*Reportable*

IN THE SUPREME COURT OF INDIA

CIVIL APPELLATE JURISDICTION

CIVIL APPEAL NO.1282 OF 2011
[Arising out of SLP [C] No.11903/2010]

Indian Oil Corporation Ltd. … Appellant

Vs.

M/s. SPS Engineering Ltd. … Respondent



**J U D G M E N T**

**R.V.RAVEENDRAN, J.**

Leave granted.



2. The Indian Oil Corporation Limited, the appellant herein, awarded an infrastructure work relating to drinking water system for its Paradip Refinery project to the respondent on 17.10.2000 and followed by a formal agreement dated 18.1.2001. The period stipulated under the contract for completion of the work was 13 months from the date of issue of the order dated 17.10.2000 and the contract value was Rs.16,61,17,473/-. The appellant

terminated the contract on 29.10.2002 alleging that the respondent contractor though required to complete the work within 13 months, had achieved a progress of hardly 15.94% till 30.4.2002 and notified the respondent that the work will be got completed through an alternative agency, at the risk and cost of the respondent under Clause 7.0.9.0 of the General Conditions of Contract.

3. In view of the said termination, the respondent raised certain claims against the appellant and invoked the arbitration agreement contained in the General Conditions of Contract and filed an application under section 11 of the Arbitration and Conciliation Act, 1996 ('Act' for short) before the Delhi High Court for appointment of an arbitrator. The Designate of the Chief Justice of the High Court, by order dated 17.3.2003, appointed a retired High Court Judge as the arbitrator.



4. Before the arbitrator, the respondent filed a statement of claims raising eight claims. However in its written submission before the Arbitrator, the contractor confined its claims to only three, aggregating to Rs.1,31,81,288/-.

5. The appellant made several counter-claims aggregating to Rs.92,72,529/-. Subsequently the statement of counter-claims was amended and the following para was added in regard to the extra cost in getting the work completed through an alternative contractor:

> *"Since the aforementioned contract is still pending and IOCL is in the process of inducting agency (ies) to complete the said* work, the Engineer-in-charge of the said contract, EIL estimated a minimum expenditure of Rs.18,36,20,000/- for completion of the works under the said contract which EIL intimated to IOCL by its letter dated 23.5.2002, a copy whereof is annexed hereto and marked Annexure RY. *The said estimated expenditure has been revised by IOCL who has arrived at the reduced figure of Rs.2,10,41,626/-* (Rupees Two Crores Ten Lacs Forty One Thousand Six Hundred Twenty Six Only) in its proposal dated 09.09.2006, a copy whereof is annexed hereto and marked Annexure RY-1. **Accordingly, IOCL is entitled to recover from SPSEL any additional sums including the abovementioned Rs.2,10,41,626/- (Rupees Two Crores Ten Lacs Forty One Thousand Six Hundred Twenty Six Only) that it will according to its estimate incur upon execution of the balance work by other agencies pursuant to the termination of the said contract in terms of Clause 7.0.6.0 of GCC along with any other additional expenditure incurred by IOCL in completion of the said works**. IOCL, therefore, is entitled to an amount of Rs.2,10,41,626/- (Rupees Two Crores Ten Lacs Forty One Thousand Six Hundred Twenty Six Only) from SPSEL which SPSEL has not paid till date."
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> *(emphasis supplied)*

The prayer in the counter-claim however remained unaltered and did not include the claim of Rs.2,10,41,626/- on account of risk - execution of balance work. Even after the above amendment, the prayer continued to be as under :

"It is therefore prayed that the learned Arbitrator may be pleased to:

(i) award a sum of Rs.92,72,529/- (Rupees Ninety Two Lacs Seventy Two Thousand Five Hundred Twenty Nine Only) against SPSEL and in favour of IOCL along with the additional amounts which in IOC's estimate, IOC will incur in further executing and completing at the Claimant's risk and cost, the balance works remaining incomplete under the said contract.

