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(2023) 8 Supreme Court Cases 226

3J

(BEFORE DR D.Y. CHANDRACHUD, C.J. AND P.S. NARASIMHA AND J.B. PARDIWALA, JJ.)

GLOCK ASIA-PACIFIC LIMITED .. Petitioner;

Versus

UNION OF INDIA .. Respondent.

Arbitration Petition No. 51 of 2022, decided on May 19, 2023

A. **Arbitration and Conciliation Act, 1996 — S. 12(5) r/w Sch. VII Para 1 and S. 11(6) — Appointment of an impartial and independent adjudicator in contracts involving State — Necessity of — Emphasised**

— Arbitration clause enabling a serving employee of the Union of India (a party to the contract) to nominate another serving employee of the Union of India as the sole arbitrator — Held, violative of S. 12(5) r/w Sch. VII Para 1 — Case of serving employee and that of a retired employee — Distinguished between — Non obstante clause in S. 12(5) — Relevance of — Law clarified

— Ministry of Home Affairs was a party to the contract where the arbitration clause enabled the Secretary representing the Ministry to appoint an officer in the Ministry of Law as the arbitrator — Whilst distinguishing the present case from the cases dealing with appointment of a retired employee to act as an arbitrator, held, the arbitration clause which authorises the Secretary, Ministry of Home Affairs, whose relationship with the Union of India is that of an employee, to nominate an officer of the Ministry of Law and Justice to act as a sole arbitrator, falls within the expressly ineligible category provided in Sch. VII Para 1 r/w S. 12(5)

— In the present case, application under S. 11(6) allowed and a former Judge of Supreme Court appointed as the sole arbitrator to adjudicate upon the disputes arising under and in connection with the conditions of tender entered into between the parties (Paras 17 to 24)

B. **Arbitration and Conciliation Act, 1996 — S. 12(5) r/w Sch. VII Para 1 — Contract entered into in the name of the President of India — Held, not immune to restriction/bar placed under S. 12(5) — General provisions of law — Applicability of, to such contracts — Law clarified**

— Held, Art. 299 of the Constitution only lays down the formality that is necessary to bind the Government with contractual liability and does not lay down the substantial law relating to the contractual liability of the Government, which is to be found in the general laws of the land — Further, it is for this reason that, even though a contract may be formally valid under Art. 299 of the Constitution, it may nevertheless fail to bind the Government if it is void or unenforceable under the general provisions of law

— Held, the contract entered into in the name of the President of India, cannot and will not create an immunity against the application of any statutory prescription imposing conditions on parties to an agreement, when the Government chooses to enter into a contract

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— In the present case, the submission that contracts entered into by the Union of India in the name of the President of India are immune from provisions that protect against conflict of interest of a party to a contract, under S. 12(5), rejected — Constitution of India, Art. 299 (Paras 12 to 16)

The Ministry of Home Affairs (Procurement Division) ("the respondent") floated a single party tender on 2-2-2011 for supply of 31,756 Glock Pistols. The bid was confirmed in favour of the applicant and a acceptance of tender was issued by the respondent on 31-3-2011.

Disputes having arisen, the applicant issued a notice invoking arbitration on 20-7-2022, and nominated a retired Judge of the High Court of Delhi as the sole arbitrator. The respondent was called upon to accept the nomination within 15 days. Replying to the notice invoking arbitration, the respondent by a letter dated 3-10-2022, stated that the nomination was contrary to Clause 28 of the conditions of tender, as per which disputes are to be referred to arbitration by an officer in the Ministry of Law, appointed by the Secretary of Ministry of Home Affairs.

The issues involved in this matter were:

(*1*) Whether the respondent, Union of India, being a party to the agreement, appointing its own employee, an officer in the Ministry of Law, as the sole arbitrator would conflict with the mandate of Section 12(5) read with Schedule VII Para 1 of the Arbitration and Conciliation Act, 1996 ("the Act")?

(*2*) Whether contracts entered into by the Union of India in the name of the President of India are immune from provisions that protect against conflict of interest of a party to a contract, under Section 12(5) of the Act?

Allowing the present application under Section 11(6), the Supreme Court

Held :

Re: Submission regarding contracts expressed in the name of the President of India

Article 299 of the Constitution provides that all contracts made in exercise of the executive power of the Union shall be expressed to be made in the name of the President. The phrase "expressed to be made" and the word "executed" are intended to mean that there must be a deed or contract, in writing, and executed by a person duly authorised by the President or the Governor in that behalf. (Para 12)

The rationale of Article 299(1) is that there must be a definite procedure according to which contracts must be made by the agents of the Government in order to bind the Government, otherwise public funds may deplete by unauthorised or illegitimate contracts. It implies that contracts not couched in the particular form stipulated by Article 299(1) of the Constitution cannot be enforced at the instance of any contracting party. (Para 13)

