* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Judgment Reserved on: 18.11.2014
% Judgment delivered on: 13.02.2015

\+ **ARB. P. 534/2013**

PUNJAB NATIONAL BANK ....Petitioner

Versus

KOHINOOR FOODS LIMITED .....Respondent

ADVOCATES WHO APPEARED IN THIS CASE:

For the Petitioner : Mr Arvind Nigam, Sr. Advocate with Mr Dhruv Dewan, Mr Rohan Batra & Mr Kostubh Devnani, Advocates.

For the Respondent : Mr Sandeep Sethi, Sr. Advocate with Ms Shyel Trehan & Ms Tejaswi Shetty, Advocates.

CORAM :-
HON'BLE MR JUSTICE RAJIV SHAKDHER

RAJIV SHAKDHER, J

Arb. P. 534/2013 & IA No. 18102/2014 (u/s 151 CPC)

1. This is a petition filed under Section 11(6) of the Arbitration & Conciliation Act, 1996 (in short the Act), seeking a direction for appointment of an arbitrator, albeit on behalf of the respondent.

1.1 The petitioner, relies upon clause 13 (b)(ii) of ISDA (International Swaps and Derivatives Association) Master Agreement dated 03.07.2006 [hereafter referred to as the Master Agreement], as modified by the accompanying schedule of even date. It may be important to note at this juncture, though the Master Agreement is dated 03.07.2006, it was signed and sealed on behalf of the respondent on 22.04.2006, and similarly, on behalf of the petitioner, on 07.06.2006. There is no dispute with regard to this aspect of the matter.

1.2 What is in dispute, in so far as the respondent is concerned, is the extension of the arbitration clause to the transaction in issue, which is referred to as USD CHF Currency Swap transaction no. 1040 dated 18.07.2007 (hereinafter referred to as the original transaction). According to the respondent, the transaction, in issue is a stand-alone bilateral arrangement between the parties herein, to which clause 13(b)(ii) of the Master Agreement, would have no application. This is one of the preliminary objections raised by the respondent.

1.3 Apart from the above, the respondent has also raised other issues, which can broadly be categorized as follows:

(i) The disputes, which have arisen between the parties, (in respect of the transaction in issue), not being arbitrable by a private forum, such as an arbitral tribunal, a suit bearing no. CS(OS) 1950/2011, has been filed in this court, in which, an application has been filed by the petitioner under Section 8 of the Act; which is pending adjudication. In other words, there is a threshold bar on the court, in proceeding to decide the instant petition, in view of the pendency of an application under Section 8 of the Act.

(ii) In CS(OS) 1950/2011, the respondent has impleaded Reserve Bank of India (RBI) as a defendant, as the legality and the validity of the transaction is assailed. Since, RBI is not a party to the Master Agreement, which contains the arbitration clause, this court cannot appoint an arbitrator, as sought for in the petition.

(iii) The disputes raised, as between the parties herein, are not arbitrable in view of the stand taken by the respondent, (both in the suit instituted by it, as well as in the present petition), that the petitioner had employed fraud, misrepresented facts, and used undue influence in having the respondent, enter into the transaction in issue. In sum, it is contended that such disputes can only be agitated before a public fora, such as, courts duly constituted under law.

2. Therefore, apart from the preliminary issue raised as to the existence of the arbitration agreement between the parties herein, there are, broadly, three other objections to the petition, as delineated hereinabove.

3. Before I deal with these objections, in the fitness of things, it would be necessary to etch out the relevant facts, which have led to the institution of the present petition.

3.1 The parties herein, in 2006, appear to have agreed to enter into an agreement to provide for rights and obligations which would govern all inter se foreign exchange derivative transactions concluded between them. This agreement, which is referred to as the Master Agreement, provided the broad legal framework for transactions entered into between the parties herein.

3.2 Pursuant to the execution of the Master agreement and accompanying schedule, the respondent made an application dated 18.07.2007, calling upon the petitioner to enter into a derivative transaction. This transaction is referred to as USD/CHF Swap. As is obvious, USD refers to US Dollars, whereas CHF refers to Swiss Francs.

3.3 By virtue of the aforementioned application, the respondent gave the petitioner a mandate to enter into the said derivative transaction for a USD 10 million; the "tenor" for which was three years.

3.4 Along with the said application, the respondent furnished a copy of RBI's approval dated 23.09.2005, as a proof of its underlying exposure, in the form of Freely Convertible Currency Bond (in short FCCB) liability, amounting to USD 20 million.

3.5 Importantly, in the application, the respondent made the following assertion:

> "….We understand that in case the underlying exposure is prepaid then the derivative transaction undertaken against the same will be unwound at the then prevailing market rate. We also understand that we will be exposed to currency exchange rates fluctuations. We confirm that proper risk management policies are in place for undertaking derivative transaction. We have understood and accepted the risk associated with the deal as mentioned in the Term Sheet…."

3.6 The original transaction was accompanied by final terms and conditions, which included clauses pertaining to risk disclosure and client representations. The scope and ambit of these clauses will be dealt with by me as and when I advert to the submissions of counsels made in this behalf.

3.7 Continuing with my narrative, it appears that the original transaction was amended, at the request of the respondent, on at least four occasions, these being: 03.03.2008, 07.03.2008, 11.09.2009 and 18.11.2009. The term sheets generated in this behalf included certain prefatory notes, which again I will refer to in extenso, in the course of the discussion at the relevant juncture.

3.8 Pertinently, between July, 2006 and July, 2008, the respondent appears to have entered into swap and option deals with the petitioner, in addition to the transaction in issue. Notably, qua these transactions what is clearly evident, is that, the respondent has, in certain deals, received payments whereas in others it had to make payments.

3.9 The reason, I am referring to these transactions, is that, the petitioner has set out the details of certain derivative transactions, consummated by the respondent, in the aforementioned period only to demonstrate that it was fully equipped to enter into sophisticated derivative transactions, contrary to what was sought to be portrayed by the respondent before this court.

