REPORTABLE

IN THE SUPREME COURT OF INDIA

CIVIL APPELLATE JURISDICTION

CIVIL APPEAL NOS. 8245-8246 OF 2016

A. AYYASAMY .....APPELLANT(S)

VERSUS

A. PARAMASIVAM & ORS. .....RESPONDENT(S)

J U D G M E N T

A.K. SIKRI, J.

The parties to this *lis,* who are brothers, had entered into a deed of partnership dated 01.04.1994 for carrying on hotel business and this partnership firm has been running a hotel with the name 'Hotel Arunagiri' located at Tirunelveli, Tamil Nadu. Some disputes arose out of the said partnership deed between the parties. Partnership Deed contains an arbitration clause i.e. Clause (8) which stipulates resolution of disputes by means of arbitration.

2. Notwithstanding the same, the respondents herein have filed a civil suit before the Court of Ist Additional District Munsif Court, Tirunelveli, Madurai (Tamil Nadu) seeking a declaration that as partners they are entitled to participate in the administration of the said hotel. Relief of permanent injunction restraining the defendant (appellant herein) from interfering with their right to participate in the administration of the hotel has also been sought. This suit was filed in the year 2012. The appellant, after receiving the summons in the said suit, moved the application under Section 8 of the Arbitration and Conciliation Act, 1996 (hereinafter referred to as the 'Act') raising an objection to the maintainability of the suit in view of arbitration agreement between the parties as contained in clause (8) of the Partnership Deed dated 01.04.1994 and submitted that as per the provisions of Section 8 of the Act, it is mandatory for the Court to refer the dispute to the arbitrator. This application was resisted by the respondents with the submission that since acts of fraud were attributed to the appellant by the plaintiffs/respondents, such serious allegations of fraud could not be adjudicated upon by the Arbitral Tribunal and the appropriate remedy was to approach the civil court by filing a suit, and that was exactly done by the respondents. For this purpose, the respondents had relied upon the judgment of this

Court in the case of ***N. Radhakrishnan*** v. ***Maestro Engineers and Others***[1]***.*** This plea of the respondents was sought to be controverted by the appellant by arguing that aforesaid judgment was found to be *per incuriam* by this Court in ***Swiss Timing Ltd.*** v. ***Commonwealth Games 2010 Organising Committee***[2], wherein the application under Section 11 of the Act was allowed holding that such a plea of fraud can be adequately taken care of even by the arbitrator. It was, thus, argued that the parties were bound by the arbitration agreement and there was no reason to file the civil suit. The trial court, however, dismissed the application of the appellant herein by its order dated 25.04.2014, relying upon the judgment in ***N. Radhakrishnan.***

3. Feeling aggrieved by this order, the appellant preferred revision petition before the High Court repeating his contention that judgment in ***N. Radhakrishnan*** was held to be *per incuriam* and, therefore, trial court had committed jurisdictional error in rejecting the application of the appellant under Section 8 of the Act. Brushing aside this plea, the High Court has also chosen to go by the dicta laid down in ***N. Radhakrishnan*** with the observations that ***Swiss Timing Ltd.*** is the order passed by a single Judge of

1 (2010) 1 SCC 72
2 (2014) 6 SCC 677

this Court under Section 11 of the Act whereas judgment in ***N. Radhakrishnan*** is rendered by a Division Bench of two Hon. Judges of this Court, which is binding on the High Court.

Whether the aforesaid view of the High Court in following the dicta laid down in the case of ***N. Radhakrishnan***, in the facts of this case, is correct or not, is the question that needs determination in the instant appeal.

4. Seminal facts in the context in which the issue falls for determination have already been taken note of above. However, few more facts need to be added to the aforesaid chronology, particularly, the nature of plea of fraud taken in the suit filed by the respondents.

The respondents are four in number who are brothers of the appellant. These five brothers are the partners. Their father A. Arunagiri was also a partner along with them who died on 28.04.2009. These six partners had 1/6th share each in the partnership business. Disputes arose between the brothers after the demise of their father. It is the allegation of the respondents, as contained in the plaint, that the subject matter of the suit 'Hotel Arunagiri' was managed and administered by their father in a

disciplined manner till his death. After his death, the appellant being the eldest brother wanted to take the administration of 'Hotel Arunagiri' with the assurance that he will be following the foot prints of his father. The respondents had no other alternative except to accept the said proposal in good faith. It was, at that time resolved by all the brothers, that the daily collection of money from 'Hotel Arunagiri' should be deposited on the very next day into the hotel Current Account No.23 maintained with the Indian Overseas Bank, Tirunelveli Junction. It was agreed that about rupees ten to fifteen thousand may be kept as cash for urgent expenses. The respondents reposed confidence with the appellant and believed that his administration would never be detrimental to the smooth running of the business. On the aforesaid understanding, administration of the hotel was taken over by the appellant. But he did not adhere to the said understanding and failed to deposit day to day collection into the bank account as promised. It is also agged that the appellant, fraudulently, signed and issued a cheque for Rs.10,00,050/- dated 17.06.2010 from the bank account in the name of 'Hotel Arunagiri' in favour of his son without the knowledge and consent of the other partners and in this manner, the money was siphoned off and misappropriated from the common fund. It is further alleged

that the appellant kept the hotel account books with him and did not show it to the respondents for their examination. The respondents sent legal notices but it did not deter the appellant to continue to act in the same manner by not depositing the day to day collections in the account. It is also alleged that appellant's wife's younger brother one Dhanapalraj was a member of Bar Council of Tamil Nadu and was also a Vice-Chairman of All India Bar Council, New Delhi. In Chennai, the Central Bureau of Investigation (C.B.I.) raided the houses of the said Dhanapalraj and his co-brother Chandrasekaran and seized Rs.45,00,000/- cash from them. As Dhanapalraj was aware of the disputes between the appellant and the respondents in respect of the 'Hotel Arunagiri', a false statement has been given by him before C.B.I. to the effect that the seized money of Rs.45 lakhs belonged to 'Hotel Arunagiri'. It is reliably learned that the appellant had also, on receipt of summons, appeared before the C.B.I. in New Delhi and given a false statement as if the said seized money of Rs.45 lakhs belonged to 'Hotel Arunagiri' which was taken to Chennai to purchase a property. This led to the issuance of another notice dated 22.01.2011 by the third respondent to the appellant stating that the money seized by the C.B.I. belong only to Dhanpalaraj and not 'Hotel Arunagiri'. On the basis of the

aforesaid allegations, which are relevant and material for the purposes of this appeal, following reliefs are sought in the suit filed by the respondents:

> "(a) for a declaration that the respondents as partners of the deed of partnership dated 01.04.1994 are entitled to participate in the administration of the Hotel Arunagiri mentioned in the schedule and for consequential permanent injunction restraining the appellant from interfering with the same;
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> (b) for cost of this suit; and
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> (c) for such other reliefs this Honourable Court deem fit and proper in the circumstances of this case."

5. As already mentioned above, the appellant filed the application under Section 8 of the Act for rejection of the plaint and reference of the dispute to an arbitrator in which attempt the appellant has not succeeded for the reasons stated hereinabove.

6. The two courts below have preferred to adopt the dicta laid down in ***N. Radhakrishnan*** while dismissing the application of the appellant under Section 8 of the Act holding that as there are serious allegations as to fraud and malpractices committed by the appellant in respect of the finances of the partnership firm and the

case does not warrant to be tried and decided by the arbitrator and a civil court would be more competent which has the requisite means to decide such complicated matter. In this backdrop, it would be appropriate to revisit the law on this aspect before adverting to the question as to whether the approach of the High Court was correct in following the judgment in ***N. Radhakrishnan*** in the instant case.