It must be emphasised that Article 299 only lays down the formality that is necessary to bind the Government with contractual liability. It is important to note that Article 299 does not lay down the substantial law relating to the contractual liability of the Government, which is to be found in the general laws of the land. It is for this reason that, even though a contract may be formally valid under Article

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299, it may nevertheless fail to bind the Government if it is void or unenforceable under the general provisions of law. (Para 14)

Chatturbhuj Vithaldas Jasani v. *Moreshwar Parashram*, (1954) 1 SCC 214; *K.P. Chowdhry* v. *State of M.P.*, 1966 SCC OnLine SC 21; *Bhikraj Jaipuria* v. *Union of India*, 1961 SCC OnLine SC 34; *Mulamchand* v. *State of M.P.*, 1968 SCC OnLine SC 21, *followed*

D.D. Basu: *Constitution of India* (Vol. 3), 13601-13619, *referred to*

A contract entered into in the name of the President of India, cannot and will not create an immunity against the application of any statutory prescription imposing conditions on parties to an agreement, when the Government chooses to enter into a contract. (Para 15)

Re: Conflict of the arbitration clause with Section 12(5) read with Schedule VII Para 1 of the Act

The arbitration clause enables the Secretary, Ministry of Home Affairs, to appoint an arbitrator for the resolution of disputes arising out of this contract. The Ministry of Home Affairs is a party to the contract. The arbitration clause enables the Secretary representing the Ministry to appoint an officer in the Ministry of Law as the arbitrator. In other words, the proposed arbitrator would be an employee of the Ministry of Law and Justice, Government of India, and at the same time, the appointing authority, the Secretary of the Ministry of Home Affairs, is also an employee of the Government of India. (Para 17)

State of Assam v. *Kanak Chandra Dutta*, 1966 SCC OnLine SC 9, *considered*

The 246th Law Commission Report which reflected on the issue of contracts with State entities and observed that when the party appointing an arbitrator is the State, the duty to appoint an impartial and independent adjudicator is even more onerous. (Para 18)

State of Odisha v. *Gangaram Chhapolia*, (1984) 3 SCC 627; *State of T.N.* v. *Munuswamy Mudaliar*, 1988 Supp SCC 651; *International Airports Authority* v. *K.D. Bali*, (1988) 2 SCC 360; *S. Rajan* v. *State of Kerala*, (1992) 3 SCC 608; *Indian Drugs & Pharmaceuticals Ltd.* v. *Indo Swiss Synthetics Gem Mfg. Co. Ltd.*, (1996) 1 SCC 54; *Union of India* v. *M.P. Gupta*, (2004) 10 SCC 504; *ACE Pipeline Contracts (P) Ltd.* v. *Bharat Petroleum Corpn. Ltd.*, (2007) 5 SCC 304; *Indian Oil Corpn. Ltd.* v. *Raja Transport (P) Ltd.*, (2009) 8 SCC 520 : (2009) 3 SCC (Civ) 460; *Denel (Pty) Ltd.* v. *Union of India*, (2012) 2 SCC 759 : (2012) 2 SCC (Civ) 37; *Bipromasz Bipron Trading SA* v. *Bharat Electronics Ltd.*, (2012) 6 SCC 384 : (2012) 3 SCC (Civ) 702, *cited*

Following the recommendation of the Law Commission, sub-section (5) to Section 12 was inserted to the Act with effect from 23-10-2015. As the statutory mandate of Section 12(5) of the Act is to apply "*notwithstanding any prior agreement*", Clause 28 of the Agreement (Conditions of Tender) falls foul of Schedule VII Para 1 to the Act. (Para 19)

In a case where only one party has a right to appoint a sole arbitrator, its choice will always have an element of exclusivity in determining or charting the course for dispute resolution. Naturally, the person who has an interest in the outcome or decision of the dispute must not have the power to appoint a sole arbitrator. (Para 20)

Perkins Eastman Architects DPC v. *HSCC (India) Ltd.*, (2020) 20 SCC 760; *TRF Ltd.* v. *Energo Engg. Projects Ltd.*, (2017) 8 SCC 377 : (2017) 4 SCC (Civ) 72, *affirmed*

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The arbitration clause which authorises the Secretary, Ministry of Home Affairs, whose relationship with the Union of India is that of an employee, to nominate an officer of the Ministry of Law and Justice to act as a sole arbitrator, clearly falls within the expressly *ineligible category* provided in Schedule VII Para 1, read with Section 12(5) of the Act. (Para 21)

Voestalpine Schienen GmbH v. *Delhi Metro Rail Corpn. Ltd.*, (2017) 4 SCC 665 : (2017) 2 SCC (Civ) 607; *Central Organisation for Railway Electrification* v. *ECI-SPIC-SMO-MCML (JV)*, (2020) 14 SCC 712, *distinguished*

