Legality of Unilateral Arbitration Clauses in India: A critical analysis

Nishant Bajoria & Mr. Shreeyash Masurkar
Year III, ILS Law College, Pune Year III, ILS Law College, Pune

Introduction

Arbitration as a mode of alternative dispute resolution provides party autonomy and flexibility where parties can ensure that a dispute resolution clause is tailor-made according to their commercial needs. When the dispute resolution mechanism in a contract between parties includes an arbitration clause, it can be of two types, namely – bilateral option clauses and unilateral option clauses. The former confers a right upon both the parties to refer the dispute to arbitration while the latter gives such a right to only one of the parties to the contract. In this article, we are concerned only with unilateral option clauses.

In unilateral clauses, the position of the parties is not equal with respect to the influence one party has over the other during their negotiation. The party who is at a superior position is able to dominate the inferior party on various terms of the agreement and may often reserve a unilateral right to invoke arbitration. Such clauses can be referred to by a variety of names such as 'asymmetrical' and 'one-sided'. These clauses are usually challenged on the grounds of unequal positions accorded to contracting parties, imbalance of rights between the parties and being opposed to the public policy of the country. The aspects of mutuality, equality and independence of parties are of paramount importance in arbitration and the same is a ground for debate on the validity of unilateral option clauses. Coupled with a silence in legislation and judicial pronouncements, an analysis into the veracity of such clauses is prompted.

Validity of unilateral arbitration clauses in India

While neither the Arbitration Act nor the Supreme Court has taken a stand regarding the validity of such clauses, on several occasions contradicting jurisprudence has been churned by various High Courts.

Judgements Upholding Validity: -

1. *Castrol India Ltd vs. Apex Tooling Solutions Ltd, 2015*[1] ["**Castrol India**"]

[1] *Castrol India Ltd & Ors v Apex Tooling Solutions Ltd & Ors* (2015) 1 LW 961.

The issue before the Madras High Court was regarding the validity of Clause 23 of an agreement, which operated as the dispute resolution clause giving Castrol India the sole power to refer the matter to either the court or to the arbitrator.

The validity of the clause was defended on two grounds: *firstly*, that Section 7 of the Arbitration Act does not require the agreement to provide for a bilateral reference and *secondly*, the mutuality of rights amongst parties to initiate arbitration is not a mandated requirement under an arbitration agreement. The appellant referred to *Russell on Arbitration*[2], where it has been stated that there is no requirement under the English Law for an arbitration agreement to confer a mutual right upon the parties to initiate a reference, and an arbitration agreement providing an option to one party alone to refer disputes to arbitration was valid.[3]

Thus, the emphasis of the appellant was on international practices being followed wherein mutuality is not a pre-condition. The court did not dispute the validity of the clause and held that since the Indian arbitration law has been modelled to be in conformity with the UNCITRAL Model, judicial construction of the clauses under it should be in conformity with international practices.

2. *Jindal Export Ltd. Vs. Fuerst Day Lawson Ltd., 2009*[4] ["**Jindal Exports**"]

Before the Delhi High Court, the petitioner had challenged the lack of mutuality in the arbitration clause, thus questioning the unilateral power vested with the respondent under it. Under clause 17 of the contract, both parties had agreed that when a dispute arose between them, the respondent would have the unilateral power to initiate arbitration or to refer the matter to the Courts in England. Due to unfavourable weather conditions, the petitioner failed to deliver the contracted product to the respondent, following which, the respondent invoked the arbitration clause seeking damages. Further, the respondent nominated its arbitrator and persuaded the petitioner to do the same. However, when the petitioner failed to appoint one, the International General Produce Association Ltd. appointed an arbitrator on behalf of the petitioner. This appointment by the IGPA was objected to by the petitioner.

The respondent referred to the English case of *Pittalis & Ors. vs. Sherefetin,*[5] wherein the court had held that such a clause is a fully bilateral agreement which constitutes a contract and the fact that the option to invoke the arbitration clause is exercisable by only one party is irrelevant since the parties have agreed upon the same. Relying upon this case, it was argued that mutuality between

---

[2] David Sutton, Judith Gill, Mathew Gearing, *Russel on Arbitration* (23rd edn, Sweet & Maxwell 2014).
[3] *NB Three Shipping Ltd v Harebell Shipping Ltd* [2004] EWHC 2001 (Comm).
[4] *Jindal Exports Ltd v Fuerst Day Lawson* [2009] 165 DLT 354.
[5] *Pittalis and Ors v Sherefetin* [1986] 1 QB 868.

the parties to initiate the arbitration clause i.e., equal rights between the parties to refer the matter to arbitration is not required.