7. In this behalf, we have to begin our discussion with the pertinent observation that insofar as the Arbitration and Conciliation Act, 1996 is concerned, it does not make any specific provision excluding any category of disputes terming them to be non-arbitrable. Number of pronouncements have been rendered laying down the scope of judicial intervention, in cases where there is an arbitration clause, with clear and unambiguous message that in such an event judicial intervention would be very limited and minimal. However, the Act contains provisions for challenging the arbitral awards. These provisions are Section 34 and Section 48 of the Act. Section 34(2)(b) and Section 48(2) of the Act, *inter alia,* provide that an arbitral award may be set aside if the Court finds that the 'subject matter of the dispute is not capable of settlement by arbitration under the law for the time

being in force.' Even when such a provision is interpreted, what is to be shown is that there is a law which makes subject matter of a dispute incapable of settlement by arbitration. The aforesaid position in law has been culled out from the combined readings of Sections 5, 16 and 34 of the Act. When arbitration proceedings are triggered by one of the parties because of the existence of an arbitration agreement between them, Section 5 of the Act, by a *non-obstante* clause, provides a clear message that there should not be any judicial intervention at that stage scuttling the arbitration proceedings. Even if the other party has objection to initiation of such arbitration proceedings on the ground that there is no arbitration agreement or validity of the arbitration clause or the competence of the Arbitral Tribunal is challenged, Section 16, in clear terms, stipulates that such objections are to be raised before the Arbitral Tribunal itself which is to decide, in the first instance, whether there is any substance in questioning the validity of the arbitration proceedings on any of the aforesaid grounds. It follows that the party is not allowed to rush to the Court for an adjudication. Even after the Arbitral Tribunal rules on its jurisdiction and decides that arbitration clause is valid or the Arbitral Tribunal is legally constituted, the aggrieved party has to wait till the final award is pronounced and only at that stage the

aggrieved party is allowed to raise such objection before the Court in proceedings under Section 34 of the Act while challenging the arbitral award. The aforesaid scheme of the Act is succinctly brought out in the following discussion by this Court in ***Kvaerner Cementation India Ltd.*** v. ***Bajranglal Agarwal & Anr.***[3]:

> "3. There cannot be any dispute that in the absence of any arbitration clause in the agreement, no dispute could be referred for arbitration to an Arbitral Tribunal. But, bearing in mind the very object with which the Arbitration and Conciliation Act, 1996 has been enacted and the provisions thereof contained in Section 16 conferring the power on the Arbitral Tribunal to rule on its own jurisdiction, including ruling on any objection with respect to existence or validity of the arbitration agreement, we have no doubt in our mind that the civil court cannot have jurisdiction to go into that question.
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> 4. A bare reading of Section 16 makes it explicitly clear that the Arbitral Tribunal has the power to rule on its own jurisdiction even when any objection with respect to existence or validity of the arbitration agreement is raised, and a conjoint reading of sub-sections (2), (4) and (6) of Section 16 would make it clear that such a decision would be amenable to be assailed within the ambit of Section 34 of the Act.
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> 5. In this view of the matter, we see no infirmity in the impugned order so as to be interfered with by this Court. The petitioner, who is a party to the arbitral proceedings may raise the question of jurisdiction of the arbitrator as well as the objection on the ground of non-existence of any arbitration agreement in the so-called dispute in question, and

3 (2012) 5 SCC 214

> on such an objection being raised, the arbitrator would do well in disposing of the same as a preliminary issue so that it may not be necessary to go into the entire gamut of arbitration proceedings."

Aforesaid is the position when Arbitral Tribunal is constituted at the instance of one of the parties and other party takes up the position that such proceedings are not valid in law.

8. What would be the position in case a suit is filed by the plaintiff and in the said suit the defendant files an application under Section 8 of the Act questioning the maintainability of the suit on the ground that parties had agreed to settle the disputes through the means of arbitration having regard to the existence of an arbitration agreement between them?

Obviously, in such a case, the Court is to pronounce upon arbitrability or non-arbitrability of the disputes.

9. In the instant case, there is no dispute about the arbitration agreement inasmuch as there is a specific arbitration clause in the partnership deed. However, the question is as to whether the dispute raised by the respondent in the suit is incapable of settlement through arbitration. As pointed out above, the Act does

not make any provision excluding any category of disputes treating them as non-arbitrable. Notwithstanding the above, the Courts have held that certain kinds of disputes may not be capable of adjudication through the means of arbitration. The Courts have held that certain disputes like criminal offences of a public nature, disputes arising out of illegal agreements and disputes relating to status, such as divorce, cannot be referred to arbitration. Following categories of disputes are generally treated as non-arbitrable[4]:

(i) patent, trademarks and copyright;

(ii) anti-trust/competition laws;

(iii) insolvency/winding up;

(iv) bribery/corruption;

(v) fraud;

(vi) criminal matters.

Fraud is one such category spelled out by the decisions of this Court where disputes would be considered as non-arbitrable.

4 See – *O.P. Malhotra on 'The Law & Practice of Arbitration and Conciliation'*, Third Edition, authored by Indu Malhotra. See also note 10 ibid.

10. 'Fraud' is a *knowing misrepresentation of the truth or concealment of a material fact to induce another to act to his detriment.* Fraud can be of diffeent forms and hues. Its ingredients are an intention to deceive, use of unfair means, deliberate concealment of material facts, or abuse of position of confidence. The Black's Law Dictionary defines 'fraud' as a concealment or false representation through a statement or conduct that injures another who relies on it[5]. However, the moot question here which has to be addressed would be as to whether mere allegation of fraud by one party against the other would be sufficient to exclude the subject matter of dispute from arbitration and decision thereof necessary by the civil court.

11. In ***Abdul Kadir Shamsuddin Bubere*** v. ***Madhav Prabhakar Oak***[6], serious allegations of fraud were held by the Court to be a sufficient ground for not making a reference to arbitration. Reliance in that regard was placed by the Court on a decision of the Chancery Division in ***Russell*** v. ***Russell***[7]. That was a case where a notice for the dissolution of a partnership was issued by

5 See – *Ramesh Kumar & Anr.* v. *Furu Ram & Anr.*, (2011) 8 SCC 613 (a decision rendered under the Arbitration Act, 1940)

6 AIR 1962 SC 406

7 (1880) 14 Ch D 471

one of the partners, upon which the other partner brought an action alleging various charges of fraud, and sought a declaration that the notice of dissolution was void. The partner who was charged with fraud sought reference of the disputes to arbitration. The Court held that in a case where fraud is charged, the Court will in general refuse to send the dispute to arbitration. But where the objection to arbitration is by a party charging the fraud, the Court will not necessarily accede to it and would never do so unless a *prima facie* case of fraud is proved.

12. The aforesaid judgment was followed by this Court in ***N. Radhakrishnan*** while considering the matter under the present Act. In that case, the respondent had instituted a suit against the appellant, upon which the appellant filed an application under Section 8 of the Act. The applicant made serious allegations against the respondents of having committed malpractices in the account books, and manipulation of the finances of the partnership firm. This Court held that such a case cannot be properly dealt with by the arbitrator, and ought to be settled by the Court, through detailed evidence led by both parties.