Union of India v. *Tantia Constructions Ltd.*, (2023) 12 SCC 330 : 2021 SCC OnLine SC 271; *JSW Steel Ltd.* v. *Railways*, 2022 SCC OnLine SC 1973, *referred to*

VN-D/70080/CV

Advocates who appeared in this case :

Ramakrishnan Viraraghavan, Senior Advocate [Shyam D. Nandan (Advocate-on-Record), Advocate], for the Petitioner;

Tushar Mehta, Solicitor General, Ms Aishwarya Bhati, Additional Solicitor General [Rajat Nair, Saurav Roy, Ms Deepabali Dutta, Ms Shivika Mehra and Arvind Kr. Sharma (Advocate-on-Record), Advocates], for the Respondent.

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1. (2023) 12 SCC 330 : 2021 SCC OnLine SC 271, *Union of India* v. *Tantia Constructions Ltd.* 239*a-b*
2. 2022 SCC OnLine SC 1973, *JSW Steel Ltd.* v. *Railways* 239*a-b*
3. (2020) 20 SCC 760, *Perkins Eastman Architects DPC* v. *HSCC (India) Ltd.* 232*a-b*, 232*b-c*, 232*c*, 236*d*, 237*e-f*
4. (2020) 14 SCC 712, *Central Organisation for Railway Electrification* v. *ECI-SPIC-SMO-MCML (JV)* 232*d*, 237*c-d*, 237*d*, 237*f*, 237*f-g*, 238*a*, 239*a*, 239*a-b*
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7. (2012) 6 SCC 384 : (2012) 3 SCC (Civ) 702, *Bipromasz Bipron Trading SA* v. *Bharat Electronics Ltd.* 235*e*
8. (2012) 2 SCC 759 : (2012) 2 SCC (Civ) 37, *Denel (Pty) Ltd.* v. *Union of India* 235*d-e*
9. (2009) 8 SCC 520 : (2009) 3 SCC (Civ) 460, *Indian Oil Corpn. Ltd.* v. *Raja Transport (P) Ltd.* 232*c*, 235*d*
10. (2007) 5 SCC 304, *ACE Pipeline Contracts (P) Ltd.* v. *Bharat Petroleum Corpn. Ltd.* 235*c-d*
11. (2004) 10 SCC 504, *Union of India* v. *M.P. Gupta* 235*c*
12. (1996) 1 SCC 54, *Indian Drugs & Pharmaceuticals Ltd.* v. *Indo Swiss Synthetics Gem Mfg. Co. Ltd.* 235*c*
13. (1992) 3 SCC 608, *S. Rajan* v. *State of Kerala* 235*c*
14. (1988) 2 SCC 360, *International Airports Authority* v. *K.D. Bali* 235*b-c*
15. 1988 Supp SCC 651, *State of T.N.* v. *Munuswamy Mudaliar* 235*b-c*
16. (1984) 3 SCC 627, *State of Odisha* v. *Gangaram Chhapolia* 235*b-c*

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17. 1968 SCC OnLine SC 21, *Mulamchand* v. *State of M.P.* 234*a*
18. 1966 SCC OnLine SC 21, *K.P. Chowdhry* v. *State of M.P.* 234*a*
19. 1966 SCC OnLine SC 9, *State of Assam* v. *Kanak Chandra Dutta* 234*e-f*
20. 1961 SCC OnLine SC 34, *Bhikraj Jaipuria* v. *Union of India* 234*a*
21. (1954) 1 SCC 214, *Chatturbhuj Vithaldas Jasani* v. *Moreshwar Parashram* 233*d*, 234*a*

The Judgment of the Court was delivered by

PAMIDIGHANTAM SRI NARASIMHA, J.— This is an application under Section 11(6) of the Arbitration and Conciliation Act, 1996 (hereinafter referred to as "the Act") for the appointment of a sole arbitrator by Glock Asia-Pacific Ltd. (hereinafter referred to as "the applicant").

Facts

2. The Ministry of Home Affairs (Procurement Division) (hereinafter referred to as "the respondent") floated a single party tender on 2-2-2011 for supply of 31,756 Glock Pistols. The bid was confirmed in favour of the applicant and a acceptance of tender was issued by the respondent on 31-3-2011. Clause 6[1] of the acceptance of tender, required the petitioner to submit a performance bond of 10% of the value of the contract, being USD 13,29,093. The applicant furnished the performance bank guarantee (hereinafter referred to as "PBG") on 24-8-2011 and proceeded to perform its contractual obligations and in fact, by 6-8-2012 delivered the entire supply under the contract. The respondent accepted the consignment and paid the entire consideration by 11-11-2012.