(ii) grant pendent lite interest @ 18% per annum on the awarded amount;

(iii) grant interest on the awarded amount @ 18% per annum from the date of award till the date of payment in full;

(iv) grant cost of arbitration proceedings to IOCL;

(v) grant such other or further order(s) and/or relief as are deemed appropriate in the circumstances of the case;"

6. The arbitrator made an award dated 27.10.2008. He awarded Rs.91,33,844 towards the claims of respondent. As against the counter claims aggregating to Rs.92,72,529 made by the appellant, the arbitrator awarded a sum of Rs.11,10,662. In regard to the averments made by the appellant in regard to the extra cost involved in getting the work completed through an alternative contractor, the arbitrator observed thus :

"102. The contract was terminated in October 2002 and till date the balance work of the contract has not been executed. Such damage could have been allowed to the respondent if in a reasonable period after termination of the contract, the respondent had executed the balance work at the risk and costs of the claimant. In case the costs actually incurred have been more than the costs which were required to be incurred under the contract, then the difference between the two costs could have been awarded as damages to the respondent. There is no proper evidence on the record to show that what could have been the costs of the balance work if it had been executed within reasonable period after the termination of the

> contract. *Such damage cannot be awarded on mere opinion of any particular person or on hypothetical basis*. Under clause 7.0.9.0 of General Conditions of the Contract, the respondent was entitled at the risk and expenses of the contractor to get completed the balance work and recover the costs from the claimant. *This clause further contemplates that on the amount actually expended by the owner for the completion of the work 15% to be added as supervision charges, the same would have become recoverable from the claimant. In the present case, no such cost has been incurred till date*. Thus, for these reasons, I reject this counter claim."
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> *(emphasis supplied).*

The arbitrator adjusted Rs.11,10,662 awarded to the appellant, towards the sum of Rs.91,33,844 awarded in favour of the respondent and consequently directed the appellant to pay to the respondent, the balance of Rs.80,23,182. He further directed that if the amount was not paid within three months from the date of award, the appellant shall pay interest at the rate of 12% per annum from the date of award till payment. The appellant did not challenge the award and it thus attained finality.



7. The appellant claims that it entrusted the incomplete work to Deepak Construction Company for completion in the year 2005, that the said contractor completed the work on 29.12.2007, and that the final bill of the said alternative agency was settled on 7.5.2008. On that basis, the appellant calculated the actual extra cost incurred in completing the work and the total amount recoverable from the petitioner in terms of the contract, as under:

| | | | |
|---|---|---|---|
| A. | Amount determined as payable to the alternative agency (Deepak Construction Co.) for the balance work | | Rs.4,05,74,465.00 |
| B. | Material supplied to the alternative agency for completing the work | (+) | Rs.2,78,68,861.64 |
| C. | Total Cost (A + B) | | Rs.6,84,43,326.64 |
| D. | The cost of such unfinished work, if it had been completed by the respondent, as per its contract rates. Rs.3,30,93,996.75 | (-) | |
| E. | Extra cost incurred on account of getting the work completed at the risk and cost of respondent (C – D) | | Rs.3,53,49,329.89 |
| F. | Supervision charges at 15% on Rs.6,84,43,326.64 | (+) | Rs.1,02,66,499.00 |
| Total amount recoverable from the respondent (E+F) | | | Rs.4,56,15,828.89 |



Towards the said claim against the respondent, the appellant adjusted the sum of Rs.80,23,182/- awarded by the arbitrator to the respondent and arrived at the net amount recoverable from the respondent towards extra cost for completion as Rs.3,75,92,646.89. The appellant by notice dated 22.1.2009 called upon the respondent to pay the said sum of Rs.3,75,92,646.89 (and interest thereon at 18% per annum if the amount was not paid within seven days) and informed the respondent that if it disputed

its liability, to treat the said letter as appellant's notice invoking arbitration. The appellant also suggested a panel of three names (including Justice P.K. Bahri - the arbitrator who had made the award dated 27.10.2008) with a request to select one of them as the arbitrator. The respondent by reply dated 18.3.2009 refused to comply, contending that the counter claim in regard to the risk-execution cost had already been rejected by the arbitrator, by his award dated 27.10.2008 and that award having attained finality, there could be no further arbitration. In view of the said stand of the respondent, the appellant filed a petition under section 11 of the Act praying for appointment of an arbitrator to decide its claim for the extra cost in getting the work completed through the alternative agency.