13. When the case involves serious allegations of fraud, the dicta contained in the aforesaid judgments would be understandable. However, at the same time, mere allegation of fraud in the pleadings by one party against the other cannot be a ground to hold that the matter is incapable of settlement by arbitration and should be decided by the civil court. The allegations of fraud should be such that not only these allegations are serious that in normal course these may even constitute criminal offence, they are also complex in nature and the decision on these issues demand extensive evidence for which civil court should appear to be more appropriate forum than the Arbitral Tribunal. Otherwise, it may become a convenient mode of avoiding the process of arbitration by simply using the device of making allegations of fraud and pleading that issue of fraud needs to be decided by the civil court. The judgment in ***N. Radhakrishnan*** does not touch upon this aspect and said decision is rendered after finding that allegations of fraud were of serious nature.

14. As noted above, in ***Swiss Timing Ltd.*** case, single Judge of this Court while dealing with the same issue in an application under Section 11 of the Act treated the judgment in ***N. Radhakrishnan*** as *per incuriam* by referring to the other judgments in the case of

P. Anand Gajapathi Raju v. ***P.V.G. Raju***[8] and ***Hindustan Petroleum Corpn. Ltd.*** v. ***Pinkcity Midway Petroleums***[9]. Two reasons were given in support which can be found in para 21 of the judgment which makes the following reading:

> "21. This judgment was not even brought to the note of the Court in ***N. Radhakrishnan's*** case. In my opinion, judgment in ***N. Radhakrishnan's*** case is *per incuriam* on two grounds; Firstly, the judgment in ***Hindustan Petroleum Corpn. Ltd.***, though referred has not been distinguished but at the same time is not followed also. The judgment in ***P. Anand Gajapathi Raju & Ors.*** Was not even brought to the notice of this Court. Therefore, the same has neither been followed nor considered. Secondly, the provision contained in Section 16 of the Arbitration Act, 1996 were also not brought to the notice by this Court. Therefore, in my opinion, the judgment in ***N. Radhakrishnan*** does not lay down the correct law and cannot be relied upon."

15. We shall revert to the question of *per incuriam* at a later stage. At this juncture, we may point out that the issue has been revisited by another Division Bench of this Court in ***Booz Allen & Hamilton Inc.*** v. ***SBI Home Finance Limited and others***[10]. In this case, one of the questions that had arisen for determination was, in the context of Section 8 of the Act, as to whether the subject matter of the suit was 'arbitrable' i.e. capable of being

8 (2000) 4 SCC 539
9 (2003) 6 SCC 503
10 (2011) 5 SCC 532

adjudicated by a private forum (Arbitral Tribunal). In this context, the Court carried out detailed discussion on the term 'arbitrability' by pointing out three facets thereof, viz.:

1) whether the disputes are capable of adjudication and settlement by arbitration?

2) whether the disputes are covered by the arbitration agreement?

3) whether the parties have referred the disputes to arbitration?

16. As we are concerned with the first facet of the arbitrability of dispute, on this aspect the Court pointed out that in those cases where the subject matter falls exclusively within the domain of public fora, viz. the Courts, such disputes would be non-arbitrable and cannot be decided by the Arbitral Tribunal but by the Courts alone. The justification and rationale given for adjudicating such disputes through the process of Courts, i.e. public fora, and not by Arbitral Tribunals, which is a private forum, is given by the court in the following manner:

> "35. The Arbitral Tribunals are private fora chosen voluntarily by the parties to the dispute, to adjudicate their disputes in place of courts and tribunals which are public fora constituted under the laws of the country. Every civil or commercial dispute, either contractual or non-contractual, which can be decided by a court, is in principle

capable of being adjudicated and resolved by arbitration unless the jurisdiction of the Arbitral Tribunals is excluded either expressly or by necessary implication. Adjudication of certain categories of proceedings are reserved by the legislature exclusively for public fora as a matter of public policy. Certain other categories of cases, though not expressly reserved for adjudication by public fora (courts and tribunals), may by necessary implication stand excluded from the purview of private fora. Consequently, where the cause/dispute is inarbitrable, the court where a suit is pending, will refuse to refer the parties to arbitration, under Section 8 of the Act, even if the parties might have agreed upon arbitration as the forum for settlement of such disputes.

36. The well-recognised examples of non-arbitrable disputes are: (*i*) disputes relating to rights and liabilities which give rise to or arise out of criminal offences; (*ii*) matrimonial disputes relating to divorce, judicial separation, restitution of conjugal rights, child custody; (*iii*) guardianship matters; (*iv*) insolvency and winding-up matters; (*v*) testamentary matters (grant of probate, letters of administration and succession certificate); and (*vi*) eviction or tenancy matters governed by special statutes where the tenant enjoys statutory protection against eviction and only the specified courts are conferred jurisdiction to grant eviction or decide the disputes.

37. It may be noticed that the cases referred to above relate to actions in rem. A right in rem is a right exercisable against the world at large, as contrasted from a right in personam which is an interest protected solely against specific individuals. Actions in personam refer to actions determining the rights and interests of the parties themselves in the subject-matter of the case, whereas actions in rem refer to actions determining the title to property and the rights of the parties, not merely among themselves but

> also against all persons at any time claiming an interest in that property. Correspondingly, a judgment in personam refers to a judgment against a person as distinguished from a judgment against a thing, right or status and a judgment in rem refers to a judgment that determines the status or condition of property which operates directly on the property itself. (Vide *Black's Law Dictionary*.)
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> 38. Generally and traditionally all disputes relating to rights in personam are considered to be amenable to arbitration; and all disputes relating to rights in rem are required to be adjudicated by courts and public tribunals, being unsuited for private arbitration. This is not however a rigid or inflexible rule. Disputes relating to subordinate rights in personam arising from rights in rem have always been considered to be arbitrable."

17. The Law Commission has taken note of the fact that there is divergence of views between the different High Courts where two views have been expressed, one is in favor of the civil court having jurisdiction in cases of serious fraud and the other view encompasses that even in cases of serious fraud, the Arbitral Tribunal will rule on its own jurisdiction. It may be pertinent here to reproduce the observations of the Law Commission as contained in paragraphs 50 & 51 of the 246th Law Commission Report, which are as under:

> ""50. The issue of arbitrability of fraud has arisen on

numerous occasions and there exist conflicting decisions of the Apex Court on this issue. While it has been held in *Bharat Rasiklal*v. *Gautam Rasiklal*, (2012) 2 SCC 144 that when fraud is of such a nature that it vitiates the arbitration agreement, it is for the Court to decide on the validity of the arbitration agreement by determining the issue of fraud, there exists two parallel lines of judgments on the issue of whether an issue of fraud is arbitrable. In this context, a 2 judge bench of the Supreme Court, while adjudicating on an application under section 8 of the Act, in *Radhakrishnan* v. *Maestro Engineers*, 2010 1 SCC 72 held that an issue of 28 fraud is not arbitrable. This decision was ostensibly based on the decision of the three judge bench of the Supreme Court in *Abdul Qadir* v. *Madhav Prabhakar*, AIR 1962 SC 406. However, the said 3 judge bench decision (which was based on the finding in *Russel* v. *Russel* [1880 14 Ch.D 471]) is only an authority for the proposition that a party against whom an allegation of fraud is made in a public forum, has a right to defend himself in that public forum. Yet, following Radhakrishnan, it appears that issues of fraud are not arbitrable.