3. The PBG which was issued on 24-8-2011 was extended from time to time during the subsistence of the contract and also thereafter till 2021 i.e. for nine years after the completion of the delivery and final payment under the contract. On 31-5-2021, the applicant informed the respondent that the PBG will not be extended any further. The respondent immediately invoked the PBG for INR 9,64,42,738, citing Clauses 11 and 18(*c*) of Schedule II of the acceptance of tender.

1 "**6. *Performance Security Deposit***— You will submit performance bond of 10% of value of contract i.e. US $13,29,093 (US dollars thirteen lakhs twenty-nine thousand and ninety-three only) in the shape of bank guarantee in the required pro forma in favour of Joint Secretary (Police Modernisation), Ministry of Home Affairs, Jaisalmer House, New Delhi within 30 days hereof i.e. by 30-4-2011. The performance guarantee will remain valid till two months after the expiry of warranty period, which will be 18 months from the date of acceptance stores at the consignee location. If necessary, firm on their own will have to direct their bankers to extend the performance bond to remain valid till two months after warranty period. Where the performance bank guarantee is obtained from a foreign bank, it shall be got confirmed by a scheduled Indian Bank and will be governed by Indian Laws and be subject to the jurisdiction of Courts of the place of issue of acceptance of tender ("A/T") i.e Delhi."

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4. These clauses, which provide for guarantee and warranty, are as follows:

"**Clause 11.** ***Guarantee/Warranty***: 40,000 rounds for pistol and ors. 18 months from the date of acceptance of EQPT/Stores in good condition at consignee location in India.

Clause 18(c). ***Warranty***: the supplier furnishes his warranty that the goods supplied under the contract on you, on use of the incorporate all recent improvement in design and material. The supplier shall for the warranty the goods supplied under this contract shall have no defect arising from design, material of workmanship or from any act or commission of the supplier normal use of the supplied goods in the condition obtained in the country of final destination. Warranty shall remain valid up to 40,000 rounds of pistol and 18 months from other items from the date of acceptance of stores. The consignee shall promptly notify the supplier in writing of any claim arising under this warranty. Upon receipt of such notice the supplier having been notified failed to remedy the defects within the warranty period prescribed in this clause, the purchaser may proceed to take such remedial action as may be necessary at the suppliers risk and expense and without prejudice to any other rights which the purchaser may have under the contract. The manufacturer will be required by the indenter on actual price basis. Warranty support will include installation and commissioning of equipment free of charge. Operational training of the users personnel free of cost at the site of installation and repair of the equipment when necessary free of cost during the warranty period."

5. The applicant issued a notice invoking arbitration on 20-7-2022, and nominated a retired Judge of the High Court of Delhi as the sole arbitrator. The respondent was called upon to accept the nomination within 15 days. Replying to the notice invoking arbitration, the respondent by a letter dated 3-10-2022, stated that the nomination was contrary to Clause 28 of the conditions of tender, as per which disputes are to be referred to arbitration by an officer in the Ministry of Law, appointed by the Secretary of Ministry of Home Affairs.

6. Clause 28 is as under:

"**28.** ***Arbitration***

In the event of any question, dispute or difference arising under these conditions or any special conditions of contract, or in connection with this contract (except as to any matters the decision of which is specially provided for by these or the special conditions) the same shall be referred to *the sole arbitration of an officer in the Min. of Law, appointed to be the arbitrator by the Secretary, Ministry of Home Affairs*. It will be no objection that the arbitrator is a government servant that he had to deal with the matters to which the contract relates or that in the course of his duties as a government servant he has expressed views on all or any of the matters in dispute or difference. The award of the arbitrator shall be final and binding on the parties to this contract…." (emphasis supplied)

7. It is in the abovereferred context that the applicant, being a foreign company, filed the present application under Section 11(6) of the Act before this Court.

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Submissions

8. Mr Ramakrishnan Viraraghavan, learned Senior Advocate, along with Mr Shayam D. Nandan, AOR appearing for the applicant, submitted that appointment of the sole arbitrator as per the respondent's letter dated 3-10-2022 would be contrary to Section 12(5) of the Act. For this purpose, he also relied on the judgment of this Court in *Perkins Eastman Architects DPC* v. *HSCC (India) Ltd.*[2] The objection is simply that the respondent, Union of India, being a party to the agreement, appointing its own employee, an officer in the Ministry of Law, as the sole arbitrator would conflict with the mandate of Section 12(5) of the Act.

9. Ms Aishwarya Bhati, learned Additional Solicitor General appearing for the respondent, submitted that the judgment in *Perkins*[2] would have no application to the facts of the present case. She would point out that the contract in the present case, unlike in *Perkins*[2], is in the name of the President of India, and that is a clear point of distinction. The learned ASG also relied on *Indian Oil Corpn. Ltd.* v. *Raja Transport (P) Ltd.*[3] to contend that once a party enters into an agreement for the appointment of a person as an arbitrator, it cannot simply opt out of the arbitration clause. In the alternative, the ASG also relied on the decision of this Court in *Central Organisation for Railway Electrification* v. *ECI-SPIC-SMO-MCML (JV)*[4], where appointment of a panel of arbitrators by the Ministry of Railways was held to be valid. She would, therefore, contend that the power to nominate an officer in the Ministry of Law is not in conflict with Section 12(5) of the Act.

