Bhanrale, Shalaka Patil & Vyapak Desai**

You can direct your queries or comments to the authors

<sup>1</sup> (2010)3 SCC 690

<sup>2</sup> *McDermott International INC v. Bum Standard Co. Ltd. and Others*, (2006) 11 SCC 181

<sup>3</sup> *Uttar Pradesh Cooperative Federation Limited v. Three Circles*, (2009) 10 SCC 374

<sup>4</sup> Report No. 246

<sup>5</sup> *Progetto Grano S.P.A. v. Shri Lal Mahal Limited*, (2014) 2 SCC 433; You may peruse our hotline on the case [here](#).

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