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& Solicitors

## **Counter-Claims can be filed before the Arbitral Tribunal even if they were not notified before invoking the Arbitration**

**National Highway Authority of India v. Transstroy (India) Limited**

<b>Citation</b>	<b>Civil Appeal No. 6732 of 2021</b>
<b>Date</b>	<b>11 July 2022</b>
<b>Court</b>	<b>Supreme Court of India</b>
<b>Coram</b>	<b>Hon'ble Mr. Justice M. R. Shah Hon'ble Mr. Justice Sanjiv Khanna</b>

## 1. BRIEF FACTS:

- 1.1. The National Highway Authority of India ("**Appellant NHAI**") on 13.11.2014 entered into an Engineering Procurement and Construction Agreement ("**Contract**") with the Transstroy (India) Limited ("**Respondent**") for improvement of Karaikudi-Ramanathapuram Section of National Highway No. 210, inclusive of 500m on SH-35 Madurai Road in Tamil Nadu.
- 1.2. NHAI was under the impression that the Respondent breached specific obligations under the Contract due to which, on 29.09.2015, NHAI issued a cure period notice under Clause 23.1.1 of the Contract towards the Respondent so that they can cure defaults within 60 days.
- 1.3. As the Respondent failed to cure the defaults, on 12.04.2016 NHAI issued a notice of intention to terminate the Contract under Clause 23.1.2 of the Contract. The Respondent sent its reply in regard to the same on 14.04.2016.
- 1.4. On finding the reply unsatisfactory, NHAI issued a termination notice dated 22.07.2016 under Clause 23.1.2 of the Contract, wherein NHAI allegedly stated "*the same is without prejudice to the Authority's right to claim damages for the Contractor's failure to comply with the unambiguous obligations casted upon it under the Contract and/or to realize any dues, losses and damages whatsoever under the Contract or under applicable laws, as the case may be*".
- 1.5. After receiving the termination notice, the Respondent on 02.01.2017, addressed a letter to NHAI with the intent that certain disputes should be referred for amicable settlement under Clause 26.2 of the Contract. By a letter dated 09.02.2017, the Respondent invoked the Arbitration Clause in the Contract and appointed the Arbitrator. Respondent had also requested NHAI to appoint their Arbitrator and thus by a letter dated 10.03.2017 NHAI nominated its Arbitrator.
- 1.6. After the Arbitral Tribunal ("**Tribunal**") was constituted, Respondent filed its Statement of Claim on 15.05.2017 and on 11.07.2016 NHAI filed its Statement of Defence before the Tribunal. Herein, NHAI stated that it had reserved its rights to claim damages and will file its counter claim separately.
- 1.7. After filing Statement of Claim, on 13.07.2017 NHAI filed a letter in the Tribunal to seek extension for filing of its counter claim. The request was rejected by the Tribunal through an email sent on 18.07.2017, on the grounds that no Application had been filed by NHAI to place its counter claim on the record.
- 1.8. Thereafter, NHAI moved an application under Section 23(2A) of the Arbitration and Conciliation Act, 1996 ("**the Act**") to again place its counter claim on the record. The Tribunal via order dated 15.09.2017 rejected NHAI's application on the grounds that the procedure envisaged under Clauses 26.1 and 26.2 of the Contract had not been followed by NHAI. The Tribunal was of the opinion that as the dispute raised in the counter claim was beyond the scope of Arbitration therefore Tribunal cannot adjudicate on the same.
- 1.9. Feeling aggrieved by the decision of Tribunal, NHAI filed an appeal under Section 34 of the Act before the Hon'ble High Court of Delhi ("**High Court**"). The High Court dismissed the application filed under Section 34 and confirmed the order passed by the Tribunal dated 15.09.2017.
- 1.10. Dissatisfied with the order passed by the High Court, NHAI filed an appeal in the Hon'ble Supreme Court of India ("**Apex Court**").

## 2. ISSUE RAISED:

- 2.1. Whether the High Court and Arbitral Tribunal had committed an error in rejecting NHAI's application under Section 23(2A) of the Act?

### **3. SUBMISSIONS OF THE APPELLANT:**

- 3.1. The Appellant contended that the High Court had committed an error by confirming the order passed by the Tribunal. It was claimed by the Appellant that the Tribunal and the High Court failed to appreciate that the counter claim was based on an overlapping cause of action. It was further argued that the Arbitration arose out of the Appellant's termination notice and thus the dispute was on the validity of the termination. As the dispute was from the same transaction any further splitting of the dispute would lead to unnecessary multiplicity of proceedings and evidence.
- 3.2. The Appellant contended that Clause 26 of the Contract is self-explanatory which states that any dispute or controversy which is to be resolved amicably can be done according to the conciliation process laid down under Clause 26.2.
- 3.3. The Appellant argued that the reason why clause 26.1 could be invoked by any party is that by its definition 'dispute' is referred to be as two sided. It was further argued that the High Court and the Tribunal failed to appreciate the difference between a 'claim' and a 'dispute'
- 3.4. The Appellant contended that the termination notice dated 22.07.2016 is the cause of dispute therefore it would be a travesty of process if dispute is interpreted in a way wherein only claims made by the Respondent is allowed to be submitted through the process mentioned under Clause 26 of the Contract.
- 3.5. The Appellant argued that the Respondent's contention that the counter claim was made by a way of counterblast should be rejected. The High Court and Tribunal failed to appreciate that it was the Appellant who terminated the contract after sufficient opportunities were provided to the Respondents to cure the defects. It was further contended that the Appellant had reserved its rights to claim damages in the termination notice which was sent to the Respondent.
- 3.6. The Appellant contended that it cannot be argued that by submitting counter claim the Appellant has bypassed the procedure agreed upon. There is no question of bypassing of the procedures when the stage had already passed.
- 3.7. It was further argued by the Appellant that the procedural provisions cannot be interpreted in a hyper-technical manner as it goes against the spirit of the Act.
- 3.8. The Appellant contended that the object and purpose of Section 23(2A) was neglected by the Tribunal and High Court by not taking on record the counter claim filed by the Appellant.

