IN THE HIGH COURT OF DELHI AT NEW DELHI

% Judgment delivered on: 29.05.2017

\+ **ARB.P. 21/2017**

AFCONS INFRASTRUCTURE LTD. ..... Petitioner

Versus

RAIL VIKAS NIGAM LIMITED ..... Respondent

Advocates who appeared in this case:

For the Petitioner : Mr P. Chidambaram and Mr Gopal Jain, Senior Advocates with Mr Manu Sheshadri, Ms Sahiba Ahluwalia, Mr Ishan Bisht and Mr Tanmay Nandi

For the Respondent: Mr N.K. Kaul, ASG with Mr Anil Seth, Mr Udit Seth, Mr Samar and Ms Hansa Kaul.

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HON'BLE MR JUSTICE VIBHU BAKHRU

JUDGMENT

VIBHU BAKHRU, J

1. The petitioner (hereinafter referred to as 'Afcons') has filed the present petition under Section 11(6) of the Arbitration and Conciliation Act, 1996 (hereinafter 'the Act') *inter alia* praying that an arbitrator be appointed - on behalf of the respondent, Rail Vikas Nigam Limited (RVNL) - for adjudicating the disputes that have arisen between the parties in relation to the agreement dated 12.12.2011.

2. The controversy involved in the present case essentially relates to the question whether former employees of the parties are disqualified for

being appointed as arbitrators by virtue of Section 12(5) of the Act and whether the procedure for appointment of an arbitral tribunal is required to be rejected in its entirety as it entails appointment of serving officers of RVNL/Railways as arbitrators.

3. Briefly stated, the relevant facts necessary to address the controversy are as under :

3.1 Afcons is a company incorporated under the Companies Act, 1956 and is engaged in the business of undertaking large infrastructure projects, including construction of roads, bridges, jetties, railway lines, tunnels etc. RVNL is a Government of India Undertaking created to undertake projects pertaining to strengthening of Golden Quadrilateral and Port Connectivity. RVNL issued a Notice Inviting Tender dated 27.06.2013, inviting bids from interested parties for the work of "*Construction of Viaduct including related works for 5.16 km length excluding station areas from Ch. 12570.00 to Ch. 18630.00 between Nicco Park to CBD- 1, in New Garia-Airport Corridor of Kolkata Metro Railway Line*" (hereafter 'the works'). Afcons' bid, submitted pursuant to the Notice Inviting Tender, was accepted and a Letter of Award dated 21.10.2011 (hereafter 'the LOA') in respect of the works for a total consolidated value of ₹2,12,54,73,130/-, was issued in favour of Afcons. Subsequently, the parties entered into a Contract Agreement dated 12.12.2011 (hereafter 'the agreement') for the afore-mentioned works.

3.2 Admittedly, certain disputes have arisen in relation to the aforesaid agreement. The same includes an arbitration clause, the relevant extract of which is quoted as under:

"17.3Arbitration

Any dispute in respect of which amicable settlement has not been reached arising between the Employer and the Domestic or Foreign Contractor related to any matter arising out of or connected with this contract, the disputes shall be settled in accordance with the Indian Arbitration Act, 1996 and any statutory modification or re-enactment thereof. Further, it is agreed between the parties as under:

(i) **Number of Arbitrators**: The arbitral tribunal shall consist of 3 (Three) arbitrators.

(ii) **Procedure for Appointment of Arbitrators**: The arbitrators shall be appointed as per following procedure:

(a) Employer will forward a panel of 5 names to the contractor and contractor will give his consent for any one name out of the panel to be appointed as one of the Arbitrators.

(b) Employer will decide the second Arbitrator out of the remaining four names in the panel as mentioned in Para (a) above.

(c) The third Arbitrator shall be chosen by the two Arbitrators so appointed by the parties and shall act as Presiding Arbitrator. In case of failure of the two Arbitrators appointed by the parties to reach upon consensus within a period of 30 days from the appointment of the Arbitrators subsequently appointed, then, upon the request of either or both parties, the presiding Arbitrator shall be appointed by the Managing Director, Rail Vikas Nigam Limited, New Delhi.