Analysis

10. As the objection about appointment of the arbitrator as per Clause 28 of the conditions of tender is based on the statutory prohibition under Section 12(5) of the Act, we will reproduce relevant part of the section for ready reference:

> "**12.** ***Grounds of challenge***.—(1) When a person is approached in connection with his possible appointment as an arbitrator, he shall disclose in writing any circumstances—
>
> * * *
>
> (2)-(4) * * *
>
> (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." (emphasis supplied)

2 (2020) 20 SCC 760
3 (2009) 8 SCC 520 : (2009) 3 SCC (Civ) 460
4 (2020) 14 SCC 712

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11. The category of relationship relevant for our purposes as provided in the Seventh Schedule to the Act is as under:

"**THE SEVENTH SCHEDULE**

Arbitrator's relationship with the parties or counsel;

1. The arbitrator is an employee, consultant, advisor or has any other past or present business relationship with a party."

Re: Submission regarding contracts expressed in the name of the President of India

12. We will first deal with the submission of the learned ASG, Ms Bhati that the contract in the present case stands on a different footing as it is entered into in the name of the President of India. Article 299 of the Constitution of India[5] provides that all contracts made in exercise of the executive power of the Union shall be expressed to be made in the name of the President. The phrase "expressed to be made" and the word "executed" are intended to mean that there must be a deed or contract, in writing, and executed by a person duly authorised by the President or the Governor in that behalf.

13. The rationale of Article 299(1), as explained in *Chatturbhuj Vithaldas Jasani* v. *Moreshwar Parashram*[6] is that there must be a definite procedure according to which contracts must be made by the agents of the Government in order to bind the Government, otherwise public funds may deplete by unauthorised or illegitimate contracts. It implies that contracts not couched in the particular form stipulated by Article 299(1) of the Constitution cannot be enforced at the instance of any contracting party.

14. It must be emphasised that Article 299 only lays down the formality that is necessary to bind the Government with contractual liability. It is important to note that Article 299 does not lay down the substantial law relating to the contractual liability of the Government, which is to be found in the general laws of the land. It is for this reason that, even though a contract may be formally

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5 "**299.** ***Contracts***.—(1) All contracts made in the exercise of the executive power of the Union or of a State shall be *expressed to be made by the President*, or by the Governor of the State, as the case may be, and all such contracts and all assurances of property made in the exercise of that power shall be executed on behalf of the President or the Governor by such persons and in such manner as he may direct or authorise.

(2) Neither the President nor the Governor shall be personally liable in respect of any contract or assurance made or executed for the purposes of this Constitution, or for the purposes of any enactment relating to the Government of India heretofore in force, nor shall any person making or executing any such contract or assurance on behalf of any of them be personally liable in respect thereof." (emphasis supplied)

6 (1954) 1 SCC 214 : 1954 SCR 817

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valid under Article 299, it may nevertheless fail to bind the Government if it is void or unenforceable under the general provisions of law.[7]

15. Having considered the purpose and object of Article 299, we are of the clear opinion that a contract entered into in the name of the President of India, cannot and will not create an immunity against the application of any statutory prescription imposing conditions on parties to an agreement, when the Government chooses to enter into a contract. We are unable to trace any immunity arising out of Article 299, to support the contention that for contracts *expressed to be made by the President of India*, the ineligibility of appointment as an arbitrator as contemplated under Section 12(5) of the Act, read with Schedule VII, will be inapplicable.

16. We have no hesitation in rejecting the submission of the learned ASG that the contracts entered into by the Union of India in the name of the President of India are immune from the provisions that protect against conflict of interest of a party to a contract, under Section 12(5) of the Act.

Re: Conflict of the arbitration clause with Section 12(5) read with Schedule VII Para 1 of the Act

17. The tender Notice dated 2-2-2011 was issued by the Government of India, Ministry of Home Affairs for the purchase of Glock pistols. The applicant's bid was accepted on 31-3-2011 as per the *Terms and Conditions* contained in Tender No. D/21013/30/3218/2-11-2011/PW 3. The said *Terms and Conditions* specifically provided for Arbitration as per Clause 28 of the Schedule appended to the Tender. The arbitration clause enables the Secretary, Ministry of Home Affairs, to appoint an arbitrator for the resolution of disputes arising out of this contract. The Ministry of Home Affairs is a party to the contract. The arbitration clause enables the Secretary representing the Ministry to appoint an officer in the Ministry of Law as the arbitrator. In other words, the proposed arbitrator would be an employee of the Ministry of Law and Justice, Government of India, and at the same time, the appointing authority, the Secretary of the Ministry of Home Affairs, is also an employee of the Government of India.[8]