51. A distinction has also been made by certain High Courts between a serious issue of fraud and a mere allegation of fraud and the former has been held to be not arbitrable (See*Ivory Properties and Hotels Private Ltd* v. *Nusli Neville Wadia*, 2011 (2) Arb LR 479 (Bom); *CS Ravishankar* v. *CK Ravishankar*, 2011 (6) Kar LJ 417). The Supreme Court in *Meguin GMBH* v. *Nandan Petrochem Ltd.*, 2007 (5) R.A.J 239 (SC), in the context of an application filed under section 11 has gone ahead and appointed an arbitrator even though issues of fraud were involved. Recently, the Supreme Court in its judgment in *Swiss Timing Ltd* v. *Organising Committee*, Arb. Pet. No. 34/2013 dated 28.05.2014, in a similar case of exercising jurisdiction under section 11, held that the judgment in *Radhakrishnan* is per incuriam and, therefore, not good law."

18. A perusal of the aforesaid two paragraphs brings into fore that the Law Commission has recognized that in cases of serious fraud, courts have entertained civil suits. Secondly, it has tried to make a distinction in cases where there are allegations of serious fraud and fraud simplicitor. It, thus, follows that those cases where there are serious allegations of fraud, they are to be treated as non-arbitrable and it is only the civil court which should decide such matters. However, where there are allegations of fraud simplicitor and such allegations are merely alleged, we are of the opinion it may not be necessary to nullify the effect of the arbitration agreement between the parties as such issues can be determined by the Arbitral Tribunal.

19. Before we apply the aforesaid test to the facts of the present case, a word on the observations in ***Swiss Timing Ltd.'s*** case to the effect that judgment of ***N. Radhakrishnan*** was *per incuriam*, is warranted. In fact, we do not have to labour on this aspect as this task is already undertaken by this Court in ***State of West Bengal & Ors.*** v. ***Associated Contractors***[11]. It has been clarified in the aforesaid case that ***Swiss Timings Ltd.*** was a judgment

11 (2015) 1 SCC 32

rendered while dealing with Section 11(6) of the Act and Section 11 essentially confers power on the Chief Judge of India or the Chief Justice of the High Court as a designate to appoint an arbitrator, which power has been exercised by another Hon'ble Judge as a delegate of the Chief Justice. This power of appointment of an arbitrator under Section 11 by the Court, notwithstanding the fact that it has been held in ***SBP & Co.*** v. ***Patel Engineering Ltd. & Anr.***[12] as a judicial power, cannot be deemed to have precedential value and, therefore, it cannot be deemed to have overruled the proposition of law laid down in ***N.Radhakrishnan.***

20. In view of our aforesaid discussions, we are of the opinion that mere allegation of fraud simplicitor may not be a ground to nullify the effect of arbitration agreement between the parties. It is only in those cases where the Court, while dealing with Section 8 of the Act, finds that there are very serious allegations of fraud which make a virtual case of criminal offence or where allegations of fraud are so complicated that it becomes absolutely essential that such complex issues can be decided only by civil court on the appreciation of the voluminous evidence that needs to be

12 (2005) 8 SCC 618

produced, the Court can sidetrack the agreement by dismissing application under Section 8 and proceed with the suit on merits. It can be so done also in those cases where there are serious allegations of forgery/fabrication of documents in support of the plea of fraud or where fraud is alleged against the arbitration provision itself or is of such a nature that permeates the entire contract, including the agreement to arbitrate, meaning thereby in those cases where fraud goes to the validity of the contract itself of the entire contract which contains the arbitration clause or the validity of the arbitration clause itself. Reverse position thereof would be that where there are simple allegations of fraud touching upon the internal affairs of the party *inter se* and it has no implication in the public domain, the arbitration clause need not be avoided and the parties can be relegated to arbitration. While dealing with such an issue in an application under Section 8 of the Act, the focus of the Court has to be on the question as to whether jurisdiction of the Court has been ousted instead of focusing on the issue as to whether the Court has jurisdiction or not. It has to be kept in mind that insofar as the statutory scheme of the Act is concerned, it does not specifically exclude any category of cases as non-arbitrable. Such categories of non-arbitrable subjects are carved out by the Courts, keeping in

mind the principle of common law that certain disputes which are of public nature, etc. are not capable of adjudication and settlement by arbitration and for resolution of such disputes, Courts, i.e. public for a, are better suited than a private forum of arbitration. Therefore, the inquiry of the Court, while dealing with an application under Section 8 of the Act, should be on the aforesaid aspect, viz. whether the nature of dispute is such that it cannot be referred to arbitration, even if there is an arbitration agreement between the parties. When the case of fraud is set up by one of the parties and on that basis that party wants to wriggle out of that arbitration agreement, a strict and meticulous inquiry into the allegations of fraud is needed and only when the Court is satisfied that the allegations are of serious and complicated nature that it would be more appropriate for the Court to deal with the subject matter rather than relegating the parties to arbitration, then alone such an application under Section 8 should be rejected.

21. When we apply the aforesaid principles to the facts of this case, we find that the only allegation of fraud that is levelled is that the appellant had signed and issued a cheque of Rs. 10,00,050/- dated 17.06.2010 of 'Hotel Arunagiri' in favour of his son without

the knowledge and consent of the other partners i.e. the respondents. It is a mere matter of accounts which can be looked into and found out even by the arbitrator. It does not involve any complex issue. If such a cheque is issued from the hotel account by the appellant in favour of his son, it is easy to prove the same and then the onus is upon the appellant to show as to what was the reason for giving that amount from the partnership firm to his son and he will have to account for the same. Likewise, the allegation of the respondents that daily collections are not deposited in the bank accounts is to be proved by the respondents which is again a matter of accounts.

Other allegation, which appears to be serious, is about the C.B.I. raid at the house of Dhanapalraj from where cash in the sum of Rs.45 lakhs was seized. Interestingly, though the appellant has taken the position that this cash belongs to 'Hotel Arunagiri', they are the respondents who have themselves alleged that the money belonged to Dhanapalraj and not to 'Hotel Arunagiri'. In view of the aforesaid stand taken by the respondents/plaintiffs themselves, this issue does not fall for consideration and, therefore, is not to be gone by the Arbitral Tribunal.

22. We, therefore, are of the opinion that the allegations of purported fraud were not so serious which cannot be taken care of by the arbitrator. The Courts below, therefore, fell in error in rejecting the application of the appellant under Section 8 of the Act. Reversing these judgments, we allow this appeal and as a consequence, application filed by the appellant under Section 8 in the suit is allowed thereby relegating the parties to the arbitration.

23. At the same time, in order to save the time and having regard to the nature of the dispute, this Court appoints Hon'ble Ms. Justice Prabha Sridevan, a retired Judge of the Madras High Court, as the arbitrator. The arbitrator shall fix her own fee.

No costs.

.....J.

(A.K. SIKRI)

.....J.

(DR. D.Y. CHANDRACHUD)

NEW DELHI;

OCTOBER 04, 2016.

REPORTABLE

IN THE SUPREME COURT OF INDIA

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CIVIL APPEAL Nos. 8245-8246 OF 2016
[Arising out of SLP(C)Nos. 16250-16251 of 2015]

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J U D G M E N T

Dr D Y CHANDRACHUD, J

1 I have had the benefit of the lucid exposition of law in the judgment of my learned brother Justice A K Sikri. I agree with the reasons contained in His Lordship's judgment while adding some of my own.

2 The issue which arises in these proceedings has generated a considerable degree of uncertainty in the law of arbitration in India. This is an area of law where the intervention of this Court is needed to ensure that a cloud on the efficacy of arbitral proceedings to resolve issues of fraud is resolved

conclusively. The litigative uncertainty which the discourse has produced is best set at rest for nothing is as destructive of legitimate commercial expectations than a state of unsettled legal precept.