8. The learned Designate of the Chief Justice of the Delhi High Court (for short 'the Designate') by the impugned order dated 8.12.2009 dismissed the application with costs of Rs.50,000/-. He held that the application under section 11 of the Act by the appellant was misconceived, barred by *res judicata*, and *mala fide*. The Designate held (i) that the claim by the appellant in regard to extra cost had already been considered and rejected by the Arbitrator; (ii) that the claim regarding extra cost was barred by limitation (by drawing an inference from the observation of the Arbitrator that the risk execution tender was not awarded to Deepak Construction Co.

within a reasonable period of termination of respondent's contract); and (iii) that as the work was completed by Deepak Construction Co. on 29.12.2007 and the earlier arbitration proceedings had came to an end much later on 27.10.2008, the claim in regard to actual extra cost ought to have been crystallized and claimed in the first round of arbitration.

9. The said order is challenged in this appeal by special leave. On the contentions urged the questions that arise for consideration are as follows :

(i) Whether the Chief Justice or his designate can examine the tenability of a claim, in particular whether a claim is barred by *res judicata,* while considering an application under section 11 of the Act?

(ii) Whether the Designate was justified in holding that the claim was barred by *res judicata* and that application under section 11 of the Act was misconceived and *mala fide*?



**Re : Question (i)**

10. This Court, in *National Insurance Co. Ltd. vs. Boghara Polyfab Private Limited* [2009 (1) SCC 267] following the decision in *SBP & Co. v. Patel Engineering Ltd*. [2005 (8) SCC 618], identified and segregated the issues that may be raised in an application under section 11 of the Act into three categories, as under :

"22.1. The issues (first category) which the Chief Justice/his designate will have to decide are :

(a) Whether the party making the application has approached the appropriate High Court?
(b) Whether there is an arbitration agreement and whether the party who has applied under Section 11 of the Act, is a party to such an agreement?

22.2. The issues (second category) which the Chief Justice/his designate may choose to decide (or leave them to the decision of the Arbitral Tribunal) are:

(a) Whether the claim is a dead (long-barred) claim or a live claim?

(b) Whether the parties have concluded the contract/transaction by recording satisfaction of their mutual rights and obligation or by receiving the final payment without objection?

22.3. The issues (third category) which the Chief Justice/his designate should leave exclusively to the Arbitral Tribunal are:

(i) Whether a claim made falls within the arbitration clause (as for example, a matter which is reserved for final decision of a departmental authority and excepted or excluded from arbitration)?

(ii) Merits or any claim involved in the arbitration."



11. To find out whether a claim is barred by *res judicata*, or whether a claim is "*mala fide*", it will be necessary to examine the facts and relevant documents. What is to be decided in an application under section 11 of the Act is whether there is an arbitration agreement between parties. The Chief Justice or his designate is not expected to go into the merits of the claim or examine the tenability of the claim, in an application under section 11 of the Act. The Chief Justice or his Designate may however choose to decide

whether the claim is a dead (long-barred) claim or whether the parties have, by recording satisfaction, exhausted all rights, obligations and remedies under the contract, so that neither the contract nor the arbitration agreement survived. When it is said that the Chief Justice or his Designate may choose to decide whether the claim is a dead claim, it is implied that he will do so only when the claim is evidently and patently a long time barred claim and there is no need for any detailed consideration of evidence. We may elucidate by an illustration : If the contractor makes a claim a decade or so after completion of the work without referring to any acknowledgement of a liability or other factors that kept the claim alive in law, and the claim is patently long time barred, the Chief Justice or his Designate will examine whether the claim is a dead claim (that is, a long time barred claim). On the other hand, if the contractor makes a claim for payment, beyond three years of completing of the work but say within five years of completion of work, and alleges that the final bill was drawn up and payments were made within three years before the claim, the court will not enter into a disputed question whether the claim was barred by limitation or not. The court will leave the matter to the decision of the Tribunal. If the distinction between apparent and obvious dead claims, and claims involving disputed issues of limitation is not kept in view, the Chief Justice or his designate will end up deciding the question of limitation in all applications under section 11 of the Act.