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7 See *Chatturbhuj Vithaldas Jasani* v. *Moreshwar Parashram*, (1954) 1 SCC 214 : 1954 SCR 817; *K.P. Chowdhry* v. *State of M.P.*, 1966 SCC OnLine SC 21 : (1966) 3 SCR 919 : AIR 1967 SC 203; *Bhikraj Jaipuria* v. *Union of India*, 1961 SCC OnLine SC 34 : (1962) 2 SCR 880 : AIR 1962 SC 113; *Mulamchand* v. *State of M.P.*, 1968 SCC OnLine SC 21 : (1968) 3 SCR 214 : AIR 1968 SC 1218; Also see, D.D. Basu, *Constitution of India* (Vol. 3), 13601-13619.

8 In *State of Assam* v. *Kanak Chandra Dutta*, 1966 SCC OnLine SC 9 : (1967) 1 SCR 679 : AIR 1967 SC 884, this Court held that: (AIR p. 886, para 9)

> "*9.* … A person holding a post under a State is a person serving or employed under the State. See the marginal notes to Articles 309, 310 and 311. The heading and the sub-heading of Part XIV and Chapter I emphasise the element of service. There is a relationship of master and servant between the State and a person holding a post under it. The existence of this relationship is indicated by the State's right to select and appoint the holder of the post, its right to suspend and dismiss him, its right to control the manner and method of his doing the work and the payment by it of his wages or remuneration."

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18. In this very context, we can beneficially refer to the recommendation of the 246th Law Commission Report which reflected on the issue of contracts with State entities and observed that when the party appointing an arbitrator is the State, the duty to appoint an impartial and independent adjudicator is even more onerous. Their deliberations and recommendations, which led to the introduction of Section 12(5) with the Seventh Schedule in the Act, are extracted as follows:

> "56. The limits of this provision have been tested in the Indian Supreme Court in the context of *contracts with State entities naming particular persons/designations* (associated with that entity) *as a potential arbitrator*. It appears to be settled by a series of decisions of the Supreme Court [See *State of Odisha* v. *Gangaram Chhapolia*[9]; *State of T.N.* v. *Munuswamy Mudaliar*[10]; *International Airports Authority* v. *K.D. Bali*[11]; *S. Rajan* v. *State of Kerala*[12]; *Indian Drugs & Pharmaceuticals Ltd.* v. *Indo Swiss Synthetics Gem Mfg. Co. Ltd.*[13]; *Union of India* v. *M.P. Gupta*[14] and *ACE Pipeline Contracts (P) Ltd.* v. *Bharat Petroleum Corpn. Ltd.*[15]] that arbitration agreements in government contracts which provide for arbitration by a serving employee of the department, are valid and enforceable. While the Supreme Court, in *Indian Oil Corpn. Ltd.* v. *Raja Transport (P) Ltd.*[3] carved out a minor exception in situations when the arbitrator 'was the controlling or dealing authority in regard to the subject contract or if he is a direct subordinate (as contrasted from an officer of an inferior rank in some other department) to the officer whose decision is the subject-matter of the dispute', and this exception was used by the Supreme Court in *Denel (Pty) Ltd.* v. *Union of India*[16] and *Bipromasz Bipron Trading SA* v. *Bharat Electronics Ltd.*[17], to appoint an independent arbitrator under Section 11, this is not enough.
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> 57. The balance between procedural fairness and binding nature of these contracts, appears to have been tilted in favour of the latter by the Supreme Court, and the Commission believes the present position of law is far from satisfactory. Since the principles of impartiality and independence cannot be discarded at any stage of the proceedings, specifically at the stage of constitution of the Arbitral Tribunal, it would be incongruous to say that party autonomy can be exercised in complete disregard of these principles — even if the same has been agreed prior to the disputes having arisen between the parties. There are certain minimum levels of independence and impartiality that should be required of the arbitral process regardless

9 (1984) 3 SCC 627
10 1988 Supp SCC 651
11 (1988) 2 SCC 360
12 (1992) 3 SCC 608
13 (1996) 1 SCC 54
14 (2004) 10 SCC 504
15 (2007) 5 SCC 304
3 (2009) 8 SCC 520 : (2009) 3 SCC (Civ) 460
16 (2012) 2 SCC 759 : (2012) 2 SCC (Civ) 37
17 (2012) 6 SCC 384 : (2012) 3 SCC (Civ) 702

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of the parties' apparent agreement. A sensible law cannot, for instance, permit appointment of an arbitrator who is himself a party to the dispute, or who is employed by (or similarly dependent on) one party, even if this is what the parties agreed. The Commission hastens to add that Mr P.K. Malhotra, the ex officio member of the Law Commission suggested having an exception for the State, and allow State parties to appoint employee arbitrators. *The Commission is of the opinion that, on this issue, there cannot be any distinction between State and non-State parties. The concept of party autonomy cannot be stretched to a point where it negates the very basis of having impartial and independent adjudicators for resolution of disputes. In fact, when the party appointing an adjudicator is the State, the duty to appoint an impartial and independent adjudicator is that much more onerous — and the right to natural justice cannot be said to have been waived only on the basis of a "prior" agreement between the parties at the time of the contract and before arising of the disputes*."