4. Importantly, these transactions, which are detailed out in annexure P-5, are not denied by the respondent.

4.1 Moving further with the narration, in respect of the transaction in issue, the respondent, suffered a loss, which is crystalized as on 08.08.2011, as CHF 4,975,000/-; equivalent to INR 29,43,58,559/-.

4.2 Within two days of the said communication, on 10.08.2011, the respondent instituted a suit; to which I have made a reference above. The said suit, which is numbered as: CS(OS) 1950/2011, seeks a declaration to the effect that the original transaction, as well as the amended transactions, are void, unenforceable and, therefore, not binding on the respondent. A supplementary prayer is also made for a declaration, that the said transactions are voidable, and having been avoided, are not binding and enforceable on the respondent. Consequential reliefs of recovery and mandatory injunction are also sought. Recovery is ought in the sum of Rs. 14,02,94,612/-. The mandatory injunction sought, seeks issuance of a direction to RBI to cancel the banking license of the petitioner herein. In addition, a prohibitory injunction is prayed for vis-à-vis the petitioner from selling and marketing derivatives, generally.

4.3 In the aforementioned suit, a Single Judge of this court, while issuing summons in the suit and notice in the accompanying interlocutory application, directed parties, in the suit, to maintain status quo with regard to the original as well as amended transactions. This order was passed on 10.08.2011, in IA No. 12636/2011. Pertinently, apart from the respondent, the other plaintiff in the suit is, one, Sh. Satnam Arora, the Jt. Managing Director of the respondent.

4.4 Evidently, the petitioner, much prior to the returnable date, moved an application under Section 8 of the Act, in the aforementioned suit. The said application is numbered as: IA No. 15903/2011. Notice, in this application was issued on 30.09.2011. This application, I am informed, is pending adjudication. The respondent herein, on its part, has filed a reply to the said application. The stand taken in the said reply is, broadly, similar to the one taken in the instant petition.

4.5 The petitioner, in the meanwhile, chose to trigger the arbitration mechanism, vide a communication dated 03.09.2013, sent via its lawyers to the respondent. By this communication, the petitioner, inter alia, called upon the respondent to agree to the appointment of a sole arbitrator from a panel supplied by it. The panel contained the names of two former Judges of the Supreme Court.

4.6 The respondent vide communication dated 23.09.2013, indicated that it rather not engage with the petitioner on the appointment of the arbitrator in view of the fact that, not only was the issue subjudice, but also that the parties had been directed to maintain status quo, with respect to the transactions in issue in the suit filed by it. The respondent, however, made it clear that the said communication was being issued without prejudice to its other legal rights, and that, nothing stated thereon ought to be construed as a waiver or relinquishment of any right or remedy that it may be possessed of.

4.7 The petitioner, in turn, rebutted the contentions of the respondent via a rejoinder dated 15.10.2013, issued by its advocates. The petitioner, in this communication, made it clear that since the respondent had failed to give its consent to appointment of a sole arbitrator, one of the persons named in its communication dated 03.09.2013 [i.e., Hon'ble Mr. Justice, S.B. Sinha, a former Judge of the Supreme Court], should now be treated as its nominee arbitrator. Accordingly, the petitioner called upon the respondent to appoint its nominee, within a period of thirty days of receipt of the said communication.

4.8 Since the respondent, it appears, wanted to have the last say in the matter, it got a sur-rejoinder issued by its lawyer dated 22.10.2013. By this communication, the respondent, reiterated its earlier stand, and furthermore, pointed out that the dispute obtaining between the parties was non-arbitrable. The petitioner was, accordingly, called upon to withdraw its notice.

4.9 On expiry of, what the petitioner construed as the notice period, the instant petition was moved. Notice in the instant petition was issued by me, on 06.12.2013. Parties, since then, have completed pleadings in the matter.

SUBMISSIONS OF COUNSELS

5. In the background of the above broad facts, the arguments on behalf of the petitioner have been advanced by Mr Arvind Nigam, Sr. Advocae assisted by Mr Dhruv Dewan and Mr Rohan Batra, while on behalf of respondent arguments have been advanced by Mr Sandep Sethi, Sr. Advocated assisted by Ms Shyel Trehan and Ms Tejaswi Shetty.

5.1 On behalf of the petitioner, the following broad submissions have been made by Messrs Nigam and Dewan.

(i) There is no bar on this court proceeding to decide the present petition, notwithstanding the pendency of an application under Section 8 of the Act, as both the scope and the relief sought for in the two actions is qualitatively, quite different. In support of this submission, reliance was placed on the judgement of the Supreme Court in the case of ***Vijay Kr. Sharma @ Manju vs Raghunandan Sharma @ Babu Ram & Ors. (2010) 2 SCC 486***.

(ii) There is in existence an arbitration agreement, which is reflected in clause 13(b)(ii) of the schedule to the Master Agreement. The transactions in issue, were governed by the broad legal framework provided in the Master Agreement. The transactions in issue, were not delinked from the Master Agreement and, therefore, the arbitration clause, referred to above, would govern the said transactions as well.

(iii) RBI, was not a proper and necessary party in so far as the present proceedings are concerned. The court was required to only examine as to whether there was an arbitration agreement in existence in so far as the parties before it were concerned, and if, it came to such a conclusion, it was duty bound to appoint an arbitrator, upon failure of the respondent to appoint its nominee, despite notice having been issued in that behalf by the petitioner.

