PRE-REFERRAL JURISDICTION: B&T AG v. MINISTRY OF DEFENCE WIDENS THE EYE OF THE NEEDLE

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I. INTRODUCTION

The Supreme Court, in *NTPC Ltd. v. SPML Infra Ltd.*[1] ["***NTPC Ltd.***"], quite pithily described the pre-referral jurisdiction of the Courts under Section 11(6) of the Arbitration and Conciliation Act, 1996 ["**Arbitration Act**"], as one of "*limited scrutiny, through the eye of the needle*"[2]. This "*extremely limited*"[3] jurisdiction extends to examining whether an arbitration agreement exists – nothing more, nothing less.[4]

As a consequence of this limited and restricted scope of review, objections pertaining to limitation or claims being time-barred are generally not entertained by the Court under Section 11 of the Arbitration Act and have to be left for the arbitrator to decide.[5] However, the Supreme Court has made an exception for a certain category of claims or disputes that are manifestly and *ex facie* time-barred and which may be interfered with by the court even at the referral stage (i.e. under Section 8 or 11 of the Arbitration Act), in attempts to "*cut off the deadwood*".[6] Mindful of the potential for opening the floodgates of unnecessary interference and long-winded scrutiny at the pre-referral stage itself (which it is widely accepted ought to be discouraged, as with other unnecessary court interference as per the mandate of Section 5 of the Arbitration Act) the Supreme Court has clarified that such scrutiny ought to be undertaken "*rarely as a demurrer*" and only in cases of manifest and *ex-facie* certainty of the claims being dead.[7]

However, in the author's view, the Supreme Court's judgment in *B&T AG v. Ministry of Defence*[8] ["***B&T AG***"] sets a troubling precedent. It may provide unwarranted impetus for unjustified and abusive objections on the ground of limitation to be taken up and entertained at the referral stage under Section 11 (or for that matter under Section 8) since the Supreme

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[1] (2023) SCC OnLine SC 389.
[2] *Id*, ¶ 28.
[3] Vidya Drolia v. Durga Trading Corporation, (2021) 2 SCC 1, ¶ 154.2 ["***Vidya Drolia***"].
[4] Duro Felguera, SA v. Gangavaram Port Ltd., (2017) 9 SCC 729, ¶ 59 ["***Duro Felguera* and *Mayavati Trading***"]; *See also* Mayavati Trading Pvt. Ltd. v. Pradyut Deb Burman, (2019) 8 SCC 714.
[5] Uttarakhand Purv Sainik Kalyan Nigam Ltd. v. Northern Coal Field Ltd., (2020) 2 SCC 455, ¶ 7.13.
[6] *Id* at 3, ¶¶ 148, 154.4.
[7] *Id* at 3, ¶¶ 148, 154.4.
[8] (2023) SCC OnLine SC 657.

Court here enters into a wider and more detailed examination than would otherwise be permitted as part of the very narrow and *ex facie* scrutiny available under Section 11 of the Arbitration Act.

II. BRIEF SURVEY OF THE LAW LEADING UPTO THE EYE OF THE NEEDLE

Prior to the seven-judge bench judgment of the Supreme Court in *SBP & Co. v. Patel Engineering. Ltd.*[9] ["***Patel Engineering***"], much controversy surrounded the nature of power exercised while appointing an arbitrator under Section 11, whether administrative or judicial. The Supreme Court in Patel Engineering held that the court under Section 11 exercised a judicial power and was required to decide all threshold issues with respect to jurisdiction, such as the existence of the arbitration agreement, its validity, whether the claim was a dead one or whether it was time-barred or discharged by accord and satisfaction.

Based on the Law Commission's 246th Report[10], Section 11 was substantially amended by the 2016 Amendment Act, which most importantly inserted sub-Section (6-A) to Section 11 which provides that:

> "(6-A) The Supreme Court or, as the case may be, the High Court, while considering any application under sub-Section (4) or sub-Section (5) or sub-Section (6), shall, **notwithstanding any judgment, decree or order of any court, confine to the examination of the existence of an arbitration agreement.**" [emphasis supplied]

By virtue of the aforesaid sub-Section (6-A), previous judgments rendered in Patel Engineering and the line of judgments following it were legislatively overruled, and the scope of examination was confined only to the existence of the arbitration agreement.[11] All other preliminary or threshold issues are left for the arbitral tribunal to decide.[12]

Thereafter, the three-judge bench in *Vidya Drolia* carved out a sliver or pinhole through which the court could excise manifestly and *ex facie* time-barred and dead cases where there is no subsisting dispute. The Supreme Court held that while Limitation law is procedural and normally disputes, being factual, it would be for the arbitrator to decide maintainability on the basis of limitation, but the court at the referral stage may interfere when it is manifest that the