3 The Arbitration and Conciliation Act, 1996 does not in specific terms exclude any category of disputes – civil or commercial – from arbitrability. Intrinsic legislative material is in fact to the contrary. Section 8 contains a mandate that where an action is brought before a judicial authority in a matter which is the subject of an arbitration agreement, parties shall be referred by it to arbitration, if a party to or a person claiming through a party to the arbitration agreement applies not later than the date of submitting the first statement on the substance of the dispute. The only exception is where the authority finds prima facie that there is no valid arbitration agreement. Section 8 contains a positive mandate and obligates the judicial authority to refer parties to arbitration in terms of the arbitration agreement. While dispensing with the element of judicial discretion, the statute imposes an affirmative obligation on every judicial authority to hold down parties to the terms of the agreement entered into between them to refer disputes to arbitration. Article 8 of the UNCITRAL Model Law enabled a court to decline to refer parties to arbitration if it is found that the arbitration agreement is null and void, inoperative or incapable of being performed. Section 8 of the Act of 1996 has made a departure which is indicative of the wide reach and ambit of the statutory mandate. Section 8 uses the expansive expression "judicial

authority" rather than "court" and the words "unless it finds that the agreement is null and void, inoperative and incapable of being performed" do not find place in Section 8.

4 Section 16 empowers the arbitral tribunal to rule upon its own jurisdiction, including ruling on any objection with respect to the existence or validity of an arbitration agreement. Section 16(1)(b) stipulates that a decision by the arbitral tribunal that a contract is null and void shall not entail ipso jure the invalidity of the arbitration clause. Hence, the invalidity of the contract between the parties does not render the arbitration agreement invalid as a consequence of law. This recognises as inhering in the arbitrator the jurisdiction to consider whether the main contract (other than the arbitration clause) is null and void. The arbitration agreement survives for determining whether the contract in which the arbitration clause is embodied is null and void, which would include voidability on the ground of fraud. The severability of the arbitration agreement is a doctrinal development of crucial significance. For, it leaves the adjudicatory power of the arbitral tribunal unaffected, over any objection that the main contract between the parties is affected by fraud or undue influence.

5 Section 34(2)(b) and Section 48(2) provide as one of the grounds for challenge to or in respect of the enforceability of an award that "the subject matter of the dispute is not capable of settlement by arbitration under the law

for the time being in force". Clearly, therefore, the Act contemplates and acknowledges that before it can be held that a particular subject matter is not capable of settlement by arbitration, such a consequence must arise under the law for the time being in force.

6 Ordinarily every civil or commercial dispute whether based on contract or otherwise which is capable of being decided by a civil court is in principle capable of being adjudicated upon and resolved by arbitration "subject to the dispute being governed by the arbitration agreement" unless the jurisdiction of the Arbitral Tribunal is excluded either expressly or by necessary implication. In **Booz-Allen and Hamilton Inc**. v. **SBI Home Finance Ltd**.[13], this Court held that adjudication of certain categories of proceedings is reserved by the legislature exclusively for public fora as a matter of public policy. Certain other categories of cases, though not exclusively reserved for adjudication by courts and tribunals may by necessary implication stand excluded from the purview of private fora. This Court set down certain examples of non-arbitrable disputes such as:

(i) Disputes relating to rights and liabilities which give rise to or arise out of criminal offences;

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13 **(2011) 5 SCC 532**

(ii) Matrimonial disputes relating to divorce, judicial separation, restitution of conjugal rights and child custody;

(iii) Matters of guardianship;

(iv) Insolvency and winding up;

(v) Testamentary matters, such as the grant of probate, letters of administration and succession certificates; and

vi) Eviction or tenancy matters governed by special statutes where a tenant enjoys special protection against eviction and specific courts are conferred with the exclusive jurisdiction to deal with the dispute.

This Court held that this class of actions operates *in rem*, which is a right exercisable against the world at large as contrasted with a right *in personam* which is an interest protected against specified individuals. All disputes relating to rights *in personam* are considered to be amenable to arbitration while rights *in rem* are required to be adjudicated by courts and public tribunals. The enforcement of a mortgage has been held to be a right *in rem* for which proceedings in arbitration would not be maintainable. In **Vimal Kishore Shah** v. **Jayesh Dinesh Shah**[14], this Court added a seventh category of cases to the six non-arbitrable categories set out in **Booz Allen**, namely,

14 (2016) SCC OnLine SC 825

disputes relating to trusts, trustees and beneficiaries arising out of a trust deed and the Trust Act.

7 In **Natraj Studios (P) Ltd.** v. **Navrang Studios**[15], a Bench of three judges of this Court dealt with the issue as to whether a dispute between a landlord and a tenant falling within the exclusive domain of the Court of Small Causes at Mumbai, to the exclusion of the civil court, is arbitrable. This Court held that the Bombay Rent Act is a welfare legislation aimed at a definite social objective of protecting tenants as a matter of public policy. The conferment of exclusive jurisdiction on certain courts was in pursuance of a specific social objective which the legislation seeks to achieve. Public policy, this Court held, requires that parties cannot be allowed to contract out of the legislative mandate which requires certain kinds of disputes to be resolved by special courts constituted under rent control legislation. Hence, arbitration agreements between parties whose rights are regulated by rent control legislation would not be recognised by a court of law.

8 In regard to disputes under the Consumer Protection Act, 1986, this Court held in **Skypak Courier Ltd.** v. **Tata Chemical Ltd**[16], that the existence of an arbitration clause will not be a bar to the entertainment of a complaint by a forum under the Consumer Protection Act, 1986 since the remedy provided

15 (1981) 2 SCR 466

16 (2000) 5 SCC 294

under the law is in addition to the provisions of any other law for the time being in force. This was reiterated in **National Seeds Corporation Ltd**. v. **M. Madhusudhan Reddy**[17], and **Rosedale Developers Pvt. Ltd**. v. **Aghore Bhattacharya**[18]. It was observed that the remedy is merely optional and is in addition to and not in derogation of the provisions of any other law for the time being in force.

9 Hence, in addition to various classes of disputes which are generally considered by the courts as appropriate for decision by public fora, there are classes of disputes which fall within the exclusive domain of special fora under legislation which confers exclusive jurisdiction to the exclusion of an ordinarily civil court. That such disputes are not arbitrable dovetails with the general principle that a dispute which is capable of adjudication by an ordinary civil court is also capable of being resolved by arbitration. However, if the jurisdiction of an ordinary civil court is excluded by the conferment of exclusive jurisdiction on a specified court or tribunal as a matter of public policy such a dispute would not then be capable of resolution by arbitration.