(iv) There was no fraud or misrepresentation employed, as alleged or at all, by the petitioner. The transactions in issue were legal and not opposed to public policy. Derivative transactions had been accorded full legal sanctity by virtue of the provisions of Section 45(v) of the RBI Act, 1934, which was inserted in Chapter III-D vide RBI (Amendment) Act, 2006 [In short 2006 RBI Amendment Act]. Furthermore, the transactions in issue fully complied with the provisions of FEMA (Foreign Exchange Derivative Contract) Regulations, 2000 (in short FEMA Regulations), RBI's Master Circular on Risk Management and Inter-Bank Dealings dated 02.07.2007 (in short Risk and Management Circular) and RBI's Notification dated 03.05.2000 (in short the RBI Notification). In so far as the respondent placed reliance on RBI Comprehensive Guidelines on Derivatives dated 20.04.2007 (in short Guidelines on Derivatives), the same was misplaced, as it was only applicable to rupee denominated derivative transactions. In any event, the transactions in issue were substantially compliant with these guidelines as well.

(v) The stand of the respondent, that since fraud is alleged qua the transaction in issue, the disputes vis-à-vis the said transactions were not arbitrable, is misconceived. The said proposition applies in a situation where the person against whom allegations of fraud are made, seeks trial by a public fora as against a private forum, such as an arbitral tribunal. In other words, had the petitioner sought a trial by public fora, the court may have to restrain itself from subjecting parties to trial by an arbitral tribunal. For this proposition, reliance was placed on the following judgements:

Russell vs Russell 1879 R 294; Abdul Kadir Shamsuddin Bubere vs Madhav Prabhakar Oak & Anr. AIR 1962 SC 406; Sundaram Brake Linings Ltd. vs Kotak Mahindra Bank Ltd. (2010) 4 Comp. LJ 345 (Mad); and judgement of this court dated 10.03.2010, passed in CS(OS) No. 2241/2009, titled: ***M/s Maruti Clean Coal and Power Ltd. vs Kolahai Infotech Pvt. Ltd. & Ors***.

(vi) The reliance placed by the respondent on the judgement of the Supreme Court in ***N. Radhakrishnan vs Maestro Engineers (2010) 1 SCC 72***, is misplaced as it in fact furthers the case of the petitioner. Without prejudice to the above, it was contended, that the Supreme Court in the case of ***Swiss Timing Ltd. vs Organizing Committee Commonwealth Games, 2010 (2014) 6 SCC 677***, has observed that its earlier judgement in the ***N. Radhakrishnan*** is per incuriam, as it overlooked the Court's earlier judgement in the case of ***P. Anand Gajapathi Raju & Ors. vs P.V.G. Raju (Died) & Ors. (2000) 4 SCC 539.***

(vii) Apart from anything else, courts in the country have found derivative transactions to be valid in law and not opposed to public policy. For this proposition reliance was placed on the following judgements: ***Rajshree Sugars & Chemicals Ltd. vs Axis Bank Ltd AIR 2011 Mad 144,*** and judgement dated 14.10.2011, passed in IA No. 10686/2011 in CS(OS) No.1656/2011, titled: ***Ms Richa Industries Ltd. & Ors. vs ICICI Bank Ltd. and Anr***.

6. On the other hand, Mr Sethi made the following broad submissions:

(i) That there was no arbitration agreement in existence vis-à-vis the transactions in issue. The transactions were stand-alone dealings undertaken by the parties herein. These transactions were not governed by clause 13(b)(ii) of the schedule to the Master Agreement.

(ii) This court could not adjudicate upon the present petition pending the decision in the application filed under Section 8 by the petitioner. I must only note here that though this submission was adverted to and an objection to this effect has been taken in reply, it was ultimately not pressed with the same vehemence as the other objections.

(iii) The transactions in issue being fraught with fraud and, therefore, being opposed to public policy had been impugned by way of a suit by the respondent. The respondent, by virtue of this act, has, indicated its preference for an adjudication by a public fora, as against a private forum, such as, an arbitral tribunal. In these circumstances, this court ought not to grant relief as prayed for in the petition. As to how the transaction was vitiated by fraud, reference was made by the learned counsel to the assertions made in that behalf in the reply, in particular, to averments made under the heading "vitiated by fraud".

(iv) The transactions were violative of the existing legal provisions, as contained in FEMA Regulations, Risk and Management Circular and RBI Guidelines on Derivatives. In order to adjudicate upon these aspects, it was necessary to have RBI's say in the matter. As a matter of fact (as averred in the reply), the respondent became aware of the illegality of the transaction in issue, only upon gaining knowledge of the RBI Circular dated 26.04.2011, whereby penalty had been imposed on various banks for acting in contravention of instructions issued qua derivative transactions. It was contended that the Orissa High Court in a Public Interest Petition titled

Pravanjan Patra vs Republic of India 109 (2010) CLT 817 had directed investigation by CBI into "exotic derivative contracts".

(v) The transactions in issue having been entered into by employment of fraud and misrepresentation; and, being otherwise, opposed to public policy, parties herein could not be relegated to a private forum, such as, an arbitral tribunal, for adjudication. In support of this submission, reliance was placed on the following cases, apart from the ***N. Radhakrishnan's*** case cited by the petitioner, as well: ***Ivory Properties & Hotels Pvt. Ltd. vs Nusli Neville Wadia 2011 (2) Arb. L.R. 479 (Bom); H.G. Oomor Sait & Anr. Vs O. Aslam Sait (2001) 2 MLJ 672;*** and ***Nahar Industries Enterprises Ltd. vs Hong Kong and Shanghai Banking Corporation Ltd. (2009) 8 SCC 646***.

(vi) Where the legality of the main contract is in issue, the parties cannot be relegated to arbitration based on an arbitration mechanism incorporated in the main contract. In view of the fact that the transactions in issue were tainted by fraud, misrepresentation and undue influence, not only the main agreement, but also the arbitration clause, would collapse. This submission was sought to be buttressed by placing reliance on the following judgements: ***India Household Healthcare Ltd. vs L.G. Household and Healthcare Ltd. (2007) 5 SCC 510; WF Ducat & Co. Pvt. Ltd. vs Hiralal Palnnalal AIR 1976 Cal 126***; ***Atul Singh & Ors. vs Sunil Kumar Singh & Ors. (2008) 2 SCC 602; TML Financial Services Ltd. vs Vinod Kumar 2010 (1) KLT 209;*** and ***MSM Satellite (Singapore) Pte. Ltd. vs World Sports Group (Mauritius) Ltd. 2010 (112) BLR 4292***.