Further, it was discussed that an agreement or a clause in an agreement requiring or contemplating a further consent or consensus before a reference to arbitration, is not an arbitration agreement but an agreement to enter into an arbitration agreement in the future. The parties to the case had agreed on future arbitration where the 'in the-future disputes' would be referred to arbitration is a possibility only when both parties consent to it. This aspect distinguishes an agreement to enter into an arbitration agreement from an arbitration agreement.

The petitioner contended that there is no specific form of arbitration agreement and the words used should disclose a determination and obligation to go to arbitration and not merely contemplate the possibility of going for arbitration. The court held that even if English law was not applicable to this case, there was an open offer by the petitioner to submit the dispute to arbitration and the power of acceptance to invoke arbitration was with the respondent, and when the option was exercised by the respondent, the arbitration clause became mandatory and thus, the petitioner's claim is not valid.

Judgements opposing the validity:-

1. *Bhartia Cutler Hammer vs. Avn Tubes Ltd., 1991*[6] ["**Bhartia Cutler Hammer**"]

In this case before the Delhi High Court, the plaintiff filed a recovery suit against the defendant. However, it was contended by the defendant that the matter should be referred to arbitration according to the agreement which contained a unilateral clause whereby only the defendant could initiate arbitral proceedings. The plaintiff challenged the validity of the clause on the grounds that it gives power to only one of the parties to refer disputes to arbitration. The plaintiff further relied on the English case of *Baron v Sunderland Corporation*[7] where the Court of Appeals had held that mutuality is an essential ingredient for a valid arbitration agreement.

The defendant argued that as the plaintiff had given his consent to refer the matter to arbitration, no fresh consent would be necessary and the previous consent would bind him throughout and such prior consent makes the clause bilateral. Thus, there was no question of want of mutuality to render the arbitration clause invalid.

---

[6] *Bhartia Cutler Hammer v Avn Tubes Ltd* (1995) 33 DRJ 672.
[7] *Baron v Sunderland Corporation* [1996] 2 QB 56.

The Court, however, held that the clause was invalid as the right to invoke the arbitration was restricted only to the respondent, it was one-sided and the clause would not amount to a bilateral arbitration agreement and even the pre-consent could not validate such a clause.

2. *Emmsons International Ltd. vs. Metal Distributors, 2005* [8] ["**Emmsons International**"]

The dispute in the above case was with respect to the jurisdiction of the court. The dispute resolution clause between the parties empowered only the seller to refer the dispute to arbitration and the validity of the same was questioned. Although the Court disregarded its validity, the reasoning had a different basis. The plaintiff had argued that the clause was opposed to public policy and was also hit by Section 28 of the Indian Contract Act, 1872, ["**the Contract Act**"], which would effectively render such agreements void on the ground that it absolutely restricts a party to enforce their rights under the contract in ordinary tribunals.

The court held that as the clause imposes an absolute restriction on the party, it is void under Section 28 of the Contract Act, apart from being opposed to public policy. Interestingly, the court also noted that if the contract had partially, and not absolutely, restricted the plaintiff's right to remedy i.e., giving them an alternative choice before other tribunals, then such a clause would have been valid.

Critical analysis

It has been seen that unilateral clauses are usually challenged on the grounds of lack of equality or mutuality between parties, besides being unconscionable and laying an absolute restraint on a party's right to legal proceedings and being opposed to the public policy of India. It is imperative to analyse these grounds of challenge along with the decisions of the respective High Courts.

Firstly, the Arbitration Act nowhere provides for mutuality or equality between parties regarding the invocation of arbitration as an essential ingredient for a valid 'arbitration agreement' under Section 7 of the Arbitration Act, as rightly argued in Castrol India.

Moreover, in Jindal Exports, the aspect of future arbitration has been discussed. Such an agreement is valid as it provides the party the option to arbitrate, and whenever such an offer to initiate arbitration is accepted and executed, it becomes a valid agreement. Only because there is uncertainty as to arbitrate at the time of entering into an agreement, cannot be a ground for rejecting the validity of the same. The parties are giving their prior consent to submit future

[8] *Emmsons International Ltd v Metal Distributors* 2005 80 DRJ 256.

disputes to arbitration, thereby satisfying the condition of a valid clause under Section 7 of the Arbitration act. Thus, the same has been rightly upheld by the court in the above case.

Additionally, taking into consideration the Bhartia Cutler Hammer case, the aspect of prior consent also needs to be looked into. If the party challenging the arbitration clause has given their consent to the agreement, it should be assumed that it has gone through the provisions of the clause and the same should be binding on them. Consent assumes that there is consensus ad idem between the parties which is a necessary requisite for a valid contract. Moreover, the doctrine of promissory estoppel provides that when one party gives an assurance or promise and the other party acts on the same faith or promise, the party making the promise or assurance becomes bound by it and cannot retract from the same due to the application of the law of estoppel. When the party challenging the clause has given their assurance to be bound by the clause, the party is thereby bound by the doctrine which would defeat their challenge. Thus, the judgement in the case of Bhartia Cutler Hammer does not hold.