10 The judgment of a two judge Bench of this Court in **N. Radhakrishnan** v. **Maestro Engineers**[19], arose out of a partnership dispute. A suit was

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17 **(2012) 2 SCC 506**

18 **(2015)1 WBLR (SC) 385**

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instituted before the civil court for declaratory and injunctive reliefs. An application under Section 8 of the Act of 1996 was rejected by the trial court and the order of rejection was affirmed in revision by the High Court. The submission of the appellant that the dispute between the partners ought to have been referred to arbitration was met with the objection that the appellant having raised issues relating to misappropriation of funds and malpractices, these were matters which ought to be resolved by a civil court. Affirming the judgment of the High Court, a Bench of two judges of this Court held as follows:

> "The High Court in its impugned judgment has rightly held that since the case relates to allegations of fraud and serious malpractices on the part of the respondents, such a situation can only be settled in court through furtherance of detailed evidence by either parties and such a situation cannot be properly gone into by the Arbitrator. " (I.d. at p. 7)

The judgment accepted the submission of the respondent that the appellant having raised serious matters alleging criminal wrongdoing, such disputes ought to be adjudicated upon by the civil court:

> "The learned counsel appearing on behalf of the respondents on the other hand contended that the appellant had made serious allegations against the respondents alleging that they had manipulated the accounts and defrauded the appellant by cheating the appellant of his dues, thereby warning the respondents with serious criminal action against them for the alleged commission of criminal offences. In this connection, reliance was placed in a decision of this Court in the case of **Abdul Kadir Shamsuddin**

(2010) 1 SCC 72

> **Bubere** vs. **Madhav Prabhakar Oak** and Another, [AIR 1962 SC 406] in which this Court under para 17 held as under:
>
> > "There is no doubt that where serious allegations of fraud are made against a party and the party who is charged with fraud desires that the matter should be tried in open court, that would be a sufficient cause for the court not to order an arbitration agreement to be filed and not to make the reference…."
>
> In our view and relying on the aforesaid observations of this Court in the aforesaid decision and going by the ratio of the above mentioned case, the facts of the present case does not warrant the matter to be tried and decided by the Arbitrator, rather for the furtherance of justice, it should be tried in a court of law which would be more competent and have the means to decide such a complicated matter involving various questions and issues raised in the present dispute."

The above extract from the judgment in **N. Radhakrishnan** relies extensively on the view propounded in **Abdul Kadir** (supra). The decision in **Abdul Kadir** arose under the Arbitration Act, 1940 and was in the context of the provisions of Section 20. In **Abdul Kadir**, this Court emphasized that sub-Section (4) of Section 20 of the Arbitration Act, 1940 left a wide discretion in the court. In contrast, the scheme of the Act of 1996 has made a radical departure from the position under the erstwhile enactment. A marked distinction is made in Section 8 where no option has been left to the judicial authority but to refer parties to arbitration. **Abdul Kadir** explains the position under the Arbitration Act, 1940. The present legislation on the subject

embodies a conscious departure which is intended to strengthen the efficacy of arbitration.

11 In **P. Anand Gajapathi Raju** v. **P.V.G. Raju (Dead)**[20], this Court held that the language of Section 8 is peremptory in nature. Hence, where there is an arbitration agreement, it is obligatory for the court to refer parties to arbitration and nothing remains to be decided in the original action after such an application is made, except to refer the dispute to an arbitrator. The judgment in **Abdul Kadir** came up for consideration before a Bench of two learned judges in **Hindustan Petroleum Corporation Ltd**. v. **Pinkcity Midway Petroleums**[21]. In that case, the appellant had appointed the respondent as a dealer for selling its petroleum products through a retail outlet. The dealership agreement contained an arbitration agreement. In the course of an inspection the appellant found a breach of the dealership agreement and sales of petroleum products were suspended. The respondent instituted a suit before the ordinary civil court seeking declaratory reliefs in which the appellant filed an application under Section 8 of the Arbitration and Conciliation Act, 1996. The civil court rejected the application and the High Court in revision affirmed the view. The submission which weighed with the High Court was that the allegation of tampering of weights and of

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20 **(2000) 4 SCC 539**

21 **(2003) 6 SCC 503**

measurement seals could only be adjudicated upon under the Standards of Weights and Measures (Enforcement) Act, 1985 and hence such a dispute was not arbitrable. This Court held that once the arbitration agreement was admitted, in view of the mandatory language of Section 8, the dispute ought to have been referred to arbitration. The judgment of this Court dealt with the submission that since the allegations in the case related to an element of criminal wrongdoing, the dispute was not arbitrable. Rejecting this submission, this Court held as follows:

> "19 It was argued before the courts below as also before us that the mis-conduct, if any, pertaining to short-supply of petroleum products or tampering with the seals would be a criminal offence under the 1985 Act. Therefore, the investigation into such conduct of the dealer can only be conducted by such offices and in a manner so specified in the said Act, and it is not open to the appellant to arrogate to itself such statutory power of search and seizure by relying on some contractual terms in the Dealership Agreement. It is further argued that such disputes involving penal consequences can only be tried by a court of competent jurisdiction and cannot be decided by an arbitrator…..
> 20 Having considered the above arguments addressed on behalf of the respondent as also the findings of the courts below, we are of the opinion that the same cannot be accepted because the appellant is neither exercising the power of search and seizure conferred on a competent authority under the 1985 Act nor does the Dealership Agreement contemplate the arbitrator to exercise the power of a criminal court while arbitrating on a dispute which has arisen between the contracting parties. This is clear from the terms of the Dealership Agreement." (Id. at p. 19-20)

In the view of this Court, the dispute between the parties was clearly referable to the terms of the contract and did not entrench upon the legislative provisions contained in the Standards of Weights and Measures (Enforcement) Act, 1985:

> "The courts below in our opinion, have committed an error by misreading the terms of the contract when they came to the conclusion that the only remedy available as against a misconduct committed by an erring dealer in regard to short-supply and tampering with the seals lies under the provisions of the 1985 Act. The courts below have failed to notice that when a dealer short-supplies or tampers with the seal, apart from the statutory violation, he also commits a misconduct under Clause 20 of the Agreement in regard to which the appellant is entitled to invoke Clause 30 of the Agreement to stop supply of petroleum products to such dealer. The power conferred under the Agreement does not in any manner conflict with the statutory power under the 1985 Act nor does the prescribed procedure under the 1985 Act in regard to search and seizure and prosecution apply to the power of the appellant to suspend the supply of its petroleum products to an erring dealer. The power exercised by the appellant in such a situation is a contractual power under the agreement and not a statutory one under the 1985 Act. The existence of dual procedure; one under the criminal law and the other under the contractual law is a well-accepted legal phenomenon in the Indian jurisprudence…….
>
> Therefore, in our opinion, the courts below have erred in coming to the conclusion that the appellant did not have the legal authority to investigate and proceed against the respondent for its alleged misconduct under the terms of the Dealership Agreement. We are also of the opinion that if the appellant is satisfied that the respondent is indulging in short-supply or tampering with the seals, it will be entitled to initiate such action as is contemplated under the agreement like suspending or stopping the supply of petroleum products to such erring dealer. If in that process any dispute arises between the appellant and such dealer, the same will have to be referred to arbitration as contemplated under Clause 40 of the Dealership Agreement." (Id. at p. 23-24)

12 Hence, allegations of criminal wrongdoing or of statutory violation would not detract from the jurisdiction of the arbitral tribunal to resolve a dispute arising out of a civil or contractual relationship on the basis of the jurisdiction conferred by the arbitration agreement.