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[9] (2005) 8 SCC 618.
[10] LAW COMMISSION OF INDIA, REPORT NO. 246: AMENDMENTS TO THE ARBITRATION AND CONCILIATION ACT, 1996 (August 2014).
[11] *Id* at 4.
[12] BSNL v. Nortel Networks India Pvt. Ltd., (2021) 5 SCC 738, ¶ 34 ["***Nortel Networks***"].

claims are *ex facie* time-barred and dead, or there is no subsisting dispute.[13] However, the Supreme Court clarified that such interference should be rare and as a demurrer, the intention behind the restricted and limited review is to check and protect parties from being forced to arbitrate when the matter is demonstrably 'non-arbitrable' and to cut off the deadwood.[14] It was further held that the pre-referral stage was not the stage for the court to enter into a mini-trial or elaborate review.[15]

In view of the aforesaid, it is evident that the idea behind exercising such a review is to lop off the evidently deadwood claims. Consequently, the contours of such review have been intentionally kept strictly narrow:

i. The Court can interfere at the referral stage only when the claims are manifestly and *ex facie* time-barred;
ii. Such interference should be rare and based on demurrer;
iii. The review ought not to be elaborate or a mini-trial.

Vidya Drolia affirms the position of law expounded in *Duro Felguera* and *Mayavati Trading*, It has not resurrected the pre-amendment position on the scope of power as held in *Patel Engineering*.[16]

Following the precedent in *Vidya Drolia*, the Supreme Court rightly rejected the evidently dead claims in *Nortel Networks* and *Secunderabad Cantonment Board v. B Ramachandraiah*[17] ["***Secunderabad Cantonment Board***"]. Even in *NTPC Ltd.,* the Supreme Court exercises what it memorably calls the "*eye of the needle*" jurisdiction. Still, since that was a case of discharge by accord and satisfaction, a detailed discussion of that case is not relevant for our purposes.

III. THE TROUBLING WIDENING OF THE EYE OF THE NEEDLE

A. Nortel Networks

In *Nortel Networks*, the Supreme Court was seized with disputes under the works contract awarded by BSNL to Nortel Networks, where on completion of the works under the Purchase Order, BSNL deducted/withheld amounts towards liquidated damages and other levies. Nortel addressed a communication dated 13th May 2014 raising a claim for the said amount, which was rejected by BSNL by way of its letter dated 4th August 2014. After over 5.5 years,

[13] *Id* at 3, ¶ 148.
[14] *Id* at 3, ¶ 154.4.
[15] *Id.*
[16] *Id*, ¶ 46.
[17] (2021) 5 SCC 705.

Nortel invoked the arbitration clause by way of a letter dated 29th April 2020.

In the judgment, the Supreme Court finds that the cause of action arose on 4th August 2014 when the claims made by Nortel were rejected by BSNL, and Nortel has not stated any event that would extend the period of limitation thereafter. Hence, since the case fell within the category of deadwood cases, the Supreme Court rightly dismissed the Section 11 application.

B. Secunderabad Cantonment Board

Similarly, in *Secunderabad Cantonment Board*, there was a clear and grossly time-barred claim where again in a works contract, the final contract certificates were issued by the appellant on 18th February 2002 and 26th March 2003, the final payment was received by the respondent. However, the respondent made further demands by way of letters last of which was dated 12th October 2004, all of which went unresponded. Eventually, the respondent resumed correspondence after a hiatus of about 2 years, which did not result in any favourable result for the respondent who then filed the applications under Section 11 on 6th November 2013. Rightly holding that the claims were hopelessly time-barred, the Supreme Court set aside the order of the concerned High Court appointing an arbitrator.

Both these cases concerned hopelessly time-barred claims on the face of it, and a reference to arbitration was rightly rejected.

C. B&T AG v. Ministry of Defence

Although even in *B&T AG*, the Supreme Court holds that the case is undoubtedly one of a hopelessly barred claim, it is the author's view that the facts weren't as clear cut as the above two cases. Furthermore, the Supreme Court's reasoning to reach the said conclusion is slightly tortured and inexplicably relies on judgments arising under the repealed Arbitration Act of 1940 under which, contrary to the position under the Arbitration Act (of 1996), the jurisdiction to decide questions of non-arbitrability including issues of limitation and accord and satisfaction rested with the courts. In any event, the examination conducted by the Supreme Court in that case most certainly did not fit the criteria of examination on a demurrer as prescribed by *Vidya Drolia*.