(emphasis supplied)

19. Following the recommendation of the Law Commission, sub-section (5) to Section 12 was inserted to the Act with effect from 23-10-2015. As the statutory mandate of Section 12(5) of the Act is to apply "*notwithstanding any prior agreement*", Clause 28 of the Agreement (Conditions of Tender) falls foul of Schedule VII Para 1 to the Act.

20. In *Perkins*[2], this Court held that any person who has an interest in the outcome of the dispute would be ineligible to be an arbitrator. Naturally, such a person should not have the power to appoint a sole arbitrator. The relevant portion of this judgment is as under: (SCC p. 779, para 21)

"*21.* But, in our view that has to be the logical deduction from *TRF Ltd.*[18] Para 50 of the decision shows that this Court was concerned with the issue, 'whether the Managing Director, after becoming ineligible by operation of law, is he still eligible to nominate an arbitrator'. *The ineligibility referred to therein, was as a result of operation of law, in that a person having an interest in the dispute or in the outcome or decision thereof, must not only be ineligible to act as an arbitrator but must also not be eligible to appoint anyone else 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*. The next sentences in the paragraph, further show that cases where both the parties could nominate respective arbitrators of their choice were found to be completely a different situation. The reason is clear that whatever advantage a party may derive by nominating an arbitrator of its choice would get counter-balanced by equal power with the other party. *But, in a case where only one party has a right to appoint a sole arbitrator, its choice will always have an element of exclusivity in determining or charting the course for dispute resolution. Naturally, the person who has an*

2 *Perkins Eastman Architects DPC* v. *HSCC (India) Ltd.*, (2020) 20 SCC 760
18 *TRF Ltd.* v. *Energo Engg. Projects Ltd.*, (2017) 8 SCC 377 : (2017) 4 SCC (Civ) 72

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interest in the outcome or decision of the dispute must not have the power to appoint a sole arbitrator. That has to be taken as the essence of the amendments brought in by the Arbitration and Conciliation (Amendment) Act, 2015 (3 of 2016) and recognised by the decision of this Court in *TRF*[18]." (emphasis supplied)

21. In conclusion, the arbitration clause which authorises the Secretary, Ministry of Home Affairs, whose relationship with the Union of India is that of an employee, to nominate an officer of the Ministry of Law and Justice to act as a sole arbitrator, clearly falls within the expressly *ineligible category* provided in Schedule VII Para 1, read with Section 12(5) of the Act. As the grounds of challenge to the appointment of an arbitrator under Section 12(5) of the Act operate *notwithstanding any prior agreement to the contrary*, we cannot give effect to the appointment of an officer of the Ministry of Law and Justice as an arbitrator. The submission of the learned ASG in favour of such an appointment is therefore rejected.

***Re: Reliance on the decision in Central Organisation for Railway Electrification*[4]**

22. We will now deal with the last limb of the learned ASG's submissions, which relates to the precedent of *Central Organisation for Railway Electrification*[4]. In this case, Clause 64(3)(*b*) provided for the constitution of an Arbitral Tribunal consisting of three members. The appointment procedure contemplated was such that the General Manager of the appellant was required to nominate the panel of four retired railway officers, out of which the respondent Contractor had to select two names. The General Manager was required to appoint at least one out of the selected officers as the contractor's nominee arbitrator(s), and unilaterally appoint the remaining arbitrators as well as the Presiding Officer to the Tribunal. The decision of *Perkins*[2] was not applicable therein as the contract contemplated a three-member Arbitral Tribunal, while *Perkins*[2] applies to cases of unilateral appointment of sole arbitrators. Further, the Court noted that, "*absolutely, there is no bar under Section 12(5) of the Arbitration and Conciliation (Amendment) Act, 2015 for appointment of a retired employee to act as an arbitrator*"[4]. The Court in *Central Organisation for Railway Electrification*[4] also relied on the principle elucidated in *Voestalpine Schienen GmbH* v. *Delhi Metro Rail Corpn. Ltd.*[19] wherein DMRC nominated a five-member panel comprising names of employees of Railways, Central Public Works Department or public sector undertakings and the Court upheld the nomination inter alia noting that empanelling of such retired persons was intended to utilise their technical