12. An application under section 11 of the Act is expected to contain pleadings about the existence of a dispute and the existence of an arbitration agreement to decide such dispute. The applicant is not expected to justify the claim or plead exhaustively in regard to limitation or produce documents to demonstrate that the claim is within time in a proceedings under section 11 of the Act. That issue should normally be left to the Arbitral Tribunal. If the Chief Justice or his designate is of the view that in addition to examining whether there is an arbitration agreement between the parties, he should consider the issue whether the claim is a dead one (long time barred) or whether there has been satisfaction of mutual rights and obligation under the contract, he should record his intention to do so and give an opportunity to the parties to place their materials on such issue. Unless parties are put on notice that such an issue will be examined, they will be under the impression that only questions of jurisdiction and existence of arbitration agreement between the parties will be considered in such proceedings.

13. The question whether a claim is barred by *res judicata,* does not arise for consideration in a proceedings under section 11 of the Act. Such an issue will have to be examined by the arbitral tribunal. A decision on *res judicata* requires consideration of the pleadings as also the claims/issues/points

and the award in the first round of arbitration, in juxtaposition with the pleadings and the issues/points/claims in the second arbitration. The limited scope of section 11 of the Act does not permit such examination of the maintainability or tenability of a claim either on facts or in law. It is for the arbitral tribunal to examine and decide whether the claim was barred by *res judicata.* There can be no threshold consideration and rejection of a claim on the ground of *res judicata,* while considering an application under section 11 of the Act.

**Re : Question (ii)**

14. We extract below the reasoning adopted by the Designate to dismiss the appellant's application under section 11 of the Act :

> "5. In my opinion, not only the aforesaid para 102 in the Award dated 27.10.2008 operates as *res judicata* against the present petitioner, I find that the present petition is misconceived and and *mala fide* because, if the present petitioner is correct in saying and which I doubt it is, that its limitation/right would only begin after the work is completed by M/s Deepak Construction Company when the amount of the higher cost is known, even then, the work was completed by the M/s Deepak Construction Company admittedly on 29.12.2007, and thus the present petitioner, could well have proved its counter claim in the earlier proceedings and could have crystallized the amount in the said earlier arbitration proceedings. If necessary it could have even amended its pleadings as regards the counter claim. On a further query by the Court to the counsel for the petitioner with respect to the statement in the notice dated 22.01.2009 sent by the petitioner to the respondent which states that M/s Deepak Construction Company has completed the work on 29.12.2007 and its final bill has now been settled" that when was the bill of M/s Deepak Construction Company settled, the counsel for petitioner

states that for the present no such information is at all available whether in the form of any assertion in the present petition or in any document in support thereof.

6. A conspectus of the aforesaid facts show that firstly in the earlier arbitration proceedings, the counter claim of the present petitioner on this very subject matter was specifically dismissed by holding and observing that the risk purchase tender awarded to M/s Deepak Construction Company was not given within a reasonable period of time after termination of the work of the present respondent. Secondly, it has further become clear that the work was completed by M/s Deepak Construction Company admittedly as per the case of the petitioner on 29.12.2007 and the earlier arbitration proceedings came to an end later by passing of the Award on 27.10.2008 and, therefore, the claim with respect to any cost of the total materials for the substitute contract for the risk purchase could very well have been crystallized and claimed in the earlier arbitration proceedings. Thirdly, admittedly there is no challenge to the award dated 27.10.2008 by the present petition whereby its counter claim was rejected. Fourthly, I am of the view that once a risk and cost tender is issued at the risk and cost of a person, then, the amount which is to be claimed from the person who is guilty of breach of contract and against whom risk and cost is tendered, becomes crystallized when the risk purchase tender at a higher cost is awarded. Once a higher cost of work is known as compared to the cost of the work for the earlier work for which the earlier contract was there and with respect to which the earlier contractor was in breach, then not only the amount becomes crystallized but limitation also commences for filing of the legal proceedings against the person in breach of obligations under the earlier contract. It cannot be that limitation and a right continues indefinitely to be extended till the performance is completed under a subsequent risk purchase contract. This would give complete uncertainty to the period of limitation striking at the very root of one of the principles of the Limitation Act and which is that evidence is lost by passage of time and which will cause grave prejudice to the person against whom a stale claim is filed."