In *B&T AG*, the Supreme Court was concerned with disputes arising out of a contract dated 27th March 2012 between a Swiss arms company (B&T AG) and the Ministry of Defence. Disputes arose between the parties in relation to the purported wrongful encashment of a bank guarantee by the Ministry of Defence on 16th February 2016, which was eventually

deducted on 26th September 2016. It was B&T AG's case that after such encashment of the bank guarantee parties were engaged in bilateral discussions, but the Ministry of Defence for the first time communicated to B&T AG that it would not reconsider the request by way of letter dated 22nd September 2017. B&T AG claimed that there was further negotiation between parties till 2019 but eventually, B&T AG invoked arbitration on 8th November 2021. Quite pertinently, in its response to the invocation dated 18th February 2022, the Defence Ministry did not oppose a reference to arbitration but objected to the appointment of a sole arbitrator (the contract itself provided for a 3-member tribunal). B&T AG claimed the benefit of the Supreme Court's *suo moto* order extending limitation on the ground of Covid and also relied on the 3-judge bench judgment of the Supreme Court in *Geo Miller and Co. Pvt. Ltd. v. Rajasthan Vidyut Utpadan Nigam Limited*[18], whereby the Supreme Court laid down the foundation for claiming exclusion of time period *bona fide* spent on exhausting pre-arbitration negotiations.

On the other hand, the Ministry of Defence contended that cause of action arose on 26th September 2016 when the amounts were finally deducted by the Government, and consequently, the limitation expired on 25th September 2019. It is pertinent to note that the Supreme Court's *suo moto* Covid Order took effect on 15th March 2020, a mere 6 months away even from the Defence Ministry's admitted position on when the cause of action arose.

In its judgment, the Supreme Court states that the question that falls for consideration is "*whether time-barred claims or claims which are barred by limitation, can be said to be live claims, which can be referred to arbitration?*", which in the framing itself goes wrong. To answer the question as framed, the nature of the Court's scrutiny will need to be such as would be prohibited under Section 11 after the 2016 Amendment Act. One must mention the apt epigram that if one asks the wrong question, one will get the wrong answer.

Thereafter, while analysing the case law on the subject, the Supreme Court most confoundingly and inexplicably relies on three judgments of the Supreme Court arising under the Arbitration Act, 1940, under which, as already mentioned, the position of law prevailing was contrary to that under Section 11 of the Arbitration Act (of 1996) as has also been noted in *Vidya Drolia*[19].

The Supreme Court then notes the judgments in *Patel Engineering* and *National Insurance*

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[18] (2020) 14 SCC 643.
[19] *Id* at 3, ¶ 84.

Company Ltd. v. Boghara Polyfab Pvt Ltd.[18], which follows *Patel Engineering*, without explaining that the position of law has changed thereafter.

Basis its reading of the law, including the aforementioned judgments and the record, the Supreme Court arrives at a finding that the disputes actually cropped up way back in 2014 itself, which does not seem to be either party's case, with the Defence Ministry itself only relying on the date of 26th September 2016 for when the cause of action arose. The Supreme Court further holds that when the bank guarantee came to be encashed and stood transferred to the Government's account in 2016, that was the end of the matter, and the basis of such finding came to the conclusion that the case on hand is a "*hopelessly barred claim*". Such a conclusion does not give due credence to B&T AG's submission on Geo Miller, which at the very least was an arguable contention, and completely ignores that accounting for the Covid period exclusion, B&T AG's claims would be a mere 6 months short of the limitation, even if B&T AG's case on the negotiation period not being excluded were to be rejected. Further, it seems to disregard the contemporaneous response of the Defence Ministry in replying to but not opposing the arbitration invocation itself but objecting to the appointment of a sole arbitrator.

Ultimately, it is not the author's contention that the Supreme Court was wrong in its finding on limitation but rather that the Supreme Court's willingness to even entertain the objections in a closely contested case of this sort is worrying and is a troubling departure from the contours of judicial review set up in *Vidya Drolia*. The *B&T AG* case was not one where it was readily apparent that the claims were time-barred, and, the applicant, B&T AG, seemed to have a wholly arguable case on the exclusion of time spent on pre-arbitration negotiations. In this background, the Supreme Court's reliance on cases under the Arbitration Act of 1940 and citation of *Patel Engineering* and *Boghra Polyfab*[20], without noting that they have both been over-ruled, is particularly deficient in the requisite judicial rigours which one would expect from the Apex Court.

IV. CONCLUSION

The effect of the amendments to Section 11 and other consequential amendments under the Amendment Act of 2019 (once enforced) would be to denude the courts of the jurisdiction to appoint arbitrators and endow it solely to designated arbitral institutions, thereby making it a purely administrative action and ending all the hand-wringing surrounding the depth and

[20] (2009) 1 SCC 267.

width of court interference.

Till such time, however, the Supreme Court's judgment in *B&T AG* may provide unwarranted support to an unscrupulous litigant seeking to merely obstruct and delay a rightful claimant.