(iii) **Qualification and Experience of Arbitrators**: The arbitrators to be appointed shall have minimum qualification and experience as under:

(a) One member of the tribunal shall be necessarily a working (not below the rank of SAG) or a

retired officer (retired not below the rank of SAG, age not exceeding 70 years and in reasonably good mental and physical fitness) of Indian Railway Accounts Service , having experience in financial matters related to construction contracts.

b) One member shall be a technical person having degree in Engineering and may be working (not below the rank of SAG) or retired officer (retired not below the rank of SAG, age not exceeding 70 years and in reasonably good mental and physical fitness) of any Engineering service of Indian Railways or equivalent service in RVNL, and having knowledge and experience of the Railway working.

(c) The Presiding Arbitrator shall necessarily be a serving railway/RVNL officer and he shall have same minimum qualification and experience as specified above for either of the two arbitrators.

(d) Out of 3 Arbitrators not more than one shall be a retired officer.

(iv) No person other than the persons appointed as per above procedure and having above qualification and experience shall act as arbitrator.

(v) Neither party shall be limited in the proceedings before such arbitrators to the evidence nor did arguments previously put before."

3.3 In view of the disputes, Afcons, by a letter dated 17.11.2016, issued a notice of dissatisfaction along with intimation of its intention to commence arbitration. Afcons contended that by virtue of the Arbitration and Conciliation (Amendment) Act, 2015 (hereafter 'the amendment act'), the procedure for appointment of the arbitral tribunal - as per the agreement - had been rendered *ultra vires* and the same was against the

mandatory provisions of the amendment act, which required the arbitrators to be appointed only in terms of the restrictions imposed by the Fifth and Seventh Schedule to the Act. Thus Afcons nominated Justice Aloke Chakrabarti (Retd.), a former judge of the Calcutta High Court, as its nominee arbitrator and called upon the RVNL to appoint its nominee arbitrator within a period of 30 days from receipt of the said letter.

3.4 RVNL responded to the aforesaid letter by a letter dated 15/12/2016 proposing a panel of 5 arbitrators - which included names of retired officers of the Railways and RVNL - and called upon the Afcons to select one name out of the said panel in terms of sub clause (ii) of clause 17.3 of the agreement so that RVNL could also select one name out of the 4 remaining arbitrators, as its nominee arbitrator. RVNL further stated that the panel as provided in the letter was as per the contractual procedure laid down in clause 17.3 of the agreement and does not violate the Act or the amendment act, including the Fifth and the Seventh Schedule. Thereafter, on 19.12.2017, Afcons sent a letter to the Chairman and Managing Director, RVNL stating that the letter dated 15.12.2016 was "*neither in terms of the contract nor the law*".

3.5 In view of the above, Afcons has filed the present petition on 09.01.2017.

Submissions

4. Mr Chidambaram, learned senior counsel appearing for Afcons contended that the arbitration clause was *ultra vires* Section 12(5) of the Act since it entailed an arbitral tribunal of three arbitrators out of which at least two were required to be serving officers of RVNL. He submitted that this was no longer permissible by amendment of Section 12(5) of the Act. Thus, the arbitral tribunal was required to be appointed by this Court. He

submitted that it was not open for RVNL to unilaterally insist on appointment of retired officers of Railways/RVNL as that would amount to rewriting the contract. Further RVNL could not insist on appointment of retired officers without the consent of Afcons. Next he contended that RVNL was an integral part of the Railways. He referred to the organization chart of the Railways, the website of RVNL, the Articles of Association of RVNL and other documents in support of his contention that the Railways exercise an absolute control over the affairs of RVNL. Lastly, he contended that appointment of former employees of RVNL/Railways falls foul of Entry 1 of Schedule 7 to the Act. He contended that past employment would fall within the scope of past business relationship and thus relationship of former employees with their past employer fell within the prohibited category of Entry 1 of Schedule 7 of the Act. It was submitted that the Afcons would be agreeable if an arbitral tribunal consisting of Retired Supreme Court Judges is appointed by this court.