REASONS

7. I have heard the learned counsels for the parties and perused the record. In order to deal with the submissions of counsels, I propose to take up each objection raised, under the heads set out below.

A. **Is the prosecution of the present petition tenable, pending the adjudication of an application under Section 8 of the Act**?

A.1 In so far as this issue is concerned, the answer lies in Section 8 of the Act itself. Sub-section (1) of Section 8 of the Act empowers a judicial authority, before which, an action is brought which is also subject matter of an arbitration agreement, to refer the parties to arbitration if, an application in that behalf is moved before it, prior to the submission of a first statement on the substance of the dispute, by such an applicant. The only pre-requisite attached to it is that, the application should be accompanied by the original agreement or a duly certified copy thereof. This condition, is prescribed in sub-section (2) of Section 8. Pertinently, Sub-section (3) of Section 8 provides that, notwithstanding the fact that an application had been moved under sub-section (1), and the fact that, such an, application is pending adjudication with the concerned judicial authority, arbitration could be commenced, or continued and, accordingly, an arbitral award could be made.

A.1.1 Clearly, the legislature mandates that the pendency of an application under Section 8 of the Act, will not come in the way of commencement or continuation of arbitral proceedings, and the resultant pronouncement of an award. [see observations of the Supreme Court in ***Vijay Kumar Sharma's*** case in paragraphs 1 to 13 at pages 489 to 490]

A.2 Therefore while considering an application under Section 8 of the Act, all that the Chief Justice or his designate has to consider is, whether the arbitral proceedings have been filed in an appropriate court having jurisdiction; and whether there is an arbitration agreement obtaining between the parties. The Chief Justice or his designate may, optionally though, choose to rule upon, whether or not the claim is alive or barred by limitation and, furthermore, whether there is accord and satisfaction achieved in respect of the transactions in issue or, discharge of the contract by virtue of performance of obligations undertaken therein or, by mutual agreement. As to whether or not a claim is arbitrable, which could include an objection, such as, it being an excepted claim, or matters with respect to merits of the claim, are best left to the arbitral tribunal. [See observations in ***National Insurance Co. Ltd. vs Bhogra Polyfab (P) Ltd. (2009) 1 SCC 267*** in paragraph 22 at page 283]

A.3 Therefore, I have no difficulty in concluding that the petitioner is well within its rights to press for grant of reliefs, as prayed for in the instant petition.

B. **Is there an arbitration agreement obtaining between the parties**?

B.1 For this purpose, one would have to extract certain vital and relevant portions of the Master Agreement, and the schedule. The same are set out below:

> "MASTER AGREEMENT
>
> Dated as of 3/7/06
>
> Punjab National Bank (party A)
>
> And

M/s Satnam Overseas Ltd. (party B)

Have entered and/or anticipate entering into one or more transactions (each a 'Transaction") that are or will be govered by this Master Agreement, which includes the schedule (the "Schedule"), and the documents and other confirming evidence (each a "Confirmation") exchanged between the parties confirming those transactions…..

1. Interpretation

(a) xxxx

(b) xxxx

(c) Single Agreement. All Transactions are entered into in reliance on the fact that this Master Agreement and all Confirmations form a single agreement between the parties (collectively referred to as this "Agreement"), and the parties would not otherwise enter into any Transactions…"

(emphasis is mine)

B.1.1 The recital to the Master Agreement, as extracted above, is indicative of the fact that the parties herein executed the same having regard to the fact that it was anticipated that they would enter into one or more transactions which will be governed by the said agreement, including the schedule attached to it, and documents, as also other confirming evidence exchanged between them which would confirm the transactions.

B.1.2 Similarly, the clause 1(c) of the Master Agreement, quite clearly provides that all transactions are entered into based on the assurance that the said agreement and all confirmations form a single agreement between parties, and that, if that were not so, the parties would have not have entered into any such transaction.

B.2 There is no dispute raised before me that the Master Agreement and the schedule was not executed by the parties herein. Therefore, by a logical corollary, the provisions of part 4(h) of the schedule, [corresponding to clause 13(b)(ii) of the Master Agreement], which contains the arbitration agreement arrived at between the parties, would apply. The said clause, for the sake of convenience, is extracted hereinbelow:

> "…Governing Law: This agreement will be governed by and construed in accordance with the Indian Law.
>
> 13(b) (i) submits to the jurisdiction of Courts/ Tribunal of Delhi in India.
>
> 13(b)(ii) All dispute, differences and claims between the parties hereto arising under this Agreement or out of or in connection with the execution, interpretation, performance or non-performance of this agreement or this schedule shall be referred and settled by arbitration in accordance with the provisions of the (Indian) Arbitration and Conciliation Act 1996 or any re-enactment or modification thereof then in force. The parties may mutually agree upon and appoint a sole arbitrator. If the parties are unable to mutually agree upon and appoint a sole arbitrator then the arbitration shall be referred to a panel of three arbitrators appointed in the following manner; one arbitrator shall be appointed by Party A; one arbitration shall be appointed by party B; and the third arbitrator shall be appointed by the aforesaid two arbitrators. The arbitration shall be held in Delhi, India. Both parties shall endeavour to appoint arbitrators based in Delhi…."