18 *TRF Ltd.* v. *Energo Engg. Projects Ltd.*, (2017) 8 SCC 377 : (2017) 4 SCC (Civ) 72
4 *Central Organisation for Railway Electrification* v. *ECI-SPIC-SMO-MCML (JV)*, (2020) 14 SCC 712
2 *Perkins Eastman Architects DPC* v. *HSCC (India) Ltd.*, (2020) 20 SCC 760
19 (2017) 4 SCC 665 : (2017) 2 SCC (Civ) 607

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expertise.[20] In *Central Organisation for Railway Electrification*[4] this Court relied on the aforementioned judgment to state that: (*Central Organisation for Railway Electrification case*[4], SCC p. 726, para 27)

> "*27.* … As held in *Voestalpine Schienen GmbH*[19], *the very reason for empanelling the retired railway officers is to ensure that the technical aspects of the dispute are suitably resolved by utilising their expertise when they act as arbitrators. Merely because the panel of the arbitrators are the retired employees who have worked in the Railways, it does not make them ineligible to act as the arbitrators*." (emphasis supplied)

23. In contrast, the arbitration clause in the present case enables a serving employee of the Union of India, a party to the contract, to nominate a serving employee of the Union of India as the sole arbitrator. Such an authorisation

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20 *Id*, paras 24 and 26: [*Voestalpine Schienen GmbH* v. *Delhi Metro Rail Corpn. Ltd.*, (2017) 4 SCC 665 at pp. 688-89]

> "*24.* … They cannot be treated as employee or consultant or adviser of the respondent DMRC. If this contention of the petitioner is accepted, then no person who had earlier worked in any capacity with the Central Government or other autonomous or public sector undertakings, would be eligible to act as an arbitrator *even when he is not even remotely connected with the party in question, like DMRC in this case*. The amended provision puts an embargo on a person to act as an arbitrator, who is the employee of the party to the dispute. It also deprives a person to act as an arbitrator if he had been the consultant or the advisor or had any past or present business relationship with DMRC. No such case is made out by the petitioner.
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> *26.* It cannot be said that *simply because the person is a retired officer who retired from the Government or other statutory corporation or public sector undertaking and had no connection with DMRC* (the party in dispute), he would be treated as ineligible to act as an arbitrator. Had this been the intention of the legislature, the Seventh Schedule would have covered such persons as well. Bias or even real likelihood of bias cannot be attributed to such highly qualified and experienced persons, simply on the ground that they served the Central Government or PSUs, even when they had no connection with DMRC. *The very reason for empanelling these persons is to ensure that technical aspects of the dispute are suitably resolved by utilising their expertise when they act as arbitrators*. It may also be mentioned herein that the Law Commission had proposed the incorporation of the Schedule which was drawn from the red and orange list of IBA guidelines on conflict of interest in international arbitration with the observation that the same would be treated as the guide 'to determine whether circumstances exist which give rise to such justifiable doubts'. Such persons do not get covered by red or orange list of IBA guidelines either." (emphasis supplied)

4 *Central Organisation for Railway Electrification* v. *ECI-SPIC-SMO-MCML (JV)*, (2020) 14 SCC 712

19 *Voestalpine Schienen GmbH* v. *Delhi Metro Rail Corpn. Ltd.*, (2017) 4 SCC 665 : (2017) 2 SCC (Civ) 607

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is clearly distinct from the arbitration clause in *Voestalpine Schienen GmbH*[19] and *Central Organisation for Railway Electrification*[4], and is in conflict with Section 12(5) of the Act. It was informed at the Bar that the correctness of the judgment of *Central Organisation for Railway Electrification*[4] has been challenged and referred to a larger Bench in *Union of India* v. *Tantia Constructions Ltd.*[21] as well as *JSW Steel Ltd.* v. *Railways*[22]. As we have noticed that the decision in *Central Organisation for Railway Electrification*[4] is not applicable in the present case, its reference to the larger Bench will have no bearing on the outcome of the present case.

24. For the reasons stated above, the present application under Section 11(6) of the Arbitration and Conciliation Act, 1996 is allowed. We hereby appoint Ms Justice Indu Malhotra, a former Judge of this Court as the sole arbitrator to adjudicate upon the disputes arising under and in connection with the conditions of tender entered into between the parties, subject to the mandatory disclosures under the amended Section 12 of the Arbitration and Conciliation Act, 1996.

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19 *Voestalpine Schienen GmbH* v. *Delhi Metro Rail Corpn. Ltd.*, (2017) 4 SCC 665 : (2017) 2 SCC (Civ) 607

4 *Central Organisation for Railway Electrification* v. *ECI-SPIC-SMO-MCML (JV)*, (2020) 14 SCC 712

21 (2023) 12 SCC 330 : 2021 SCC OnLine SC 271

22 2022 SCC OnLine SC 1973