5. Mr Kaul, learned ASG appearing for RVNL countered the submissions advanced on behalf of Mr Chidambaram.

6. First, he submitted that clause 17.3 of the agreement was mandatory in nature and has to be strictly followed. He relied upon the decision of the Supreme Court in ***Shin Satellite Public Co. Ltd v. Jain Studios Ltd.***: ***(2006) 2 SCC 628*** in support of his contention that if any part of a clause violates the law and that part of clause can be severed/ignored without affecting other parts thereof, the remaining part would be binding on the parties. He submitted that entry no (C) of Sub-clause (iii) of clause 17.3 - which mandates the presiding arbitrator to necessarily be a serving

Railway/RVNL officer and violates Schedule V and VII of the Act - can be severed from the rest of Sub-clause (iii) of clause 17.3 and therefore, rest of the qualifications as mentioned in the said sub-clause have to be strictly followed. He submitted that similarly, entry (D) of Sub-clause (iii) of clause 17.3, which requires that out of 3 arbitrators, not more than one shall be a retired officer, would have to be severed from the arbitration clause.

7. Second, he submitted that appointment of Retired officers of the Railways/RVNL would not violate Schedule V and VII of the Act. He relied on the decisions of the Supreme Court in ***Voestalpine Schienen GMBH v. Delhi Metro Rail Corporation Limited: AIR 2017 SC 939*** and **Ircon International Ltd. v. PNC Jain Corporation:** ***(Civil Appeal No. 2840/2017)*** and of this court in ***Hindustan Construction Co Ltd v Ircon International Ltd.*** : ***2016 SCC Online 6073*** and ***M/s Era- Patel- Advance-Kiran (JV) v. Rail Vikas Nigam Limited : (Arb. P. 763/2016 order dated 21.12.2016)*** in support of his contention.

8. Third, he submitted that RVNL is a distinct and a separate entity, even though 100% shareholding of RVNL is held by the Railways. He relied on the decision in the case of ***Electronics Corporation of India Limited and Ors v. Secretary, Revenue Department, Government of Andhra Pradesh and Ors. :(1999)4 SCC 458***.

Reasoning and Conclusion

9. It is common ground between the parties that a part of the arbitration clause is *ultra vires* Section 12(5) of the Act and that the doctrine of severability is applicable to sever the offending part of the arbitration

clause and enforcing the remaining agreement. Both the parties are committed for referring the disputes to arbitration. They also concur that by virtue of Section 12(5) of the Act read with Seventh Schedule to the Act, a serving officer of the Railways/ RVNL is ineligible for being appointed as an arbitrator.

10. The controversy that remains is whether the entire procedure for appointing an arbitral tribunal - which also includes sub-clause 17.3(ii) of the agreement - has become void and has to be discarded; or, only sub-clause 17.3(iii) of the agreement, which prescribes for qualification and experience for arbitrators is to be disregarded. Whereas Afcons claims that RVNL cannot unilaterally substitute the selection process by limiting the selection of arbitrators to former employees of Railways/ RVNL as that would amount to re-writing the contract, RVNL disputes the same. According to RVNL, sub clause 17.3(iii) of the agreement is now void as it is *ultra vires* Section 12(5) of the Act and, therefore, needs to be ignored; however, sub-clause 17.3(ii) of the agreement, which prescribes the procedure for appointment of arbitrators, does not offend any provision of the Act and, thus, is enforceable and binding.

11. It is well settled that the doctrine of severability or the Blue Pencil Rule is applicable where a part of the contract, which is void or unenforceable, can be severed from the main contract without affecting the substantial agreement between the parties. In ***Shin Satellite*** (*supra*), the Supreme Court had held that "*it is the duty of the court to severe and separate trivial or technical part by retaining the main or substantial part and by giving effect to the latter if it is legal, lawful and otherwise enforceable. In such cases, the Court must consider the question whether*

the parties could have agreed on the valid terms of the agreement had they known that the other terms were invalid or unlawful. If the answer to the said question is in the affirmative, the doctrine of severability would apply and the valid terms of the agreement could be enforced, ignoring invalid terms."