B.2.1 A perusal of the aforesaid clause would show that if the said clause applies, then the courts in Delhi would have jurisdiction to entertain a petition seeking to trigger the arbitration mechanism provided therein. The clause not only provides that the arbitration will be held in Delhi, but also propels the parties to appoint arbitrators based in Delhi. Clause 13(b)(i) is indicative of the fact that the parties have agreed to submit to the jurisdiction of the courts in Delhi. There is no dispute that the respondent's registered office is located in Delhi, and therefore, for all these reasons, the petition as instituted, is maintainable.

B.3 In the context of the above, one may also have to deal with the submission that RBI is, a proper and necessary party as the legality of the transaction has been assailed by the respondent based on the provisions of the FEMA Regulations, Risk and Management circular, and the RBI Notification. The submission, according to me, is untenable, for the reason that all that the court has to examine in the ordinary course is : as to whether or not the parties before it, in a section 11 petition, are also, parties to the arbitration agreement. Once that is established, the court has to usually look no further. The scope of a Section 11 proceeding is limited to that extent.

B.3.1 In any event, dehors this aspect, I may note that RBI, in respect of the transaction in issue, to my mind, is neither a proper nor a necessary party. The legality or the validity of the transaction in issue, can be assailed by the respondent before the arbitral tribunal by referring to the aforementioned regulations, circulars, and guidelines. A party is necessary to a proceedings if no effective order or judgement, or even an award, can be passed by a judicial authority in its absence, and similarly, an entity may be impleaded as a "proper party", if in its absence adjudication of the dispute is not possible. This argument, if at all, can only be entertained in conjunction with the submission advanced on behalf of the respondent, that the transaction is fraught with fraud, misrepresentation and undue influence.

B.3.2 Sans the said submission, it is difficult for me to come to a conclusion that RBI is a proper and necessary party, and therefore, the said petition will not lie. Any illegality, that the respondent may wish to bring to fore, can be examined by the arbitral tribunal in light of the relevant regulations, circulars and guidelines, on which it seeks to place reliance. Since, it is a matter which ultimately the arbitral tribunal will rule upon, I do not wish to enter the arena, as to whether or not the transactions in issue are legal, having regard to the applicable law.

C. **Do allegations of fraud, misrepresentation and undue influence, by the respondent, qua the transactions in issue, render the instant petition 'not maintainable'**?

C.1 Before I proceed further, I would like to set out the principles articulated by the various judgements in that behalf. First and foremost, one would have to draw a distinction between forgery and fabrication and allegation of fraud, misrepresentation and undue influence. If it were a case where the respondent had alleged that the documents in issue which contained the arbitration agreement, i.e., Master Agreement and the schedule to the said Master Agreement, were forged and fabricated, the court, while adjudicating upon a petition under Section 11 of the Act, may have to decide and rule upon it. [See ***National Insurance Company*** paragraph 23 at page 283].

C.2 The allegation, however, herein is that the respondent herein, in a sense was duped or induced to, enter into, a derivative transaction, which, instead of reducing its risk and liability, had exposed it to a monetary liability greater than that envisaged by it.

C.3 Transactions which are impugned on the ground of fraud, misrepresentation or undue influence are voidable at the instance of a party making such an allegation. (See Section 17, 18 and 19 of the Contract Act). The respondent, recognizing this principle in its suit, has made a prayer to that effect. Therefore, what would have to be examined by me, prima facie, is whether a case of fraud, misrepresentation and undue influence is made out, since parties have invited a finding on the issue, though I have grave doubts as to whether this is the scope of a petition preferred under Section 11 of the Act. It is because a distinction has to be made between a fraud employed in inducing another party to enter into a contract, that is, qua the underlying transaction or its performance, and a fraud, which pertains to the execution of the contract itself; say for example, where signatures are not of the person concerned. Fraud of the former kind will have to be left for determination, ordinarily, by an arbitral tribunal.

C.3.1 The determination of this issue though, is being made dehors the contentions advanced on behalf of the respondent before me that once an allegation of fraud, misrepresentation and undue influence is made, then necessarily, parties cannot be relegated to a private forum, such as an arbitral tribunal, irrespective of the party making the allegation. In other words, according to the respondent, it would make little difference, whether the objection is taken by the accuser or the accused.

C.4 Therefore, one would have to briefly advert to what according to the respondent, is the fraud and/or misrepresentation employed by the petitioner. According to the respondent, it was incumbent upon the petitioner to hedge the respondent's liability and exposure on account of depreciation of the US Dollar. In this behalf, it was contended that the transaction which notionally swapped, i.e., USD 10 million into CHF (Swill Francs), at the rate of 1.2012 for a term of three years, exposed the respondent to the risk of Dollar depreciating against Swiss Francs (CHF) below 1.2012 rate in the defined period. The transaction gave the option to the respondent to sell the Dollars at the rate of 1.2012, if it fell below this rate, with the caveat that this, so called protection, got 'knocked out' if, the Dollar depreciated below 1.0200.

C.4.1 According to the respondent, what compounded the problem, was that, the respondent was obliged to purchase the Dollar if, it appreciated above 1.2012 rate. Furthermore, the respondent was required to pay the petitioner penalty equivalent to CHF 25000/- per day in case the CHF/Dollar traded above or below the lower barrier 1.0200 or the upper barrier 1.3500. As per the respondent, the transaction was configured to limit the protection till such time the depreciation of the dollar reached the level of 1.0200. Beyond that, there was no protection and, similarly, when the Dollar appreciated above the 1.2012 rate, it was required to purchase Dollars. The respondent claims that in this process, it has already paid, approximately, Rs.40 crores to the petitioner, which excludes the outstanding demand of approximately Rs. 29 crores.

