SHYAM SUNDER AGARWAL

v.

P. NAROTHAM RAO AND ORS.

(Civil Appeal No. 6872 of 2018)

JULY 23, 2018

[R. F. NARIMAN AND INDU MALHOTRA, JJ.]

Arbitration and Conciliation Act, 1996 – Memorandum of Understanding (MoU)/Agreement executed between the parties for sale and purchase of shares of a Company – Issue as to whether Clause 12 of the said Agreement can be stated to be an arbitration clause – Held: On reading of various clauses it is clear that two persons though, styled as Mediators/Arbitrators, are escrow agents who were appointed to keep certain vital documents in escrow, and to ensure a successful completion of the transaction contained in the MOU – The very fact that they were referred to as "Mediators/ Arbitrators" and as "Mediators and Arbitrators" would show that the language used is loose – The idea really was that the two named persons do all things necessary during the implementation of the transaction between the parties to see that the transaction gets successfully completed – Clause 8 makes it clear that the idea was to prevent disputes from occurring and to ensure smooth implementation of the Agreement – Object was not to adjudicate disputes but to prevent them – Clause 12 has to be read in the light of Clauses 8 and 11 of the MOU, and therefore, the expression "decision" used in Clause 12 is only a pro tem *decision, namely, that the two escrow agents were to make decisions only during the period of the transaction and not thereafter – They were "functus officio" after the transaction got completed – Wording of the Agreement, is clearly inconsistent with the view that the Agreement intended that disputes be decided by arbitration – Further, indeed, three of the four purchasers of shares did not read Clause 12 as an arbitration clause, but approached the Civil Court instead – Discretionary jurisdiction u/Art.136 not exercised – Constitution of India – Art.136.*

Disposing of the appeal, the Court

HELD: 1.1 On a conspectus of reading of Clauses 6, 8, 10, 11 and 12 it emerges that Mr. SR and Mr. GPR, though styled as

Mediators/Arbitrators, were without doubt escrow agents who were appointed to keep certain vital documents in escrow, and to ensure a successful completion of the transaction contained in the MOU. Indeed, the very fact that they were referred to as "Mediators/Arbitrators" and as "Mediators and Arbitrators" would show that the language used was loose – the idea really was that the two named persons do all things necessary during the implementation of the transaction between the parties to see that the transaction gets successfully completed. Clause 8 expressly declared and confirmed "that for successful completion of this transaction in order to avoid any further unforeseen litigations", the two escrow agents were appointed. Clause 11 further made it clear that these two gentlemen were escrow agents but shall not handover certain documents till the total transaction is satisfactorily completed. Clause 12 has to be read in the light of these Clauses of the MOU, and that, therefore, the expression "decision" used in Clause 12 is only a *pro tem* decision – namely, that the two escrow agents were to make decisions only during the period of the transaction and not thereafter. They were "*functus officio*" after the transaction got completed. Further, the "breaches" that were referred to in Clause 12 refer, *inter alia,* to an undertaking given by the party of the first part which was contained in Clause 10, which, if breached, the escrow agents have necessarily to decide on before going ahead with the transaction. Therefore, when viewed as a whole, it is clear that the two escrow agents were not persons who were to decide disputes that may arise between the parties, whether before or after the transaction is completed, after hearing the parties and observing the principles of natural justice, in order to arrive at their decision. A reading of the MOU as a whole leaves no manner of doubt that the said MOU only invests the two gentlemen named therein with powers as escrow agents to smoothly implement the transaction mentioned in the MOU and not even remotely to decide the disputes between the parties as Arbitrators. [Paras 9, 10] [1142-H; 1143-A-F]

1.2 In the present case, it is clear that the wording of the Agreement was clearly inconsistent with the view that the Agreement intended that disputes be decided by arbitration. Indeed, three of the four purchasers did not read Clause 12 as an

arbitration clause, but approached the Civil Court instead, strengthening the conclusion that the subsequent conduct of the parties to the Agreement also showed that they understood that Clause 12 was not an arbitration clause in the Agreement. Clause 8 of the MOU made it clear that the idea was to prevent disputes from occurring and to ensure smooth implementation of the Agreement, thereby making it clear that the object was not to adjudicate disputes but to prevent them.[Paras 11, 12] [1145-C, E]

