

II. RP GARG V. THE CHIEF MANAGER, TELECOM DEPARTMENT, 2024 INSC 743: IS S. 31(7)(B) ARBITRATION ACT A DEFAULT RULE?

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I. INTRODUCTION

This case comment evaluates the recent decision of the Supreme Court of India *RP Garg v. The Chief Manager, Telecom Department*.¹ The decision addresses a nuanced aspect of the law regarding interest in arbitrations and provides an opportunity to discuss about the nature of rules of contract law in the context of Section 31(7) of the Arbitration and Conciliation Act, 1996.

Section 31(7) has been amended since its enactment. The provision as it stands today contains two clauses. Section 31(7)(a) deals with pre-award interest and Section 31(7)(b) concerns post-award interest. Insofar as party autonomy is concerned, there is a difference between both these provisions, which has been brought out in the judgment of the Supreme Court in *RP Garg*.

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II. FACTS AND PROCEDURAL HISTORY

An agreement was executed on 17 October 1997 between the appellant, a contractor, and the Haryana Telecom Department (“Telecom Department”) for trenching and laying underground cables. Clause 1(iv) of the agreement between the Telecom Department and the appellant provided:

“No interest will be payable on the earnest money or security deposit amount or any amount payable to the contractor under the contract.”

Disputes arose between the parties, and the arbitrator passed the arbitral award on 08.03.2001. The arbitrator allowed the appellant’s claim but disallowed the appellant’s claim for interest by relying on the aforesaid clause barring interest.

While pursuing the execution of the arbitral award, the appellant claimed post-award interest on the amount awarded. The court executing the award rejected the same. On appeal, the District Court allowed the appeal and directed payment of post-award interest at 18% per annum. The Telecom Department filed a revision petition before the High Court, which was allowed. The award holder filed a petition for special leave before the Supreme Court.

III. DECISION OF THE COURT

The Supreme Court held that the statutory scheme of Section 31(7) created a distinction between pre-award and post-award interest: a grant of pre-award interest under Section 31(7)(a) of the Arbitration Act by the arbitral tribunal is subject to an agreement between the parties. On the other hand, the

grant of post-award interest to the award holder is not subject to any agreement between the parties.²

The court stressed on the use of the expression “unless otherwise agreed by the parties” in Section 31(7)(a) and its absence in Section 31(7)(b) thereby signifying the absence of party autonomy as it relates to post-award interest.³ Accordingly, the court held that in the absence of a determination by the arbitral tribunal, the interest rate as specified in the Arbitration Act, that is, 18% per annum, prevailed.

The court relied on the decision of the Supreme Court in *Morgan Securities & Credits (P) Ltd. v. Videocon Industries Ltd*⁴ and distinguished *Jaiprakash Associates Ltd. v. Tehri Hydro Development Corporation (India) Ltd.*⁵ a decision of a three-judge Bench of the Supreme Court, on the ground that *Jaiprakash Associates* dealt with pre-award and not post-award interest.⁶

IV. COMMENT

This comment addresses two aspects: first, unlike how the Supreme Court held in *Morgan Securities*, the court was correct in *RP Garg* in holding that while Section 31(7)(a) reflected party autonomy in having an agreement contrary to the provision, Section 31(7)(b) did not admit such power of the parties. Second, Section 31(7)(b) should not always be construed as a mandatory rule but as a sticky default rule.

In *RP Garg*, the Supreme Court quoted extensively the judgment of the Supreme Court in *Morgan Securities*, where the court distinguished

² R.P. Garg v. Telecom Department [2024] SCC OnLine SC 2928 [9].

³ *ibid.*

⁴ *Morgan Securities & Credits (P) Ltd. v. Videocon Industries Ltd.* (2023) 1 SCC 602.

⁵ *Jaiprakash Associates Ltd. v. Tehri Hydro Development Corpn. (India) Ltd* (2019) 17 SCC 786 (SC).