13 In a more recent judgment of two judges of this Court in **Sundaram Finance Ltd**. v. **T. Thankam**[22], the same position in regard to the mandate of Section 8 has been reiterated. The earlier decisions in **Anand Gajapathi Raju**, **Pink City** and in **Branch Manager, Magma Leasing and Finance Ltd**. v. **Potluri Madhvilata**[23], emphasizing the mandate of Section 8, have been reaffirmed. This Court has held:

> "Once an application in due compliance of Section 8 of the Arbitration Act is filed, the approach of the civil court should be not to see whether the court has jurisdiction. It should be to see whether its jurisdiction has been ousted. There is a lot of difference between the two approaches. Once it is brought to the notice of the court that its jurisdiction has been taken away in terms of the procedure prescribed under a special statute, the civil court should first see whether there is ouster of jurisdiction in terms or compliance of the procedure under the special statute. The general law should yield to the special law - *generalia specialibus non derogant*. In such a situation, the approach shall not be to see whether there is still jurisdiction in the civil court under the general law. Such approaches

22 **AIR 2015 1303**

23 **(2009) 10 SCC 103**

> would only delay the resolution of disputes and complicate the redressal of grievances and of course unnecessarily increase the pendency in the court." (Id. at p. 15)

14 The position that emerges both before and after the decision in **N. Radhakrishnan** is that successive decisions of this Court have given effect to the binding precept incorporated in Section 8. Once there is an arbitration agreement between the parties, a judicial authority before whom an action is brought covering the subject matter of the arbitration agreement is under a positive obligation to refer parties to arbitration by enforcing the terms of the contract. There is no element of discretion left in the court or judicial authority to obviate the legislative mandate of compelling parties to seek recourse to arbitration. The judgment in **N. Radhakrishnan** has, however, been utilised by parties seeking a convenient ruse to avoid arbitration to raise a defence of fraud. First and foremost, it is necessary to emphasise that the judgment in **N. Radhakrishnan** does not subscribe to the broad proposition that a mere allegation of fraud is ground enough not to compel parties to abide by their agreement to refer disputes to arbitration. More often than not, a bogey of fraud is set forth if only to plead that the dispute cannot be arbitrated upon. To allow such a plea would be a plain misreading of the judgment in **N. Radhakrishnan**. As I have noted earlier, that was a case where the appellant who had filed an application under Section 8 faced with a suit on a dispute in partnership had raised serious issues of criminal wrongdoing, misappropriation

of funds and malpractice on the part of the respondent. It was in this background that this Court accepted the submission of the respondent that the arbitrator would not be competent to deal with matters "which involved an elaborate production of evidence **to establish the claims relating to fraud and criminal misappropriation**". Hence, it is necessary to emphasise that as a matter of first principle, this Court has not held that a mere allegation of fraud will exclude arbitrability. The burden must lie heavily on a party which avoids compliance with the obligation assumed by it to submit disputes to arbitration to establish the dispute is not arbitrable under the law for the time being in force. In each such case where an objection on the ground of fraud and criminal wrongdoing is raised, it is for the judicial authority to carefully sift through the materials for the purpose of determining whether the defence is merely a pretext to avoid arbitration. It is only where there is a serious issue of fraud involving criminal wrongdoing that the exception to arbitrability carved out in **N. Radhakrishnan** may come into existence. Allegations of fraud are not alien to ordinary civil courts. Generations of judges have dealt with such allegations in the context of civil and commercial disputes. If an allegation of fraud can be adjudicated upon in the course of a trial before an ordinary civil court, there is no reason or justification to exclude such disputes from the ambit and purview of a claim in arbitration. Parties who enter into commercial dealings and agree to a resolution of disputes by an arbitral forum exercise an option and express a choice of a preferred mode for the resolution of their

disputes. Parties in choosing arbitration place priority upon the speed, flexibility and expertise inherent in arbitral adjudication. Once parties have agreed to refer disputes to arbitration, the court must plainly discourage and discountenance litigative strategies designed to avoid recourse to arbitration. Any other approach would seriously place in uncertainty the institutional efficacy of arbitration. Such a consequence must be eschewed.

15 The position as it obtains in other jurisdictions which value arbitration as an effective form of alternate dispute resolution is no different. In the UK, Section 24(2) of the Arbitration Act, 1950 provided that the court could revoke the authority of a tribunal to deal with claims involving issues of fraud and determine those claims itself. The English Act of 1979 provided for a stay of proceedings involving allegations of fraud. However, under the English Arbitration Act, 1996, there is no such restriction and the arbitral tribunal has jurisdiction to consider and rule on issues of fraud. In **Fiona Trust and Holding Corporation** v. **Yuri Privalov**[24]**,** the Court of Appeal emphasised the need to make a fresh start in imparting business efficacy to arbitral agreements. The Court of Appeal held that:

> "For our part we consider that the time has now come for a line of some sort to be drawn and a fresh start made at any rate for cases arising in an international commercial context. Ordinary business men would be surprised at the nice distinctions drawn

24 [2007] 1 All E R (COMM) 891

> in the cases and the time taken up by argument in debating whether a particular case falls within one set of words or another very similar set of words. If business men go to the trouble of agreeing that their disputes be heard in the courts of a particular country or by a tribunal of their choice they do not expect (at any rate when they are making the contract in the first place) that time and expense will be taken in lengthy argument about the nature of particular causes of action and whether any particular cause of action comes within the meaning of the particular phrase they have chosen in their arbitration clause. If any business man did want to exclude disputes about the validity of a contract, it would be comparatively simple to say so. .. One of the reasons given in the cases for a liberal construction of an arbitration clause is the presumption in favour of one-stop arbitration. It is not to be expected that any commercial man would knowingly create a system which required that the court should first decide whether the contract should be rectified or avoided or rescinded (as the case might be) and then, if the contract is held to be valid, required the arbitrator to resolve the issues that have arisen. This is indeed a powerful reason for a liberal construction".

Arbitration must provide a one-stop forum for resolution of disputes. The Court of Appeal held that if arbitrators can decide whether a contract is void for initial illegality, there is no reason why they should not decide whether a contract is procured by bribery, just as much as they can decide whether a contract has been vitiated by misrepresentation or non-disclosure. The judgment of the Court of Appeal was affirmed by the House of Lords in **Premium Nafta Products Ltd. (20th Defendant)** v. **Fily Shipping Co. Ltd**[25]. The House of Lords held that claims of fraudulent inducement of the

25 [2007] UKHL 40

underlying contract (i.e. alleged bribery of one party's officer to accept uncommercial terms) did not impeach the arbitration clause contained within that contract. The Law Lords reasoned that "if (as in this case) the allegation is that the agent exceeded his authority by entering into a main agreement in terms which were not authorized or for improper reasons, that is not necessarily an attack on the arbitration agreement". They went on to conclude that, "the principle of separability…means that the invalidity or rescission of the main contract does not necessarily entail the invalidity or rescission of the arbitration agreement. The arbitration must be treated as a 'distinct agreement' and can be void or voidable only on grounds which relate directly to the arbitration agreement."

16 The basic principle which must guide judicial decision making is that arbitration is essentially a voluntary assumption of an obligation by contracting parties to resolve their disputes through a private tribunal. The intent of the parties is expressed in the terms of their agreement. Where commercial entities and persons of business enter into such dealings, they do so with a knowledge of the efficacy of the arbitral process. The commercial understanding is reflected in the terms of the agreement between the parties. The duty of the court is to impart to that commercial understanding a sense of business efficacy.

17 Lord Hoffmann, speaking for the House of Lords in **Premium Nafta Products**, placed the matter eloquently in the following observations:

> "In approaching the question of construction, it is therefore necessary to inquire into the purpose of the arbitration clause. As to this, I think there can be no doubt. The parties have entered into a relationship, an agreement or what is alleged to be an agreement or what appears on its face to be an agreement, which may give rise to disputes. They want those disputes decided by a tribunal which they have chosen, commonly on the grounds of such matters as its neutrality, expertise and privacy, the availability of legal services at the seat of the arbitration and the unobtrusive efficiency of its supervisory law. Particularly in the case of international contracts, they want a quick and efficient adjudication and do not want to take the risks of delay and, in too many cases, partiality, in proceedings before a national jurisdiction".