12. It is also well settled that the Blue Pencil Doctrine (or the doctrine of severability) would apply to cross out (by running a blue pencil across) that part of the contract, which is invalid and unenforceable without affecting the other part of the contract. It is also trite law that only that part, which is void or unenforceable (and no more) would be deleted in order to save the validity of the contract, without affecting the substratal bargain between the parties. Under the Blue Pencil Doctrine, it is only the bare minimum, which is necessary to make the contract reasonable, is to be deleted or ignored.

13. In the present case, there is no dispute that clause 17.3(iii), which prescribes for qualification of the members of arbitral tribunal, is no longer valid and, therefore, should be deleted / ignored. However, the procedure for appointment of arbitrators as contained in clause 17.3(ii) clearly does not offend any provision of the Act and, thus, the Blue Pencil Doctrine cannot be applied to delete or ignore the said sub-clause.

14. The fact that serving officers of RVNL/Railways cannot be appointed as arbitrators, does not itself frustrate the procedure for constitution of the arbitral tribunal as contained in clause 17.3(ii) of the agreement. Thus, RVNL (Employer) retains the right to forward a panel of five names to the contractor (in this case Afcons) to choose any one to be appointed as an arbitrator. In the facts of the present case, RVNL did

forward a panel of five persons for Afcons to choose one, to be appointed as the arbitrator. This procedure was in terms of the agreement between the parties.

15. All five names that are suggested by RVNL were former employees of the Railways/RVNL and this gives rise to the second question, that is; whether former employees of a party are ineligible for being appointed as arbitrators by virtue of Section 12(5) of the Act read with the Seventh Schedule to the Act. In this context, it was contended that RVNL is an independent company and has its separate identity, thus, former employees of Railways cannot be stated to have any connection with RVNL so as to disqualify them from being appointed as arbitrators. Whilst it is correct that RVNL is an independent company, it is difficult to accept that it can be considered as separate from the Railways.

16. Indisputably, Railways exercise a pervasive control in respect of the affairs of RVNL. RVNL was established as a "*Special Purpose Vehicle*" to undertake project development, mobilization of financial resources and implementation of projects pertaining to strengthening of Golden Quadrilateral & Diagonals, Port Connectivity and other railway infrastructure projects. The expression "*Special Purpose Vehicle*" only indicates that RVNL has been created to undertake a specified function of the Railways. The organisation structure of the Railways as available on the official website of the Ministry of Railways, Government of India clearly indicates that the Railway Board is directly in-charge of various other units including RVNL and certain other PSUs. The projects undertaken by RVNL are for the Railways and are in terms of the budget

allocations provided by the Railways. The projects after being executed are also handed over to the concerned railway departments.

17. Article 66 of the Articles of Association of RVNL empower the President of India to appoint all directors including Full Time Chairman, Managing Director, other Directors, part time Directors, and Government Directors (in other words, all directors) on the Board of RVNL. It is also specified that the Directors appointed would hold office until removed. Thus, the Ministry of Railways has full control over appointment and removal of the Directors of RVNL. In terms of Article 67 of the Articles of Association of RVNL, the Board of Directors is to manage the affairs of RVNL subject to the directives issued by the President from time to time.

18. The Senior Management of RVNL are also officers from the various services of the Indian Railways. The profile of the Board of Directors of RVNL as downloaded from its website indicates that the Chairman and the Managing Director as well as the Director Projects are from the cadres of the Indian Railways Service of Engineers. The Director (Personnel) is from Indian Railways Personnel Service and the Director (Operations) is from Indian Railway Traffic Service. It is, thus, seen that the Management of RVNL are/were also officers to the Railways. Although, RVNL has a cadre of its own, but the majority of its cadre is also drawn from the employees of the Railways. Afcons has also produced Office Orders issued by Ministry of Railways granting non-functional upgradation to various officers in the Railways which include officers serving in RVNL, thus, indicating that the service conditions of the employees of RVNL sent on deputation are also managed by the Railways.