C.4.2 In this context, it is also stated by the respondent, that the petitioner had paid little attention to the FEMA Regulations, the Risk and Management Circular, the RBI Notification and the RBI Guidelines on Derivatives. It is the submission of the respondent that the petitioner's conduct was questionable on the following counts : it was guilty of mis-selling the derivative transactions; it had no regard to the fact that the risks involved were not commensurate with the respondent's business, financial operations, skill and sophistication, internal policy and risk appetite; the petitioner failed to carry out a proper, due diligence, with regard to user appropriateness, or suitability of the product qua the respondent; and lastly, the petitioner failed to take into account the relevant provisions of the Risk and Management Circular, which required it to ensure that "options contracts involving cost reduction structures", were such structures which did "not result in increase in risk in any manner" and "do not result in net receipt of premium by the customer".

C.5 The sum of these allegations is that the respondent, which is essentially in the business of exporting rice, does not have the wherewithal and the necessary financial sophistication available with it for understanding the nuances of the transaction in issue. For this purpose the relevant extracts of the FEMA Regulations, the Risk and Management Circulars, the RBI Notification and the RBI Guidelines on Derivatives were relied upon.

C.5.1 In my opinion, this stand of the respondent seems, prima facie, suspect, in view of the fact, as indicated right in the beginning, that the petitioner has entered into several swap and option deals, apart from the transaction in issue, between July, 2006 and July, 2008. In some of these transactions the respondent has received moneys, whereas in others it had to make pay outs.

C.5.2 This apart, the respondent in its application made on 18.07.2007, categorically stated that it understood that there would be an exposure to currency exchange rate fluctuations. The respondent went on to say that proper risk management policies were in place for undertaking derivative transactions, and having understood the same, it had accepted the risk associated with it as mentioned in the "Term Sheet". The Term Sheet dated

18.07.2007 includes, amongst others, the following assertions qua risk disclosure and client representation (i.e., in the present case the respondent herein):

> "…. Risk Disclosure:
>
> 1. Client is protected from USD/CHF exchange rate fluctuations up to USD/CHF 1.0200 for principal exchange part…
>
> 2. xxxx
>
> Further the client represents that :
>
> 1. It is acting for its own account, and it has made its own independent decisions to enter into this Transaction and as to whether this Transaction is appropriate or proper for it is based upon its own judgement and upon advice from such advisors as it has deemed necessary.
> 2. It is not relying on any communication (written or oral) of the other party as investment advice or as a recommendation to enter into this Transaction and has not placed any reliance on the other party or any officer or third party acting on behalf of the other party; it being understood this information and explanations related to the terms and conditions of this Transaction shall not be considered investment advice or a recommendation to enter into this Transaction.
> 3. It has not received from the other party any assurance or guarantee as to the expected results of this Transaction.
> 4. It is capable of evaluating and understanding (on its own behalf or through independent professional advice), and understandings and accepts; the terms, conditions and risks of this Transaction. It is also capable of assuming, and assumes, the financial and other risks of this Transaction….."
>
> (emphasis is mine)

C.5.2.1 The respondent accepted, inter alia, the aforementioned terms and, thus, consciously, chose to execute the transactions in issue. If, there was any doubt, it is set to rest, when one has regard to the letter dated 18.11.2009, issued by Sh. Satnam Arora, the Jt. Managing Director of the respondent. A perusal of the said document would show that the respondent had the necessary skills available to understand the impact of the transaction it was entering into. For the sake of convenience the said letter is extracted hereinbelow:

> "Dear Sir,
>
> This is with reference to our USD CHF Swap Derivative Deal No. 1040 dated 18th July 2007 done with your bank.
>
> As it is obvious, the CHF is trading at its all time low and we are below the lower barrier of our range on the trade and accordingly accruing a considerable amount on a per day penalty basis and this would be expected to remain for some time now, as per forecasts available.
>
> However, the USD is expected to recover in the near future and as per common consensus we should see the CHF weakening starting beyond the second half of next year.
>
> In view of the above, we request you to amend the observation dates as under:
>
> - Observation of daily penalty below 1.0200 & above 1,3500 (Ongoing, till 18th January 2010) to be shifted to start from 9 August 2010 till 22 October 2010 which will be settled on 26th October 2010
>
> - Observation of daily penalty below 1.0500 & above 1,3500 (Existing start from 19th January 2010) to be shifted to start from 18 January 2011 till 04 August 2011 which will be settled on 8th August 2011.
>
> Exact dates should be informed to us as per your calculations. The option premium for the above shifting may be charged as applicable.

> On the subject of existing negative accruals of CHF 1,075,000 (for 43 days) as per the terms of the trade, it would be cleared by us maturity i.e. 08th July 2010….."

C.6 Therefore, to my mind, at least at this stage the respondent has not been able to make out any case of fraud, misrepresentation or undue influence having been employed in the execution of the transactions.

C.7 According to me this discussion was necessary as one was required to examine, at least prima facie, the contours of fraud. In cases such as the present one, if such an assertion is made a court is duty bound to examine, albeit tentatively, whether the plea of fraud is borne out prior to taking a decision as to whether or not parties ought to be relegated to a public fora, such as a court. If this exercise is not embarked upon, then the remedy by way of arbitration as agreed to between parties, could end up being avoided even when on the face of it, the allegation of fraud lacks substance.

D. **Can the party which makes an allegation of fraud, insist that the dispute be tried by a public fora such as the court, as against the agreed private forum, i.e., the arbitral tribunal**?

D.1 To my mind, ordinarily the leeway as to the forum, where adjudication should take place, is available to the party which is charged with fraud, as against one which makes the allegation. This proposition, however, is hemmed in by a caveat, which is that, ultimately the discretion in that behalf is vested in the court. If, the one who levels the charge makes out a tenable case, that is, a prima facie case, in the very least, the court, could in the given facts of the case refuse to send the parties to arbitration. The reason, to my mind, is simple: parties could not have agreed to have the charge of "cheating" or "serious fraud" involving complicated questions of law referred to an arbitral tribunal. The rationale though, for grant of a leeway by courts, to a party charged with fraud, is that, he could desire a public vindication of allegation made against him and, therefore, may convey to the court that he does not want such an allegation to be tried by a private forum. Therefore, ordinarily, the court would sustain the plea of a person charged with fraud that his case should be tried by a public fora such as a court.