1.3 The conduct of the appellant leaves much to be desired. Having issued a notice for arbitration way-back on 24.05.2007, there was no reason whatsoever to delay a Section 11, Arbitration and Conciliation Act, 1996 application for a period of two and a half years until December, 2009. The appellant knew that Clause 12 could not possibly be construed as an arbitration clause, yet somehow sought to delay the proceedings not joining his brethren in the civil suit that was filed by them. Equally, his conduct during the pendency of the Section 11 petition leaves a lot to be desired. Even before judgment was pronounced in the Section 11 petition on 22.07.2011, the Appellant approached another forum, namely, the Company Law Board on 16.06.2011, for reliefs based upon the MOU. He, thereafter, continued with the Company Petition which would have led this Court to believe that he was abandoning any further recourse against the judgment dated 22.07.2011, but then on second thoughts, filed a Special Leave Petition with a delay of 358 days against the judgment rejecting his Section 11 petition on 22.07.2011. During the pendency of the Special Leave Petition as well, his conduct leaves much to be desired. On 24.01.2017, he asked that his petition that was filed before the Company Law Board be withdrawn not with the liberty to pursue arbitration, as one would have expected, but with the liberty to file a fresh company petition on the same set of facts. Thus, apart from decision on merits, discretionary jurisdiction under Article 136 of the Constitution also not exercised. [Para 13] [1145-F-H; 1146-A-B]

Bihar State Mineral Development Corporation v. Encon Builders (I) (P) Limited **(2003) 7 SCC 418 : [2003] 2 Suppl. SCR 812 – relied on.**

A *P. Dasaratharama Reddy Complex v. Government of Karnataka and Another* **(2014) 2 SCC 201 : [2013] 14 SCR 579 ;** *K.K. Modi v. K.N. Modi* **(1998) 3 SCC 573 : [1998] 1 SCR 601 ;** *State of U.P. v. Tipper Chand* **(1980) 2 SCC 341 – referred to.**

B **Case Law Reference**

[2013] 14 SCR 579	**referred to**	**Para 5**
[1998] 1 SCR 601	**referred to**	**Para 5**
(1980) 2 SCC 341	**referred to**	**Para 11**
C **[2003] 2 Suppl. SCR 812**	**relied on**	**Para 12**

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 6872 of 2018.

From the Judgment and Order dated 22.07.2011 of the High Court D of Judicature, Andhra Pradesh at Hyderabad in Arbitration Application No. 112 of 2009.

Guru Krishnakumar, Amit Sibal, Sr. Advs., M. Srinivas R. Rao, Abid Ali Beeran P., Mrs. Sudha Gupta, D. Bharat Kumar, Nitish Bandari, Tadimalla Bhaskar Gowtham, Aman Shukla, Sayooj Mohandas M., Abhijit E Sengupta, Rana S. Biswas, Sunil Kr. Sharma, Ms. Sharmila Upadhyay, T. Srinivasa Murthy, Senthil Jagadeesan, Ms. Suriti Chowdhary, K.S. Mahadevan, Krishna Kumar R.S, Ms. Swati Bansal, Rajesh Kumar, Advs. for the appearing parties.

The Judgment of the Court was delivered by

F **R. F. NARIMAN, J.** 1. Leave granted.

2. The present dispute arises out of a Memorandum of Understanding (MoU)/Agreement executed between the parties dated 08.12.2005 for sale and purchase of shares of a Company called M/s Mancherial Cement Company Private Limited of which all the parties G are Directors. The bone of contention in the present proceedings is as to whether Clause 12 of the said Agreement can be stated to be an arbitration clause.

3. Heard the learned Senior Counsel appearing for the parties at considerable length.

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4. Mr. Guru Krishnakumar, learned Senior Advocate, appearing on behalf of the Appellant has brought to our notice the said MOU in which he relies, in particular, upon Clause 12. According to him, the language of the said clause is language that leads inevitably to the conclusion that the said clause is an arbitration agreement. The word "decision" is used; the word "Mediators/Arbitrators" is used; the expression "any breaches" is used; and the "decision" is to be final and binding on all parties to the said Agreement. Based on these words, in particular, the learned Senior Advocate argues that the three essentials of an arbitration clause have been met, namely, that there must be disputes between the parties which have to be adjudicated upon by giving the parties a hearing, at the end of which there is a decision which is final and binding between the parties. He also argued that the MOU read as a whole would not militate against his argument given the words used in Clause 12.

