

AWARD OF INTEREST ON DAMAGES BY THE ARBITRATORS

In any arbitration proceeding in addition to direct claims of receivables, declaration, amounts due etc., the claim for interest on those due amounts and damages form an important part of the claim. The interest component is awarded as a damage for the loss incurred to the Claimant due to the delay in receiving the payments for the above said direct claims. In addition to the above said direct claims in most of the arbitrations there can be claim for damages also for breaches of contract. This article deals with the principles to be followed by the arbitrators while granting interest on damages.

Some Contracts provide for damage clauses quantifying the damages payable to the affected party by the breaching party and prescribe an interest rate that can be paid on the liquidated damages prescribed in the contract. In some types of contracts, there are negative covenants prohibiting any payment of interest along with damages. In some other contracts there is no provision for interest as well as no bar for paying interest on damages. The Supreme Court of India, after considering the above said three types of contracts settled the law with regard to the interest payable on the damages arising out of the above said contracts. The Constitution Bench of the Supreme Court of India, in irrigation department case¹, Dhenkanal Minor Irrigation Division², Bhawagati Oxygen Ltd³. held that in the absence of an express bar, the arbitrator has the jurisdiction and authority to award interest for all the three periods pre-reference, pendente lite and future. Hence, the arbitrator can grant interest at the rate specified in the contract or a reasonable rate of interest as long as there is no prohibition to grant interest. But at the same time, it should be kept in mind that if there is an express prohibition in the contract for the award of interest then award cannot contain the interest for pre-reference and pendente lite periods. But future interest cannot be prohibited by way of a provision in the contract and hence arbitrator has absolute power in granting future interest.

It is true that the position of law earlier was that in regard to award of damages, interest was not payable before quantification of damages by a court or an Arbitration tribunal. The above said position of law was supported by the justification that it would not be true to say that a person who commits a breach of contract incurs pecuniary liability, nor would it be true to say that the other party to the contract who complains of the breach has any amount due to him from the other party. Hence, the only right which he has is the right to go a court of law and recover damages as held by High Court of

¹ (1992) 1 SCC 508, Irrigation department, Govt of Orissa v. G.C. Roy

² (2001) 2 SCC 721, Dhenkanal Minor Irrigation Division v. N.C. Budharaj

³ (2005) 6 SCC 462, Bhagawati Oxygen Ltd. v. Hindustan Copper Ltd.

Bombay in Iron and Hardware⁴ case. But the position regarding award of interest after the Interest Act, 1978 came into force can be stated thus:

(a) where a provision has been in any contract, for interest on any debt or damages, interest shall be paid in accordance with such contract.

(b) Where payment of interest on any debt or damages is expressly barred by the contract, no interest shall be awarded.

(c) Where there is no express bar in the contract and where there is also no provision for payment of interest then the principles of section 3 of the Interest Act will apply in regard to the pre-suit or pre-reference period and consequently interest will be payable:

(i) where the proceeding relate to a debt (ascertained sum) payable by virtue of a written instrument at a certain time, then from the date when the debt is payable to the date of institution of the proceedings;

(ii) where the proceedings is for recovery of damages or for recovery of a debt which is not payable at a certain time, then from the date mentioned in a written notice given by the person making a claim to the person liable for the claim that interest will be claimed, to date of institution of proceedings.

(d) Payment of interest pendente lite (date of institution if proceedings to date of decree) and future interest (from the date of decree to date of payment) shall no be governed by the provisions of the Interest Act, 1978 but by the provisions of section 34 of the Code of Civil Procedure, 1908 or the provisions of the law governing arbitration as the case may be.

Hence the law relating to grant of interest on damages underwent a change after the enactment of the Interest Act, 1978. In view of the Interest Act, 1978 even in regard to the claims for damages, interest can be awarded for a period prior to the date of ascertainment of quantification and hence if (a) the contracts specifically provides for such payment from the date provided in the contract or (b) a written demand had been made for the payment of interest on the amount claimed as damages before initiation of action, from the date mentioned in the notice of demand (that is from the date of demand or any future date mentioned therein). In regard to claims for ascertained sums due, interest will be due from the date payment became due as held in State of Rajasthan case⁵. Hence, the arbitrators are required to keep in mind the above said change in law, while granting interest on damages to achieve a sustainable award.

⁴ AIR 1954 Bom 423, Iron and Hardware (india) Co. v. Firm Shamlal & Bros.

⁵ (2009) 12 SCC 1, State of Rajasthan and Another v. Ferro Concrete Construction Private Limited