Secondly, concerning the aspect of unconscionability, lack of mutuality and equality, Section 16 of the Contract Act defines contracts induced by undue influence as being voidable at the option of the party whose consent has been obtained by those means. It covers contracts in which a party is in a position to dominate the will of another and uses the same to obtain an unfair advantage over the other which are known as unconscionable contracts. Unilateral option clauses are usually challenged on similar grounds. In the case of *Central Inland Water Transport Corp Ltd v. Brojo Nath Ganguly, 1986*[9] ["**Brojo Nath Ganguly**"], the Supreme Court had struck down an employment agreement which provided for termination of services of a permanent employee by serving a three month notice and held that such a provision was unreasonable, unfair, and opposed to Section 23 of the Contract Act. However, it held that only such unreasonable and unfair clauses would be declared void where inequality of bargaining power results from great disparity in the economic strength of the parties or where one party can obtain the means of livelihood by only relying upon the terms imposed by the stronger party. This principle was held to not apply in a commercial transaction and where both parties are businessmen, as considering the number of large corporations, such myriad situations might arise. Thus, as the concept of unconscionability does not apply in case of commercial transactions, unilateral arbitration clauses, almost all of which are found in a commercial setting, cannot be held as being unconscionable, and those being induced by undue influence, thereby establishing consent, mutuality & equality between the parties with respect to the clause.

---

[9] *Central Inland Water Transport Corp Ltd v Brojo Nath Ganguly* 1986 3 SCC 156.

Lastly, public policy also has been a ground for challenge for such clauses. Public policy has been defined as a ground for challenge of awards under section 34 of the Arbitration Act and further elaborated by the Supreme Court in various judgements, such as *Renusagar Power Co. Ltd v. General Electric Co*[10] as something being in contravention with fundamental policy of Indian law or that is in conflict with its most basic notions of morality or justice. Unilateral arbitration clauses restrain a party from invoking the dispute resolution clause, thus restraining a party's right to legal remedy and consequently contravene Section 28 of the Contract Act. However, exception 1 to Section 28 of the Contract Act which provides that the rule of agreement in restrain of legal proceedings are void shall not apply in cases where the parties agree to refer the disputes between them to arbitration has not been looked into by the Delhi High Court in the case of Emmsons International. Thus, unilateral option clauses are not void by virtue of Section 28 and public policy concerns. Additionally, the scope of public policy as a ground for challenge of arbitral awards has been well defined under the 2015 amendment of the Arbitration act & the Delhi High Courts' decision invalidating such clauses was pronounced prior to this amendment and thus a re-valuation of whether these clauses violate the recently defined scope of public policy also needs to be relooked.

Recently, the issue of legality of unilateral appointment of arbitrators has been considered by the Supreme Court. In *Perkins Eastman Architects DPC and another v. HSCC (India) Limited, 2019* [11], the respondent company's Managing Director's power of unilateral appointment of a sole arbitrator was challenged. The Court held that such a clause is invalid as there exists a possibility that the arbitrator may act to safeguard the interests of the party appointing him thereby negating the principle of party autonomy and neutrality in an arbitration. Thus, impartiality and independence of parties has been a ground of challenge.

However, regarding unilateral arbitration clauses, a party only has the right to decide to invoke the dispute resolution clause, i.e., giving the party procedural right, however, the substantive rights of the party remain the same & are not affected. Thus, the process of arbitration remains neutral. Further, here the principle laid down in *Brojo Nath Ganguly* needs to be considered, which establishes that there is an absence of undue influence in commercial transactions, thus proving consent & equality between the parties.

Thus, to settle the dispute, the question before the Supreme Court would be with regard to lack of equality, mutuality between the parties and public policy concerns. The court should consider

---

[10] *Renusagar Power Co Ltd v General Electric Co* 1994 Supp 1 SCC 644.
[11] *Perkins Eastman Architects DPC and another v HSCC (India) Ltd* 2019 SCC OnLine 1517 SC.

the principle laid down in *Brojo Nath Ganguly*, as in a commercial transaction where unequal positions between parties do exist and it benefits both the parties in some way or other. The authors have also explained how such clauses are not opposed to public policy. Thus, as there is prior consent between the parties, without undue influence and also as no statutory provision invalidates such clauses along with being in conformity with public policy, the authors find no reason why the validity of such clauses should not be upheld.