D.1.1 The same, however, is not true of a person levelling a charge, save and except where the court comes to a conclusion that the matter requires adjudication by a court of law as it involves serious allegations of fraud. The person making the allegation of fraud qua another may want a trial qua an allegation of fraud before a public forum, to which the accused could respond, and quite reasonably, if I may say so, that he desires to have the matter tried by a private forum, such as an arbitral tribunal, without a public glare as it is easy to fling trumped-up charges of fraud, which could irreversibly damage his character by the time trial by a public fora gets concluded.

D.1.2 This was precisely the view which the Chancery Division took in ***Russell vs Russell***. The relevant observations of the court are extract hereinbelow:

> "…First of all, is it true that the parties to a contract can hardly be supposed to have endeavoured to refer to an arbitrator an attempt by one of them to cheat the other? I can find no reason for assuming it. A fraudulent man would not desire publicity, but would wish the question to be inquired into before a private tribunal. Nor does it follow that the man who has been defrauded wants publicity. It is an injury to the credit of the firm. It is an injury to the reputation of a man who has been his partner, who may be connected with him not only by the ties of

partnership, but, as in the case before me, by nearer and dearer ties. Why should it be necessarily beyond the purview of this contract to refer to an arbitrator questions of account, even when those questions do involve misconduct amounting even to dishonesty on the part of some partner? I do not see it. I do not say that in many cases which I will come to in the second branch of the case before the court, the Court may not, in the exercise of its discretion, refuse to interfere; but it does not appear to me to follow of necessity that this clause was not intended to apply to all questions, even including questions either imputing moral dishonesty or moral misconduct to one or other of the parties.

I now come to the first ground where personal fraud is in issue. Though I quite agree it is within the discretion of the Court to say, where one of the two partners desires it, that a dispute shall not be referred to arbitration, yet I must consider for a moment which of the two partners does desire to exclude arbitration. Does the party charging the fraud desire it, or the party charged with the fraud desire it? Where the party changed with the fraud desires it, I can perfectly understand the Court saying, "I will not refer your character against your will to a private arbitrator." It seems to me in that case it is almost a matter of course to refuse the reference, but I by no means think the same consideration follows when the publicity is desired by the person charging the fraud. His character is not at stake, and the other side may say, "the very object that I have in desiring the arbitration is that the matter shall not become public. It is very easy for you to trump up a charge of fraud against me, and damage my character, by an investigation in public." There is a very old and familiar proverb about throwing plenty of mud, which applies very much to these charges made by members of the same family, or members of the same partnership, against one another in public. It must be an injury, as a rule, to against one another in public. It must be an injury, as a rule, to the person charged with fraud to have it published, and I must say that I am by no means satisfied that the mere desire of the person charging the fraud is sufficient reason for the Court refusing to send the case to arbitration.

It may be that that must deped upon the circumstances of the case, not forgetting both the evidence before the Court when the motion is made, and the nature of the charge that is actually made. But I for one do not wish to countenance the doctrine that the mere fact of a partner, who has a contract in a deed to refer partnership disputes to arbitration, making a charge of fraud against a co-partner, is sufficient to prevent the co-partner insisting upon a reference to arbitration. As I conceive it, that rule ought only to be applied, as a matter of course, without investigating the circumstances, in cases where the person charged with the fraud desires the enquiry to be public….

..... The next question, I have to consider is, what foundation there is for the charges, because, if the mere making of a charge of fraud would entitle the person making it to call upon the court, in the exercise of its discretion, to refuse to refer to arbitration, there would be a very easy way of getting rid of all these clauses of arbitration. I am satisfied that the mere making of a charge will not do that, even in a case where the Court ought to exercise its discretion by refusing to refer the case to arbitration. There must be sufficient prima facie evidence of fraud, not conclusive or final evidence, because it is not the trial of the action, but sufficient prima facie evidence......"

D.1.3 The Supreme Court in the case of ***Abdul Kadir Shamsuddin Bubere vs Madhav Prabhakar Oak & Anr.,*** adopted the ***Russell vs. Russell*** principle. The relevant observations made in the said judgment of the Supreme Court, which support this principle, are extracted hereinbelow:

"There is no doubt that where serious allegations of fraud are made against a party and the party who is charged with fraud desires that the matter should be tried in open court, that would be a sufficient cause for the court not to order an arbitration agreement to be filed and not to make the reference. But it is not every allegation imputing some kind of dishonesty, particularly in matters of accounts, which would be enough to dispose a court to take the matter out of the forum which the parties themselves have chosen. This to our mind is clear even from the decision in Russel's case [1880] 14 Ch. D. 471..

> We are clearly of the opinion that merely because some allegations have been made that accounts are not correct or that certain items are exaggerated and so on that is not enough to induce the court to refuse to make a reference to arbitration. It is only in cases of allegations of fraud of a serious nature that the court will refuse as decided in Russel's case [1880] 14 Ch. D. 471 to order an arbitration agreement to be filed and will not make a reference..
>
> It is only when serious allegations of fraud are made which it is desirable should be tried in open court that a court would be justified in refusing to order the arbitration agreement to be filed and in refusing to make a reference..."

D.1.4 Therefore, I do not wholly agree with Mr. Nigam's view that the court is left with no discretion to relegate the parties to a public fora as against a private forum, such as, an arbitral tribunal when, a plea in that respect is made by the person making an allegation of fraud, i.e., the accuser. It is though another matter that in ***Russel Vs. Russel,*** the defendant against whom the allegation of fraud had been made was seeking to be referred to an arbitral tribunal in accordance with the agreement obtaining with the plaintiff. However, in the case of ***Abdul Kadir Shamsuddin Bubere Vs. Madhav Prabhakar Oak***, the allegations of fraud though were made against the appellant before the Supreme Court by the respondents, who had filed an application under Section 20 of the Arbitration Act, 1940. The Supreme Court after noticing the decision in the case of ***Russel Vs. Russel***, ruled that on facts, the allegations made did not amount to serious allegations of fraud necessitating a trial in open court. The net result is that, even in a case where a person charged with fraud, seeks trial by public forum, the court could refuse such a request.