### **4. SUBMISSIONS OF THE RESPONDENT:**

- 4.1. The Respondent contended that the Clause 26 of the Contract mandatorily required parties to attempt amicable settlement of disputes as a pre-condition to Arbitration. This approach was not taken by the Appellant. It was further contended that Clause 26 of the Contract is unambiguous and lays down a two-step process which has to be followed before the invocation of the Arbitration. The 1<sup>st</sup> step is the 'notification of dispute' in writing by any party and 2<sup>nd</sup> step is 'resolution by amicable settlement'. It was further argued that only on failure to settle the dispute amicably, the dispute under Clause 26.1.1 will be referred to Arbitration.
- 4.2. The Respondent contended that the term 'disputes' under Clause 26.1.1 has been contractually defined by the parties and has to be strictly understood as those disputes, differences, or controversies which were identified and referred for conciliation by any of the party. It was claimed that this kind of identification was not made by the Appellant for placing its counter-claim on record and thus the same cannot be raised further.

- 4.3. The Respondent argued that mere reservation of rights does not entitle any party to bypass the contractually agreed mechanisms and procedures as laid down under Clause 26 of the Contract. Unless there is a waver clause, doing the same will amount to as rewriting of the contract. It was further contended that as the Clause 26 is mandatory in nature, claims which are contrary to the contractual mechanism should not be allowed to be introduced.
- 4.4. The Respondent contended that Section 23(2A) does not permit a counter claim to be raised in a manner which is inconsistent with the Contract agreed upon by the parties. On co-joint reading of Section 23(2A) and Sections 2(1)(b), 7 and 21 of the Act it is apparent that parties have the choice to select which dispute will be referred to Arbitration. Therefore, counter claim filed before the Tribunal even without being categorised as dispute under clause 26.1 will be beyond the jurisdiction of the Tribunal.

## **5. DECISION OF THE COURT:**

- 5.1. The Hon'ble Supreme Court of India observed that Clause 26 of the Contract was conciliatory in nature and therefore the main dispute which was the termination of the contract had to be resolved through conciliation after following the procedure mentioned in the Contract. The Apex Court further noted that the dispute also may include claims and counter claim. Since the dispute pertained to the validity of the termination and was required to be resolved through conciliation. The Respondent cannot contend that the counter claim was in contravention of prescribed procedure.
- 5.2. The Hon'ble Supreme Court of India observed that the Tribunal and High Court failed to distinguish between 'claim' and 'dispute', with the former being made up by one side and the latter being two sided in nature.
- 5.3. The Hon'ble Supreme Court of India observed that when the Tribunal rejected NHAI's request seeking extension of time to file counter claim, it did not reject the same on the grounds that it would not be maintainable without following the process prescribed under Clause 26.
- 5.4. Moreover, the Apex Court further observed that NHAI from the very beginning reserved its right to claim the damages and also in its Statement of Defence it was specifically stated that the Appellant had reserved its right to file counter claim.
- 5.5. The Hon'ble Supreme Court of India observed that the grounds on which the Tribunal rejected NHAI's application to place counter-claim on record ran contrary to the intent between the parties which was to resolve the dispute through conciliation. The Apex Court was of the opinion that the "*Arbitral Tribunal has taken away the valuable right of the NHAI to submit counter claim, which is of a very huge amount thereby negotiating the statutory and contractual rights of the NHAI and paving way for a piecemeal and inchoate adjudication*".
- 5.6. The Hon'ble Supreme Court of India observed that when the Act has a specific provision for filing of counter claim, then there is no reason to curtail the Appellant's right to submit counter claim. Further, it was observed by the Apex Court that the High Court in its judgment had lost sight of the fact that, by denying counter claim to be placed on record various parallel proceedings will emerge.
- 5.7. The Hon'ble Supreme Court of India held that by not permitting *the NHAI to file the counter claim would defeat the object and purpose of permitting to file the counter claim/set off as provided under Section 23(2A) of the Arbitration Act, 1996*. The High Court had narrowly interpreted the Clause 26 of the Contract and had therefore erred by rejecting the application under Section 34/37 of the Act and also by confirming the order passed by the Arbitral Tribunal.

5.8. The Hon'ble Supreme Court of India by acknowledging the above reasons, quashed and set aside the order of the Tribunal dated 15.09.2017 and impugned judgment of the High Court and permitted NHA1 to file its counter claim before the Tribunal.

**6. PSL OPINION:**

6.1. The judgement delivered by the Apex Court, clarified that counter claims cannot be rejected merely because the claims thereunder were not notified at the pre-arbitral stage. As a result of the same, the object behind Section 23(2A) of the Act is safeguarded as parties will be able to file the counter claim even at the later stages of the proceedings. Moreover it prevents multiplicity of proceedings and parallel proceedings, which if not promptly curtailed will ruin the smooth functioning of Arbitral Mechanism by overburdening the system. This will prevent parties from securing timely and prompt resolution and will do little to motivate parties to undertake Arbitration as a matter of dispute resolution mechanism as it will be on par with overburdened courts of the land.