15. The appellant submitted that having regard to clause 7.0.9.0 of the contract, damages can be claimed by it (as employer), in regard to the additional amount incurred for getting the work completed through an alternative agency at the risk and cost of the contractor along with the

supervision charges, only when the *amount was actually expended* for completion of the entire work; and therefore, unless the work was completed by the alternative agency and the final bill was settled or finalized, the actual extra cost could not be determined. It was pointed out that in the first round of arbitration, the hearing was concluded by the Arbitrator on 13.3.2008 and matter was reserved for orders and the award was declared on 27.10.2008; that the work was completed by the alternative agency on 29.12.2007 and final bill of the alternative agency was drawn and settled only on 7.5.2008, *after the conclusion of the hearing,* by the Arbitrator; that the actual extra cost could be worked out only when the final bill was prepared, and not on the date of completion of work; that therefore the appellant could not make the claim for actual extra cost, in the first round arbitration. It was also submitted that the appellant was not expected to give details of completion of work and preparation of the final bill, or produce documents in support of it in a proceeding under section 11 of the Act; and that the Designate was not therefore justified in finding fault with the appellant for not stating the date of settlement of the final bill in the petition under section 11 of the Act and for not producing the final bill.

16. The appellant also contended that when its statement of counter claim was amended before the Arbitrator, the appellant had only indicated its

estimation of the probable extra cost to be Rs.2,10,41,626/-, as advance indication of a claim to be made in future on the basis of actuals, and that it had not prayed for award of the said amount in the said proceeding. It was pointed out that even after mentioning the proposed claim by amending the statement of counter claim, the actual counter claim before the arbitrator remained as only Rs.92,72,529/- exclusive of any claim on account of the risk completion cost. It was submitted that having regard to clause 7.0.9.0, the counter claim for extra cost could not have been made when the first arbitration was in progress and that the arbitrator had in fact noticed in his award (at para 102) that only when the cost actually incurred, the appellant could make the claim for the extra cost. It is contended that the "rejection" by the arbitrator was not on the ground that the claim for extra cost was not recoverable, nor on the ground that no extra cost was involved in completing the work, but on the ground that as on the date of the award, the appellant had not actually incurred any specific extra cost; and that as the arbitrator clearly held that any claim for extra cost was premature and could not be considered at that stage, the observation that 'I reject this counter claim' only meant that the claim relating to extra cost was not being considered in that award and that appellant should make the claims separately after the amount was actually expended.

17. Clause 7.0.9.0 of the contract relied upon by the appellant reads thus :

> "clause 7.0.9.0
>
> Upon termination of the contract, the owner shall be entitled at the risk and expenses of the contractor by itself or through any independent contractor(s) or partly by itself and/or partly through independent contractor(s) to complete to its entirety the work as contemplated in the scope of work and to recover from the contractor in addition to any other amounts, compensations or damages that the owner may in terms hereof or otherwise be entitled to (including compensation within the provisions of clause 4.4.0.0 and clause 7.0.7.0 hereof) the difference between the amounts as would have been payable to the contractor in respect of the work (calculated as provided for in clause 6.2.1.0 hereof read with the associated provisions thereunder and clause 6.3.1.0 hereof) *and the amount actually expended by the owner for completion of the entire work as aforesaid together with 15% (fifteen per cent) thereof to cover owner's supervision charges, and in the event of the latter being in the excess former, the owner shall be entitled (without prejudice to any other mode of recovery available to the owner) to recover the excess from security deposit or any monies due to the contractor."*
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> *(emphasis supplied)*

