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# Grant of Interest in Arbitral Awards: Understanding the Supreme Court's Perspective in its Recent Ruling in a Construction Dispute

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## MRP Advisory

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### INTRODUCTION

Construction disputes, especially in large infrastructure projects, are often resolved through arbitration, a method intended to be faster and more straightforward than court litigation. However, when the losing party is dissatisfied with the outcome, they may challenge the arbitral award in court, and further even before the Supreme Court. This post-arbitration litigation can seem frustrating, as it extends the process, defeating the very purpose of arbitration, which is to save time and avoid lengthy court proceedings.

Despite this, there is a positive aspect when the Supreme Court intervenes in such disputes. Its judgments provide legal clarity and finality on key issues, not only resolving the immediate case but also setting legal precedents for similar future disputes.

Recently, in *PAM Developments Pvt. Ltd. v. State of West Bengal*<sup>1</sup> (“*PAM Developments*”), the Supreme Court addressed the validity of an arbitral award concerning interest in a road project dispute. The case sheds light on the arbitrator's power to grant interest, a debated issue in arbitration. By clarifying the distinction between pre-reference, *pendente lite*, and post-award interest, the Court has reinforced the legal framework governing such awards, ensuring greater consistency in future arbitration cases.

### INDIAN LEGAL FRAMEWORK AND JUDICIAL LANDSCAPE REGARDING GRANT OF INTEREST IN ARBITRAL AWARDS

Prior to 1996, there was no specific provision that empowered an arbitrator to grant interest under the Arbitration Act, 1940. However, the arbitrators' powers to award interest were determined by judicial pronouncements. An important case in this context is *Secretary, Irrigation Department, Government of Orissa v. G.C. Roy*<sup>2</sup>, where the Supreme Court held that an arbitrator could award interest even if the contract was silent on the matter, provided it was not expressly prohibited, on the rationale that a person who has been deprived of the use of money to which he is legitimately entitled has a right to be compensated for the same.

The Arbitration and Conciliation Act, 1996 (“the 1996 Act”) brought more clarity to the issue. Under Section 31(7) of the 1996 Act, the arbitrator's discretion to grant interest is clearly outlined, where Section 31(7)(a) provides that arbitrators can award interest from the cause of action to the award date unless agreed otherwise by the parties, and Section 31(7)(b) lays down that the post-award interest is to be set at 2% higher than the current rate unless the award specifies otherwise. Consequently, the scope of judicial scrutiny is now largely restricted to examining whether or not the arbitrators acted within their jurisdiction.

One of the important considerations while awarding pre-reference interest is the language of Section 31(7)(a), which says the interest can be awarded “unless agreed otherwise by the parties”. Accordingly, the courts have limited the arbitrator's discretion when contractual provisions expressly exclude the payment of interest.

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This distinction was emphasized in the case of *Sayeed Ahmed & Company v. State of Uttar Pradesh*<sup>3</sup>, where the Supreme Court held that if the agreement between the parties bars the award of interest, arbitrators are bound to follow that stipulation. This ruling reinforced the principle that party autonomy, as reflected in the contract, must be respected.

## SUPREME COURT'S DECISION IN *PAM DEVELOPMENTS* (2024)

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In the said case, one of the claims pertained to the interest awarded by the arbitrator on the sums that were awarded to the appellant. Specifically, it involved the interest calculated from the date of the claim until the date of the award.

The arbitrator had awarded interest at the rate of 12% per annum from 12 April 2016 (the date on which the claim was made by the appellant), to 30 January 2018 (the date of the award). Additionally, post-award interest was set at 9.25% per annum until the actual payment was made. This award was based on the principle that the appellant should be compensated for the time value of money due to the delayed payments.

The High Court rejected the pre-reference interest awarded by the arbitrator. The Supreme Court examined the reasoning behind the High Court's rejection and found it lacking. The Court emphasized that the arbitrator had provided cogent reasons for awarding pre-reference interest, which were not irrational or against public policy.

The Court reiterated the principle that a party should be compensated for the loss of use of money that was rightfully theirs but was delayed in being paid, and that denying pre-reference interest would unjustly enrich the respondent at the expense of the appellant.

The Supreme Court thereby allowed the appeal concerning the interest component, thereby reinstating the arbitrator's award for pre-reference interest. The Court concluded that the appellant was entitled to claim pre-reference interest as originally awarded by the arbitrator, affirming the importance of fair compensation for delays in payment.

## KEY TAKEAWAYS FROM THE JUDGEMENT

Under the 1996 Act, the power of the arbitrator to grant interest is governed by the statutory provision in Section 31(7). This provision has two parts. Under sub-section (a), the arbitrator can award interest for the period between the date of cause of action to the date of the award, *unless otherwise agreed by the parties*. Sub-section (b) provides that unless the award directs otherwise, the sum directed to be paid by an arbitral award shall carry interest at the rate of 2% higher than the current rate of interest, from the date of the award to the date of payment.

The Supreme Court also emphasized on the difference between the Arbitration Act, 1940 and the 1996 Act. The wording of Section 31(7)(a) of the 1996 Act marks a departure from Arbitration Act, 1940 in two ways: *first*, it does not make an explicit distinction between pre-reference and *pendente lite* interest as both of them are provided for under this subsection; *second*, it upheld party autonomy and restricts the power to grant pre-reference and *pendente lite* interest the moment the agreement bars payment of interest, even if it is not a specific bar against the arbitrator.

An interesting approach adopted by the Supreme Court in this case was the classification of interest into substantive and procedural categories. It was observed that while *pendente lite* interest is a matter of procedural law, pre-reference interest is governed by substantive law.

Therefore, the grant of pre-reference interest cannot be sourced solely in Section 31(7)(a) (which is a procedural law). *Pendente lite* interest, being procedural, follows the arbitration's local procedural rules, while pre-reference interest, considered substantive, must be grounded in the parties' agreement and statutory provisions.

The author finds this distinction to be useful, especially in international arbitration, where multiple legal systems come into play. It helps ensure that procedural matters adhere to the governing law of the arbitration seat, while substantive issues, like interest claims, follow the applicable law of agreement, reducing jurisdictional conflicts. This classification also aids in determining the proper scope of law application and mitigates confusion over the interplay between procedural and substantive elements across different legal systems. [Access my saved content](#)

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### CONCLUSION


The Supreme Court's ruling in *PAM Developments case* has reaffirmed the broad discretion of arbitrators in awarding interest in arbitral proceedings. It serves as an important reminder that parties should be diligent when drafting contracts, particularly concerning interest provisions.

Additionally, the Supreme Court's observations in this case highlight the procedural nuances between Section 34 and Section 37, reaffirming the limited scope of judicial interference in arbitral awards. Arbitrators remain the primary decision-makers on issues of interest, with courts only intervening when there is a clear violation of law or contract.

The judicial landscape continues to evolve, and this latest ruling is a significant step in affirming the autonomy of arbitral tribunals while promoting the need for fairness in compensating parties for delayed payments. The Supreme Court's judgment in this case reflects a balanced approach to contractual interpretation, the rights of parties to claim interest, and the respect for arbitral awards. The judgment will serve as a significant reference point for similar disputes in the future.


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