18 Lord Hoffmann held that if this is the purpose underlying an agreement to arbitrate, it would be inconceivable that parties would have intended that some, amongst their disputes should first be resolved by a court before they proceed to arbitration:

> "If one accepts that this is the purpose of an arbitration clause, its construction must be influenced by whether the parties, as rational businessmen, were likely to have intended that only some of the questions arising out of their relationship were to be submitted to arbitration and others were to be decided by national courts. Could they have intended that the question of whether the contract was repudiated should be decided by arbitration but the question of whether it was induced by misrepresentation should be decided by a court? If, as appears to be generally accepted, there is no rational basis upon which

> businessmen would be likely to wish to have questions of the validity or enforceability of the contract decided by one tribunal and questions about its performance decided by another, one would need to find very clear language before deciding that they must have had such an intention".

While affirming the judgment of the Court of Appeal, the House of Lords held:

> "13 In my opinion the construction of an arbitration clause should start from the assumption that the parties, as rational businessmen, are likely to have intended any dispute arising out of the relationship into which they have entered or purported to enter to be decided by the same tribunal. The clause should be construed in accordance with this presumption unless the language makes it clear that certain questions were intended to be excluded from arbitrator's jurisdiction. As Longmore LJ remarked, at para 17: "if any businessmen did want to exclude disputes about the validity of a contract, it would be comparatively easy to say so".... If one adopts this approach, the language of clause 41 of Shelltime 4 contains nothing to exclude disputes about the validity of the contract, whether on the grounds that it as procured by fraud, bribery, misrepresentation or anything else. In my opinion it therefore applies to the present dispute".

This principle should guide the approach when a defence of fraud is raised before a judicial authority to oppose a reference to arbitration. The arbitration agreement between the parties stands distinct from the contract in which it is contained, as a matter of law and consequence. Even the invalidity of the main agreement does not ipso jure result in the invalidity of the arbitration

agreement. Parties having agreed to refer disputes to arbitration, the plain meaning and effect of Section 8 must ensue.

19 In the United States, the Supreme Court in **Buckeye Check Cashing, Inc.** v. **Cardegna**[26], followed its earlier decisions in **Prima Paint Corp.** v. **Flood & Conklin Manufacturing Co**.[27], and in **Southland Corporation** v. **Keating**[28]. Justice Scalia, who delivered the judgment of the Supreme Court, summarized the position thus:-

> "Prima Paint and Southland answer the question presented here by establishing three propositions. First, as a matter of substantive federal arbitration law, an arbitration provision is severable from the remainder of the contract. Second, unless the challenge is to the arbitration clause itself, the issue of the contract's validity is considered by the arbitrator in the first instance. Third, this arbitration law applies in state as well as federal courts. The parties have not requested, and we do not undertake, reconsideration of those holdings. Applying them to this case, we conclude that because respondents challenge the Agreement, but not specifically its arbitration provisions, those provisions are enforceable apart from the remainder of the contract. The challenge should therefore be considered by an arbitrator, not a court".

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26 **546 U.S. 440 (U.S.S.Ct.2006)**

27 **388 US 395 (U.S. S.Ct. 1967)**

28 **465 U.S. 1 (1984)**

20 The Arbitration and Conciliation Act, 1996, should in my view be interpreted so as to bring in line the principles underlying its interpretation in a manner that is consistent with prevailing approaches in the common law world. Jurisprudence in India must evolve towards strengthening the institutional efficacy of arbitration. Deference to a forum chosen by parties as a complete remedy for resolving all their claims is but part of that evolution. Minimising the intervention of courts is again a recognition of the same principle.

21 Academic literature on the law of arbitration points in the same direction. In **Russell on Arbitration**[29], the doctrine of separability has been summarized in the following extract:

> "**The doctrine of separability**. An arbitration agreement specifies the means whereby some or all disputes under the contract in which it is contained are to be resolved. It is however separate from the underlying contract: "An arbitration clause in a commercial contract … is an agreement inside an agreement. The parties make their commercial bargain … but in addition agree on a private tribunal to resolve any issues that may arise between them." This is known as the doctrine of separability and s.7 of the Arbitration Act 1996 provides a statutory codification of the previous case law on this subject. As the House of Lords noted in Lesotho Highlands v Impreglio SpA:
>
> > "it is part of the very alphabet of arbitration law as explained in Harbour Assurance Co. (UK) Ltd. v Kansa General International Insurance Co. Ltd … and spelled out in s.7 of the Act, the

29 (24th Edition, 2015, para 2-007)

> arbitration agreement is a distinct and separable agreement from the underlying or principal contract"…..
>
> The Court of Appeal has confirmed that the doctrine of separability as it applies to arbitration agreements and jurisdiction clauses is uncontroversial also as a matter of European law".

Dealing with arbitrability of matters of fraud, the treatise contains the following statement of the legal position:

> "Fraud. Claims involving conduct amounting to fraud can be the subject matter of arbitration, as s.107(2) of the Arbitration Act makes clear. The Act expressly recognises that an arbitral tribunal may decide an issue of fraud, and the courts have acknowledged that an arbitrator has jurisdiction to decide allegations of bribery against a party to an arbitration agreement. Even in this context, however, an arbitral tribunal does not have jurisdiction to impose criminal sanctions on a party, even if bribery of a public officer is established; its power is limited to the civil consequences of that conduct".

Under Section 24(2) of the Arbitration Act, 1950, the court could revoke the authority of a tribunal to deal with claims involving issues of fraud and determine those claims itself. This provision has been repealed in Section 107(2) of the Arbitration Act, 1996.

22 Similarly, **Redfern and Hunter** on **International Arbitration**[30] contains the following statement of legal position in relation to arbitrability of matters involving fraud:-

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30 (6th Edition para 2.154)

> "(vi) Fraud
> Where allegations of fraud in the procurement or performance of a contract are alleged, there appears to be no reason for the arbitral tribunal to decline jurisdiction. Indeed, in the heat of battle, such allegations are frequently made, although much less frequently proven".

23 The legal position has been succinctly summarized in **International Commercial Arbitration** by **Gary B Born**[31] thus:

> "…..under most national arbitration regimes, claims that the parties' underlying contract (as distinguished from the parties' arbitration clause) was fraudulently induced have generally been held not to compromise the substantive validity of an arbitration clause included in the contract. The fact that one party may have fraudulently misrepresented the quality of its goods, services, or balance sheet generally does nothing to impeach the parties' agreed dispute resolution mechanism. As a consequence, only fraud or fraudulent inducement directed at the agreement to arbitrate will, as a substantive matter, impeach that agreement. These circumstances seldom arise: as a practical matter, it is relatively unusual that a party will seek to procure an agreement to arbitrate by fraud, even in those cases where it may have committed fraud in connection with the underlying commercial contract".

(See also in this context, **International Arbitration Law and Practice** by **Mauro Rubino-Sammartano**)[32]

24 For the above reasons, I agree with the eloquent judgment of my learned brother in coming to the conclusion that a mere allegation of fraud in the

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31 (2nd Edition Vol. I, P.846)

32 (2nd Edition p.179)

present case was not sufficient to detract from the obligation of the parties to submit their disputes to arbitration. I also agree with the directions issued. A fresh line must be drawn to ensure the fulfilment of the intent of Parliament in enacting the Act of 1996 and towards supporting commercial understandings grounded in the faith in arbitration.

.....J
[Dr D Y CHANDRACHUD]

New Delhi
October 04, 2016