5 The learned Senior Advocate then relied upon a judgment of this Court in ***P. Dasaratharama Reddy Complex*** vs. ***Government of Karnataka and Another***, (2014) 2 SCC 201, and distinguished judgments cited therein by stating that in the arbitration clause that was considered in that case, it was clear that clauses of earlier judgments of this Court either spoke of a preliminary decision which was then subject to a final decision by a Court or spoke of decisions that had to be rendered only "for the time being". According to him, his case was entirely different, and therefore, he would squarely fall within the parameters laid down by the judgment in ***K.K. Modi*** vs. ***K.N. Modi***, (1998) 3 SCC 573.

6. Mr. Amit Sibal, learned Senior Advocate on behalf of the Respondent Nos. 1 to 4, is at pains to point out that the MOU, read as a whole, makes it clear that the expression "Mediators/Arbitrators" is used loosely. In fact, the two gentlemen said to be arbitrators, Mr. K. Sudhakar Rao and Mr. Gone Prakash Rao, are escrow agents who have with them the custody of three sets of documents to ensure successful implementation of the MOU. He relied strongly upon Clauses 6, 8, 10 and 11 and stated that these must be read along with Clause 12 so that it is clear that the expression "decision" must be read only with "during the period of entire transaction" and has reference to breaches that may occur under Clause 10, as parties of the first part undertake to substitute personal guarantees given by parties of the second part with personal guarantees of their associates, and that if this is not done, then a "decision" is to be taken by the escrow agents as to what to do next.

A 7. Mr. Sibal also pointed out that three other purchasers of shares, who were sailing in the same boat as the present Appellant, had gone to the Civil Court and had filed O.S. No. 241 of 2017, which has since been dismissed in default. He also points out that the entire exercise before us is a *mala fide* exercise by the Appellant to hedge his bets by first issuing a notice in 2007 under the said MOU as if the said MOU contained an arbitration clause, but following it up only two and a half years later by filing a Section 11 petition in December 2009. He also stated that while the Section 11 petition was pending, the Appellant had filed a Company Petition No. 49 of 2011 on 16.06.2011 in which he asked for reliefs that flow directly out of the said MOU. This Company Petition was again withdrawn by him on 24.01.2017 in order to file a fresh Company Petition on the same set of facts, thereby showing or indicating willingness to continue with the remedy in company law as against the remedy in arbitration. He also pointed out to us that his own clients had gone in a Company Petition to the Company Law Board, and had succeeded in the Company Petition by getting the necessary reliefs on 16.03.2016 as the Appellant was in no mood, from the very beginning, to implement the terms of the MOU. We are told that an appeal is pending before the High Court, having been filed by the Appellant against the aforesaid order. He also argued that he was seriously prejudiced by the fact that the Appellant continues to hedge his bets and, in fact, filed a Special Leave Petition against the impugned order, belatedly, with a delay of 358 days. According to Mr. Sibal, therefore, not only is it clear that the MOU does not contain any arbitration clause but equally, given our discretionary jurisdiction under Article 136, we ought not interfere in the facts of this case.

8. Having heard the learned Senior Counsel for the parties, it is necessary to first set out some of the clauses of the MOU executed between the parties. Clause 3 declares that the parties have reached a settlement, as a result of which certain shares have to be sold in the Company, so that the internal disputes within the Company may end, in order that the Company purchase certain assets of yet another Company. Equally, Clauses 6, 8, 10, 11 and 12 are of importance and are set out herein below:-

> "6. The parties of 1st part hereby handed over 9 cheques favouring Sri P. Narotham Rao as detailed below to Sri K. Sudhakar Rao S/o Late Sri K. Madhava Rao, R/o Plot No.7, UBI Colony, Road

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No.3, Banjara Hills, Hyderabad and Sri Gone Prakash Rao S/o Gone Chalapathi Rao R/o Transport Guest House, Tarnaka, Hyderabad Mediators/Arbitrators.

	Particulars of Cheque		Amount
Date	Ch. No.	Bank & Branch Holder Name	
09.12.2005	450547	Andhra Bank, St. John's EM High School Branch, Karimnagar of S. Hareender Rao	Rs.25,00,000/-
09.01.2006	450543	Andhra Bank, St. John's EM High School Branch, Karimnagar of S. Hareender Rao	Rs.78,12,500/-
09.01.2006	450444	HDFC Bank, Himayathnagar Branch, Hyderabad of Shyam Sunder Agarwal	Rs.78,12,500/-
09.02.2006	450544	Andhra Bank, St. John's EM High School Branch, Karimnagar of S. Hareender Rao	Rs.78,12,500/-
09.02.2006	450445	HDFC Bank, Himayathnagar Branch, Hyderabad of Shyam Sunder Agarwal	Rs.78,12,500/-
09.03.2006	450545	Andhra Bank, St. John's EM High School Branch, Karimnagar of S. Hareender Rao	Rs.78,12,500/-
09.04.2006	450546	Andhra Bank, St. John's EM High School Branch, Karimnagar of S. Hareender Rao	Rs.78,12,500/-
09.04.2006	450447	HDFC Bank, Himayathnagar Branch, Hyderabad of Shyam Sunder Agarwal	Rs.78,12,500/-