19. RVNL is also a "railway administration" under the provisions of the Railways Act, 1989. Keeping the totality of circumstances in view, it would be very difficult to accept that RVNL should not be considered as an arm of the Indian Railways.

20. Thus, the issue whether former employees of the Railways could be appointed as arbitrators has to be considered in the aforesaid context. Keeping in view the objective of Section 12 of the Act read with the Fifth and the Seventh Schedule to the Act, no distinction can be drawn between former employees of RVNL and former employees of the Railways.

21. According to Afcons, former employees of a party are disqualified to act as arbitrators by virtue of Section 12(5) of the Act read with Entry - 1 of the Seventh Schedule, which reads as under:-

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

22. A plain reading of the aforesaid entry indicates that a person who is related to a party as an employee, consultant or an advisor, is disqualified to act as an arbitrator. In addition, an arbitrator which has *"other"* past or present business relationship with the party is also disqualified. The word *"other"* is obviously used to indicate a relationship other than an employee, consultant or an advisor. Thus, on a plain reading, the relationship of being a former employee would not fall within Entry - 1 of the Seventh Schedule. The expression "business relationship" as used in Entry 1 of the Seventh Schedule cannot be understood to include an employer-employee relationship. This is also the view expressed by the Punjab and Haryana

High Court in ***Reliance Infrastructure Ltd. v. Haryana Power Generation Corporation Ltd.:*** ***2016 (6) ArbLR 480 (P&H)***.

23. Having stated the above, it is also necessary to add a caveat that merely because an arbitrator is not disqualified under Section 12(5) read with Seventh Schedule of the Act, does not necessarily mean that his appointment cannot be challenged if there are other grounds which give rise to justifiable doubts as to his independence or impartiality. For instance if a former employee has been given other assignments by the employer or had an involvement with the project in connection with which the disputes arise, his appointment may be challenged under the procedure prescribed under Section 13 of the Act.

24. Having stated the above, it is also necessary to refer to the other decision of the Supreme Court in ***Voestalpine Schienen*** *(supra)*. In that case, the Supreme Court was considering an application under Section 11 of the Act for appointment of an arbitrator in respect of the disputes that had arisen in respect of an Austrian Company and the Delhi Metro Rail Corporation Ltd. (DMRC). In that context, the court had observed that persons retired from the Government or other statutory corporations or Public Sector undertakings, who had "*no connection with DMRC"* would not be ineligible for being appointed as an arbitrator. The Supreme Court explained that Section 12 of the Act was amended by the Arbitration and Conciliation (Amendment) Act, 2015 keeping in view the recommendations of the Law Commission made in its 246th Report. The legislative intent in introducing amendments to Section 12 of the Act was to ensure neutrality of arbitrators.

25. In ***Voestalpine's*** case, the arbitration clause provided DMRC to forward a panel of five members for the petitioner to choose any one of them for being appointed as an arbitrator. The Supreme Court frowned on the said procedure and struck down the clause, which required the petitioner to choose from only one out of the five names as suggested by DMRC. The relevant extract of the said decision is set out below:-

> "Before we part with, we deem it necessary to make certain comments on the procedure contained in the arbitration agreement for constituting the arbitral tribunal. Even when there are number of persons empanelled, discretion is with the DMRC to pick five persons therefrom and forward their names to the other side which is to select one of these five persons as its nominee (Though in this case, it is now done away with). Not only this, the DMRC is also to nominate its arbitrator from the said list. Above all, the two arbitrators have also limited choice of picking upon the third arbitrator from the very same list, i.e., from remaining three persons. This procedure has two adverse consequences. In the first place, the choice given to the opposite party is limited as it has to choose one out of the five names that are forwarded by the other side. There is no free choice to nominate a person out of the entire panel prepared by the DMRC. Secondly, with the discretion given to the DMRC to choose five persons, a room for suspicion is created in the mind of the other side that the DMRC may have picked up its own favourites. Such a situation has to be countenanced. We are, therefore, of the opinion that sub-clauses (b) & (c) of clause 9.2 of SCC need to be deleted and instead choice should be given to the parties to nominate any person from the entire panel of arbitrators. Likewise, the two arbitrators nominated by the parties should be given full freedom to choose third arbitrator from the whole panel."