18. On a perusal of the order of the Designate, we find that the Designate has clearly exceeded his limited jurisdiction under section 11 of the Act, by deciding that the claim for extra cost, though covered by the arbitration agreement was barred by limitation and by the principle of res judiata. He was also not justified in terming the application under section 11 of the Act as 'misconceived and malafide'. Nor could he attribute '*mala fides'* to the appellant, a public sector company, in filing an application under section 11 of the Act, without any material to substantiate it. We may refer to some of the findings of fact recorded by the Designate, which were wholly

unwarranted in a proceeding under section 11 of the Act and the fallacy in such findings :

(i) *Finding : The appellant did not state anywhere in the petition the date which the final bill was settled and did not produce any document containing such information.* The appellant was not expected or required to give such information in a petition under section 11 of the Act or produce the documents showing the settlement of final bill along with the said petition. Therefore, the appellant could not be found fault for such omission. In fact, the Designate noticed that the work was completed on 29.12.2007. The claim was in time with reference to the date on which the work completed (29.12.2007) by the alternative agency.

(ii) *Finding : As the work was completed on 29.12.2007 and as the award was made only on 27.10.2008, the appellant ought to have crystalised the extra cost and claimed it in the first arbitration proceedings.* The assumption that the appellant ought to have made the claim for extra cost which arose after the commencement of the arbitration proceedings, in the pending proceedings by way of amendment, has no basis either in law or in contract. If the cause of action arose after the completion of pleadings and

commencement of hearing in the first round of arbitration, nothing prevented the appellant from making a separate claim by initiating a second arbitration.

(iii) *Finding : Once a risk and cost tender is issued at the risk and cost of a person, then, the amount which is to be claimed from the person who is guilty of breach……. becomes crystallized when the risk purchase tender at a higher cost is awarded..* This may be true as a general proposition. But it may not apply if there is a specific provision in the contract (like clause 7.0.9.0) which requires that the employer should claim as extra cost, only the difference between the "amounts as would have been payable to the contractor in respect of the work" and "the amount actually expended by the owner for completion of the entire work".

19. The Designate should have avoided the risks and dangers involved in deciding an issue relating to the tenability of the claim without necessary pleadings and documents, in a proceeding relating to the limited issue of appointing an Arbitrator. It is clear that the Designate committed a jurisdictional error in dismissing the application filed by the appellant under section 11 of the Act, on the ground that the claim for extra cost was barred by *res judicata* and by limitation. Consideration of an application under

section 11 of the Act, does not extend to consideration of the merits of the claim or the chances of success of the claim.

20. We may at this stage refer to one aspect of the claim for extra cost. The award amount due to the respondent under the award dated 27.10.2008 is an ascertained sum due, recoverable by executing the award as a decree. On the other hand the claim of the appellant for reimbursement of the extra cost for getting the work completed, is a claim for damages which is yet to be adjudicated by an adjudicating forum. The appellant cannot therefore adjust the amount due by it under the award, against a mere claim for damages made by it against the respondent. The appellant will have to pay the award amount due to the respondent and if necessary modify its claim for extra cost against the respondent.



21. In view of the foregoing, this appeal is allowed and the order of the Designate is set aside. The application under section 11 of the Act filed by appellant before the Chief Justice of the Delhi High Court is allowed and Justice P.K.Bahri (Retd.) who was the earlier Arbitrator is appointed as the sole arbitrator to decide the appellant's claim in regard to the additional cost for completing the work. It is open to the respondent to raise all contentions against the claim of the appellant including the contention of limitation,

maintainability and res judicata, before the arbitrator. Nothing in this order shall be construed as expression of any opinion on the merits or tenability of the claim of the appellant regarding extra cost.

…….J.
(R V Raveendran)

New Delhi;
February 3, 2011.

……..J.
(A K Patnaik)