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A 8. The parties hereinabove declare and confirm that for successful completion of this transaction in order to avoid any further unforeseen litigations, both the parties hereby mutually appointed Sri K. Sudhakar Rao S/o Sri Late Sri K. Madhava Rao, R/o Plot No.7, UBI Colony Road No.3, Banjara Hills, Hyderabad and Sri Gone Prakash Rao S/o Gone Chalapathi Rao R/o Transport Guest
B House, Tarnaka, Hyderabad as mediators and arbitrators to whom the above cheques as well as all other following documents are handed over and the same will be under their custody till satisfactory completion of the entire transaction as per the terms and conditions contained herein.

C a) Above referred 9 cheques

b) The share certificates along with the duly signed transfer deeds pertaining to 22,40,000 equity shares of parties of 2nd part and their associates.

D xxx xxx xxx

10. The parties of 1st part further agree and undertake to substitute the personal guarantees given by the parties of 2nd part with the personal guarantors of their associates with M/s Andhra Bank within two months from the date of this document.

E 11. Till the total transaction is satisfactorily completed and till entire sale consideration is paid and till the personal guarantees of parties of 2nd part are substituted by the personal guarantees of the Associates of parties of First Part with M/s Andhra Bank, the above named Arbitrators/Mediators shall not hand over the share
F certificate with duly signed share transfer deeds in respect of the shares of the parties of 2nd part to the parties of 1st part.

12. It is further agreed that any decision to be taken by said Mediators/Arbitrators during the period of entire transaction in the event of any breaches committed by either of the parties shall
G be final and binding on all the parties hereinabove."

9. What emerges on a conspectus of reading of these clauses is that Mr. Sudhakar Rao and Mr. Gone Prakash Rao, though styled as Mediators/Arbitrators, are without doubt escrow agents who have been appointed to keep certain vital documents in escrow, and to ensure a successful completion of the transaction contained in the MOU. Indeed,
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the very fact that they have been referred to as "Mediators/Arbitrators" and as "Mediators and Arbitrators" would show that the language used is loose – the idea really is that the two named persons do all things necessary during the implementation of the transaction between the parties to see that the transaction gets successfully completed. This becomes even clearer when Clauses 8 and 11 are seen minutely. Clause 8 expressly declares and confirms "that for successful completion of this transaction in order to avoid any further unforeseen litigations", the two escrow agents have been appointed. Clause 11 further makes it clear that these two gentlemen are escrow agents but shall not handover certain documents till the total transaction is satisfactorily completed.

10. We agree with Mr. Sibal that Clause 12 has to be read in the light of these Clauses of the MOU, and that, therefore, the expression "decision" used in Clause 12 is only a pro tem decision – namely, that the two escrow agents are to make decisions only during the period of the transaction and not thereafter. He has correctly contended that, to use a well-known latin expression, they are "*functus officio"* after the transaction gets completed. Further, the "breaches" that are referred to in Clause 12 refer, *inter alia,* to an undertaking given by the party of the first part which is contained in Clause 10, which, if breached, the escrow agents have necessarily to decide on before going ahead with the transaction. Therefore, when viewed as a whole, it is clear that the two escrow agents are not persons who have to decide disputes that may arise between the parties, whether before or after the transaction is completed, after hearing the parties and observing the principles of natural justice, in order to arrive at their decision. A reading of the MOU as a whole leaves no manner of doubt that the said MOU only invests the two gentlemen named therein with powers as escrow agents to smoothly implement the transaction mentioned in the MOU and not even remotely to decide the disputes between the parties as Arbitrators.