26. The Supreme Court had further directed that instead of only serving or retired engineers of government departments, DMRC should broad base

the panel by appointing persons with legal background like judges and lawyers of repute and also persons from the field of accountancy. A plain reading of the said decision indicates that the Supreme Court had issued such directions as it considered that it was necessary to instill confidence in the arbitral process.

27. The arbitration clause in the present case also has a similar provision where the petitioner is restricted to select only one of the five names as suggested by RVNL. Further, the panel of RVNL, which is not disclosed, apparently consists of only former or serving employees of Railways/RVNL. It is also seen that all five persons who have been suggested by RVNL are ex-employees of Railways/RVNL.

28. In view of the aforesaid, there is little doubt that RVNL had to also broad base their panel and follow the Supreme Court's view as expressed in ***Voestalpine Schienen*** *(supra)*. Restricting the panel to only former employees of Railways/ RVNL would do little to instill any confidence in the arbitral process.

29. As pointed out by the Supreme Court in ***Voestalpine Schienen*** *(supra)*, clause restricting the petitioner to choose only one out of the five names forwarded by RVNL would have adverse consequences which need to be countenanced.

30. There is yet another aspect that needs to considered. Afcons had also referred to the guidelines issued by the Railway Board for appointment of retired railway officers as arbitrators - which is admittedly followed by RVNL - and drew the attention of this court to paragraph 8 of the said guidelines which required the General Manager to keep a watch on the

performance of the arbitrator and if he found that the arbitrator "*does not appear to be fair*", he would consider deleting arbitrator's name from the panel for the subsequent period. It is understandable that such stipulations would also be discomforting to other party seeking to refer the dispute to arbitration. The arbitration is an adversarial process. It is possible that the impartiality of an arbitrator would appear to be compromised if it is perceived that he does not want to appear as unfair to a particular party (in this case RVNL) for the fear of losing the opportunity to be appointed as an arbitrator in future.

31. It is well settled that in given cases, the court may disregard the agreed procedure to secure the appointment of an impartial arbitrator. (See: ***Union of India v. Uttar Pradesh State Bridge Corporation Limited: (2015) 2 SCC 52***).

32. This court is of the view that it would be in the interest of securing an independent and impartial arbitral tribunal if the procedure under clause 17.3(ii) is disregarded. This is, essentially, for three reasons. First, the decision of the Supreme Court that the procedure that limits the party's choice to select only one out of the five persons suggested by the other party has *"adverse consequences"* and needs to be countenanced.

33. Second, that RVNL has only suggested the names of former employees of Railways/RVNL for appointment of an arbitrator. Thus, all persons have a past relationship (however remote) with RVNL/Railways. Such relationship may not fall within the rigour of Section 12(5) of the Act read with the Seventh Schedule to the Act, but undeniably does give rise to apprehensions (whether justifiable or not) in the minds of the other party. It is essential that all parties have full confidence with the arbitral process.

34. And third, the General Manager does wield the power to remove the arbitrator from panel if it appears to him that the arbitrator is unfair; thus depriving him of further work.

35. The petitioner has indicated that it would be willing if any former judge of the Supreme Court may be appointed as an arbitrator. Thus RVNL may appoint any former Judge of the Supreme Court as an arbitrator on behalf of the petitioner within a period of two weeks. RVNL will also nominate its arbitrator within a period of two weeks from today. Both the arbitrators shall concur on appointment of a third arbitrator. If RVNL fails to appoint the arbitrators or if the arbitrators fail to concur on appointment of a third arbitrator, the petitioner would be at liberty to approach this court.

36. The petition is disposed of with the aforesaid directions.

VIBHU BAKHRU, J

MAY 29, 2017
MK/RK