⁶ R.P. Garg v. Telecom Department [2024] SCC OnLine SC 2928 [13] 2.

between Section 31(7)(a) and 31(7)(b), in terms of “discretion” to an arbitral tribunal. According to the court, while Section 31(7)(a) granted considerable discretion to grant pre-award interest, it was “against the grain of statutory interpretation”⁷ to construe Section 31(7)(b) as having reduced that discretion when it came to post-award interest.

Rather than couching the rationale in terms of discretion, it would have been appropriate for the court to have construed the sub-clauses from the point of view of default rules and party autonomy.

A default rule is a rule which could be contracted around by parties to an agreement. Such a provision typically contains language that allows parties to contract around the rule, such as “unless otherwise agreed between the parties”, which expression is found in Section 31(7)(a). Thus, there is an explicit marker that this provision is a default rule. These types of rules of contract law containing the explicit marker are known as explicit default rules. Implicit default rules, on the other hand, are default rules that do not contain the explicit marker. Examples of such rules include sections 33, 134, 135, 139, and 141 of the Indian Contract Act, 1872.⁸

So, when Section 31(7)(a) provides that an arbitral tribunal may include pre-award interest on the sum for which award is made, except where parties have otherwise agreed. If a clause in the agreement, such as the one in the agreement in the case, bars payment of interest, such bar would operate to contract around the default rule contained in terms of Section 31(7)(a). This position has been upheld in multiple judgments of the Supreme Court

⁷ [2023] 1 SCC 601 (SC) [25].

⁸ Corporation Bank v. Mohandas Baliga [1992] SCC OnLine Kar 314 (KHC).

including that of a three judge Bench in *Union of India v. Bright Power Projects (India) Pvt. Ltd.*⁹

On the other hand, Section 31(7)(b) does not contain a marker such as “unless otherwise agreed by the parties”. Therefore, literally, Section 31(7)(b) could be considered as a provision barring contracting around or contracting out of post-award interest.

This difference has been brought out by the Supreme Court in *RP Garg*, where the court held: “*In other words, clause (b) does not give the parties the right to “contract out” interest for the post-award period.*”¹⁰ Hence, Section 31(7)(a) is a default rule, while Section 31(7)(b) is not.

There is reason for this treatment in the statute, although not borne explicitly in these judgments. When a judgment or an award holds certain amount as due in relation to a contract, the amounts due under the contract merges with the judgment/ award and ceases to be mere contractual dues: such amounts become due under the judgment/ award.¹¹ Therefore, the interest rate to be paid under the judgment could not have been the contractual interest rate.

Such is the position not only under the 1996 Act but also in its earlier avatar, the Arbitration Act, 1940. Section 29 thereof read: “*Where and in so far as an award is for the payment of money the Court may in the decree order interest, from the date of the decree at such rate as the Court deems*

⁹ *Union of India v. Bright Power Projects (India) (P) Ltd* (2015) 9 SCC 695 (SC). *See also*, *Pam Developments Private Limited v. The State of West Bengal*, MANU/SC/0933/2024; *Oriental Structural Engineers Private Limited v. State of Kerala*, 2021:INSC:269; *Union of India v. Ambica Construction*, MANU/SC/0309/2016.

¹⁰ *R.P. Garg v. Telecom Department* [2024] SCC OnLine SC 2928 [11].

¹¹ *In re Sneyd; Ex p Fewings* (1883) 25 Ch D 338, reiterated in *Economic Life Assurance Society v. Osborne* [1902] AC 147; *First National Bank v. D-G of Fair Trading* [2002] 1 AC 481; *Standard Chartered Bank v. Ceylon Petroleum Corporation* [2011] EWHC 2094 (Comm).

reasonable, to be paid on the principal sum as adjudged by the award and confirmed by the decree.”