11. This Court in ***P. Dasaratharama Reddy Complex (supra)*** referred to a large number of decisions of this Court in order to distinguish between clauses that were arbitration clauses and clauses that either led to expert determinations or were otherwise not arbitration clauses. For example, in para 17 of the judgment, the case of ***State of U.P***. vs. ***Tipper Chand***, (1980) 2 SCC 341 is referred to, in which this Court held that the Superintending Engineer was really vested with supervision of the execution of the work and administrative control which would not

render the clause an arbitration clause. Equally, the Court relied extensively on ***K.K. Modi*** (supra), which again made it clear that the Chairman of the IFCI, who is to decide all disputes in respect of implementation of the agreement and whose decision will be final and binding, could not be construed to be an arbitration clause, *inter alia,* for the reason that the clause does not invest the Chairman IFCI with quasi judicial powers to decide disputes between the parties, as it was only in respect of implementation of the agreement between the parties. Para 22 of the judgment is important, and sets out from ***K.K. Modi*** (supra) as to what are the valid pre-requisites for a valid arbitration agreement.

> "22. One of the questions formulated by this Court was whether Clause 9 of the memorandum of understanding constituted an arbitration agreement and whether the decision of the Chairman, IFCI constituted an award. The two-Judge Bench first culled out the following attributes of an arbitration agreement:
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> "17. … (1) The arbitration agreement must contemplate that the decision of the tribunal will be binding on the parties to the agreement,
>
> (2) that the jurisdiction of the tribunal to decide the rights of parties must derive either from the consent of the parties or from an order of the court or from a statute, the terms of which make it clear that the process is to be an arbitration.
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> (3) the agreement must contemplate that substantive rights of parties will be determined by the agreed tribunal.
>
> (4) that the tribunal will determine the rights of the parties in an impartial and judicial manner with the tribunal owing an equal obligation of fairness towards both sides.
>
> (5) that the agreement of the parties to refer their disputes to the decision of the tribunal must be intended to be enforceable in law and lastly,
>
> (6) the agreement must contemplate that the tribunal will make a decision upon a dispute which is already formulated at the time when a reference is made to the tribunal.
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> 18. The other factors which are relevant include, whether the agreement contemplates that the tribunal will receive evidence

from both sides and hear their contentions or at least give the parties an opportunity to put them forward; whether the wording of the agreement is consistent or inconsistent with the view that the process was intended to be an arbitration, and whether the agreement requires the tribunal to decide the dispute according to law."

In the present case, it is clear that the wording of the Agreement, as has been held by us above, is clearly inconsistent with the view that the Agreement intended that disputes be decided by arbitration. Indeed, three of the four purchasers did not read Clause 12 as an arbitration clause, but approached the Civil Court instead, strengthening our conclusion that the subsequent conduct of the parties to the Agreement also showed that they understood that Clause 12 was not an arbitration clause in the Agreement.

12. Equally, the decision in ***Bihar State Mineral Development Corporation*** vs. ***Encon Builders (I) (P) Limited***, (2003) 7 SCC 418 was referred to, and what is important in that judgment is that a clause which is inserted in an Agreement for the purpose of prevention of a dispute will not be an arbitration agreement. In the present case, Clause 8 of the MOU makes it clear that the idea was to prevent disputes from occurring and to ensure smooth implementation of the Agreement, thereby making it clear that the object was not to adjudicate disputes but to prevent them.

13. Mr. Sibal's contention that the conduct of the appellant leaves much to be desired is also correct. We are of the view that having issued a notice for arbitration way-back on 24.05.2007, there was no reason whatsoever to delay a Section 11 application for a period of two and a half years until December, 2009. The appellant knew that Clause 12 could not possibly be construed as an arbitration clause, yet somehow sought to delay the proceedings not joining his brethren in the civil suit that was filed by them. Equally, his conduct during the pendency of the Section 11 petition leaves a lot to be desired. Even before judgment was pronounced in the Section 11 petition on 22.07.2011, the Appellant approached another forum, namely, the Company Law Board on 16.06.2011, for reliefs based upon the MOU. He, thereafter, continued with the Company Petition which would have led us to believe that he was abandoning any further recourse against the judgment dated

A 22.07.2011, but then on second thoughts, filed a Special Leave Petition with a delay of 358 days against the judgment rejecting his Section 11 petition on 22.07.2011. During the pendency of the Special Leave Petition as well, his conduct leaves much to be desired. On 24.01.2017, he asked that his petition that was filed before the Company Law Board be withdrawn not with the liberty to pursue arbitration, as one would have B expected, but with the liberty to file a fresh company petition on the same set of facts. All this leads us to observe that, apart from the decision on merits, our discretionary jurisdiction under Article 136 of the Constitution also should not be exercised in favour of such a person.

14. The appeal is disposed of accordingly.

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Divya Pandey Appeal disposed of.