D.1.5 The Supreme Court in ***N. Radhakrishnan Vs. Maestro Engineers and Ors.***, noticed the ratio of the judgment in ***Russel Vs. Russel*** and ***Abdul Kadir Shamsuddin Bubere Vs. Madhav Prabhakar Oak***. Upon noticing the ratio, it came to the conclusion that the application filed under Section 8 of the Act by the appellant before the Supreme Court in a suit filed by the respondents was, inter alia, dismissed on the ground that he had made allegations relating to misappropriation of funds and malpractices on the part of the respondents. The Supreme Court accepted the plea of the person charged with fraud that the matter required adjudication by a public fora. As a matter of fact, the Supreme Court in this case recognized the power of a court not to refer parties to arbitration even where an arbitration agreement is obtaining between the parties where serious or complicated questions of law and facts require adjudication. In that sense, the Supreme Court extended the discretionary power available under the Arbitration Act, 1940 Act to the Act under consideration i.e., the Arbitration and Conciliation Act, 1996. This is evident on a bare perusal of paragraph 25 of the judgment where the court has accepted the principle laid down by the Madras High Court in the case of ***H.G. Oomor Sait Vs. O. Aslam Sait, [(2001) 3 CTC 269 (Mad)]***. Notably though, the language of sub-Section (1) of Section 8 of the Act is suggestive of the legislative intent that once conditions prescribed in the Section are fulfilled, the court shall refer the parties to arbitration.

D.1.6 I may only indicate that in coming to this conclusion I have not relied upon a judgement of the Single Judge of Supreme Court in the case of ***Swiss Timing***, wherein it has been observed that the judgement rendered by a larger Bench of the Supreme Court in ***N. Radhakrishnan***, is *per incuriam*.

The reason for this is that the said judgement, does not adversely impact the case of the petitioner.

8. Since the judgment in H.G. Oomor Sait has already been considered in N. Radhakrishnan case, I need not dilate on the same. I may, however, refer to two other judgments cited by the respondents. First one, is the judgment of the Supreme Court in the case of ***Nahar Industrial Enterprises Ltd. Vs. Hong Kong and Shanghai Banking Corporation, (2009) 8 SCC 646***. This judgment dealt with the issue concerning the power of the High Court to transfer a civil suit filed after the enactment of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 (in short RDDB Act) to the Debt Recovery Tribunal (DRT). In my view, this judgment has no applicability to the issue at hand. The only reason perhaps this judgment has been cited is because the transaction in issue involved facets of International Swaps and Derivates Agreement.

8.1 That brings me to the last judgment, which is the judgment of a single judge of the Bombay High Court in the case of ***Ivory Properties and Hotels Pvt. Ltd. Vs. Nusli Neville Wadia, 2011 (2) ARBLR 479 (Bom)***. This judgment is in line with the view that I have taken hereinabove in as much as it does not deride from the principle articulated above by me. In this case, the court was dealing with an application under Section 11(6) of the Act. The applicant before the court sought appointment of an arbitrator qua disputes which arose with the opposite party concerning development rights in an immovable property. The respondent no.2 i.e., the opposite party before the court had filed both a suit as well as a criminal case against the applicant. In the suit, the applicant had interceded by an application under Section 8 of the Act, which at the relevant time, was pending adjudication.

The court came to the conclusion since the allegations of fraud were of a serious nature, they ought to be determined by a civil court. As is evident from the brief facts, adverted to above, that in this case even though the person who had been charged with fraud sought to trigger the arbitration mechanism, the court did not oblige. The rationale behind the same is found in the following observations made in the judgment :-

> "..Now, it is necessary for the Court to emphasize that it is not every stray allegation of fraud which would lead to the consequence of a refusal on the part of the court to refer parties to arbitration. The law certainly is not that on an isolated or stray reference to fraud without material particulars that the jurisdiction to refer parties to arbitration would stand ousted.."

8.2 I must also, however, note that in the aforementioned case, there was an attendant circumstance which, perhaps propelled the court not to entertain the application under Section 11(6) of the Act, which was that in the suit, the respondents had sought an injunction not only against the applicant who was party to the arbitration agreement but qua other entities as well, which were not parties to the suit.

8.3 In my view, the ratio of the judgment is that the decision of the court whether or not parties should be relegated to a public forum is not wholly dependent on who takes the plea but is governed by the assessment of the court as to whether a serious case of fraud is made out which requires a public trial.

8.4 In the facts of this case, I have come to the conclusion that respondent has not been able to make out a case of serious fraud which requires a trial by a public forum.

9. In view of the foregoing discussion, the other contention, that the arbitration agreement will collapse on account of the alleged fraud, is also not sustainable. In any event, an arbitration agreement is severable from the main contract. (See Section 16 of the Act).

10. In these circumstances, the petition is allowed. Since the respondents have not appointed an arbitrator in the matter, the court is inclined to appoint one. Accordingly, Hon'ble Mr. Justice R.V. Raveendran, a former Judge of the Supreme Court (Ph. No. 080-26601279) is appointed as an arbitrator. The arbitrator appointed by this court and the one appointed by the petitioner shall convene and appoint a third arbitrator in terms of the arbitration agreement obtaining between the parties. Parties will, however, bear their own costs.

11. Needless to say, any observation made hereinabove, will not impact the merits of the case.

RAJIV SHAKDHER, J.

FEBRUARY 13, 2015
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