Post-award interest is a matter of discretion of the court/ arbitral tribunal. Therefore, the contractual interest rate may not bind the tribunal. If the post-award interest provided under the statute¹² is lower than the contractual rate, the statutory rate would prevail and if the statutory rate is more, such rate will prevail over the contractual rate.¹³

The second point this case comment addresses is whether Section 31(7)(b) should always be construed as a mandatory rule. There could be situations where holding that Section 31(7)(b) absolutely restricts contracting around would do a serious injustice to party autonomy.

For instance, take a situation where two sophisticated commercial parties enter into a standstill agreement after an arbitral award has been rendered. A standstill agreement is an agreement to stop the limitation period from running or in some cases, extend the limitation period for the purposes of preserving or freezing the rights of the parties and their enforceability for a limited time in order to enable them to solve the dispute amicably either by themselves or through settlement mechanisms such as conciliation, mediation, etc. Imagine that in such a standstill agreement, they agree that parties will attempt to resolve their dispute through conciliation/ mediation for six months.

¹² Section 31(7)(b) pegs the post-award “interest at the rate of two per cent. higher than the current rate of interest prevalent on the date of award” and the explanation therein defines “current rate of interest” “as assigned to it under clause (b) of section 2 of the Interest Act, 1978”. Section 2(b) of the Interest Act, 1978 defines the expression as “the highest of the maximum rates at which interest may be paid on different classes of deposits (other than those maintained in savings account or those maintained by charitable or religious institutions) by different classes of scheduled banks in accordance with the directions given or issued to banking companies generally by the Reserve Bank of India under the Banking Regulation Act, 1949 (10 of 1949).”

¹³ Standard Chartered Bank v. Ceylon Petroleum Corporation [2011] EWHC 2094.

They also agree that for the period of three months or pendency of mediation/conciliation, whichever is later, no interest on the arbitral award would be claimed.

Now, assume that having attempted to resolve the dispute through, say, conciliation, but have failed in doing so within the three-month period. Both parties challenge the award, which fails. One of the parties files a petition for the execution of the award while claiming post-award interest, including for the three-month period they agreed not to claim interest. Is it right on the part of the execution petitioner to claim interest for that three-month period after having committed through an agreement not to charge such interest? Hence, it would not be correct to construe Section 31(7)(b) as a mandatory rule in all circumstances, especially when the provision does not seek to protect against any internality¹⁴ or externality.¹⁵

Generally, party sophistication may have a role to play in the context of construing a legal provision as a default or a mandatory rule. Absent statutory objective of guarding against an internality or an externality, in appropriate circumstances, courts should not resist from holding provisions like Section 31(7)(b) as default rules. However, such contracting around should not be easily read in, unless specifically made by the parties. Sticky default rules are default rules which make it difficult for parties to contract around.¹⁶

¹⁴ Zamir and Ian Ayres, 'A Theory of Mandatory Rules: Typology, Policy and Design' (2020) 99(283) TLR 287.

¹⁵ Eyal Zamir and Ian Ayres, 'A Theory of Mandatory Rules: Typology, Policy and Design' (2020) 99(283) TLR 287.

¹⁶ Eyal Zamir, 'Default Rules: Theoretical Foundations' in Chen-Wishart, Mindy and Saprai, Prince (eds), *Research Handbook on the Philosophy of Contract Law*, (Edward Elgar Publishing 2022).

Provisions like Section 31(7)(b) should, in apt situations, be construed as sticky default rules so that the intent to contract around is explicit. Clearly, whether parties can agree on applicable interest post-judgment or post-award should be a matter of comprehensive study.

V. CONCLUSION

As per the statute, the jurisdiction of the arbitral tribunal regarding post-award interest cannot be circumscribed by an agreement between the parties. But arbitration is a dispute resolution process built on party consensus. In appropriate situations, parties should have the right to determine even the post-award interest. However, such a right to agree on an interest rate (post-award) different from the statutory rate should not be easily presumed. There should be an explicit agreement marking such departure, and such an agreement should not be unreasonable.