S.N. PRASAD

v.

MONNET FINANCE LTD. AND ORS.

(Civil Appeal No. 9224 of 2010 etc.)

OCTOBER 22, 2010

[R.V. RAVEENDRAN AND H.L. GOKHALE, JJ.]

Arbitration and Conciliation Act, 1996:

ss.7(4)(a), (b), 7(5) – Arbitration agreement – Parties to – Appellant was not a party to the tri-partite agreements containing arbitration clause executed between lender, borrower and guarantor – Prior to loan agreements, a letter was given by appellant to the lender indicating his willingness to stand guarantee for loan – The said letter did not contain a provision for arbitration nor did it refer to any document containing an arbitration clause – Arbitration award directing appellant also, to repay the loan amount and interest thereon – Held: If there is a dispute between a party to an arbitration agreement, with other parties to the arbitration agreement as also non-parties to the arbitration agreement, reference to arbitration or appointment of arbitrator can be only with respect to the parties to the arbitration agreement and not the non-parties – As there was no arbitration agreement between the lender and the appellant as defined u/ss.7(4)(a) or (b) or 7(5), the claim against appellant could not be referred to arbitration nor could any award be made against him – Awards against appellant liable to be set aside u/s.34(2)(a)(ii).

s.7(4)(c) – When can an exchange of statements of claims and defence be construed as an 'arbitration agreement' – Meaning of the words 'existence of the agreement is alleged by one party and not denied by the other party' Application by lender company u/s.11 referring to the loan agreement containing the arbitration clause, which

A *was executed by borrower and guarantor in favour of lender – The said application not alleging or referring to the existence of any arbitration agreement between lender and appellant – Held: In such a case, the question of the appellant accepting such arbitration agreement by 'non-denial' would not arise.*

B *Pleadings: 'Allegation' of existence of an 'arbitration agreement' and denial thereof in the statement of defence – Discussed.*

Words and phrases: 'allegation' and 'statement of claim C *and defence – Meaning of.*

The second respondent company (borrower) sought a loan of Rs.75 lakhs. The first respondent company (lender) sanctioned the loan. The appellant by letter dated 27.10.1995 in his capacity as a director of the borrower D **company agreed to guarantee the loan of Rs.75 lakhs sanctioned by the lender company. The third respondent was also the director of the borrower company. On 28.10.1995, a tri-partite loan agreement was entered into between the lender company, the borrower company and** E **the third respondent as the guarantor, in regard to the lending of a sum of Rs.50 lakhs. The agreement provided for the arbitration clause. Similarly another tri-partite loan agreement was entered in respect of a loan of Rs.25 lakhs on 6.11.1995 among the lender company, the** F **borrower company and the third respondent followed by a promissory note by the borrower company and a deed of guarantee by the third respondent. The appellant was not a party to the loan agreements nor did he execute any separate deed of guarantee or other document in favour** G **of the lender company. The loan agreements also did not refer to the letter of guarantee by the appellant.**

The lender company issued a notice demanding payment and proposing to refer the claims against the borrower company and its guarantors for arbitration. This H **was followed by two applications by the lender company**

under Section 11 of the Arbitration and Conciliation Act, 1996 for appointment of an arbitrator. The borrower company, its Director-cum-Guarantor, and the appellant were impleaded as respondents in the said application. A

The arbitrator was appointed who passed two awards. The first award directed the borrower company, the third respondent and the appellant to pay Rs.96.23 lakhs including interest in respect of the loan amount of Rs.50 lakhs. The second award directed the borrower company, the third respondent and the appellant to pay Rs.46.49 lakhs including the interest in respect of loan of Rs.25 lakhs. The awards were challenged by the appellant, the borrower company and the third respondent. The High Court upheld the awards. The instant appeals were filed challenging the order of the High Court. B C D

It was contended for the appellant that he was not a party to the tri-partite loan agreements containing the arbitration clause and he merely gave a short letter dated 27.10.1995 standing guarantee for a loan of Rs.75 lakhs sanctioned by the lender company. As there was no arbitration agreement between the lender company and the appellant, the claim against the appellant could not be referred to arbitration, nor could any award be made against him. The awards against the appellant were, therefore, liable to be set aside under Section 34(2)(a)(ii) of the Arbitration and Conciliation Act. E F

Allowing the appeals, the Court

HELD: 1.1. Section 2(b) of the Arbitration and Conciliation Act, 1996 defines "arbitration agreement' as an agreement referred to in Section 7 of the Act. Section 7 of the Act defines an 'arbitration agreement'. Sub-section (1) of Section 7 defines an arbitration agreement as an agreement by the parties to submit to arbitration all or certain disputes which have arisen or which may G H

A arise between them in respect of a defined legal relationship, whether contractual or not. Sub-section (2) provides that an arbitration agreement may be in the form of an arbitration clause in a contract or in the form of a separate agreement. Sub-section (3) requires an B arbitration agreement to be in writing. Sub-section (4) explains as to when an arbitration agreement could be said to be in writing, that is : (a) a document signed by the parties; (b) an exchange of letters, telex, telegrams or other means of telecommunication which provide a C record of the arbitration agreement; or (c) an exchange of statements of claim and defence in which the existence of the arbitration agreement is alleged by one party and not denied by the other. Sub-section (5) provides that the reference in a contract to a document D containing an arbitration clause constitutes an arbitration agreement if the contract is in writing and the reference is such as to make that arbitration clause a part of the contract. Thus, there can be reference to arbitration only if there is an arbitration agreement between the parties. The Act makes it clear that an arbitrator can be appointed E under the Act at the instance of a party to an arbitration agreement only in respect of disputes with another party to the arbitration agreement. If there is a dispute between a party to an arbitration agreement, with other parties to the arbitration agreement as also non-parties to the F arbitration agreement, reference to arbitration or appointment of arbitrator can be only with respect to the parties to the arbitration agreement and not the non-parties. [Para 7] [217-F-G; 218-A-E]

G 1.2. There is no dispute that the loan agreements among the lender company, the borrower company and the third respondent (guarantor) contained a provision for arbitration. But the appellant was not a party to the same. In fact, the appellant's letter of guarantee for Rs.75 H lakhs was given on 27.10.1995, prior to the dates of the

two loan agreements. It was also not disputed that the letter dated 27.10.1995 given by the appellant to the lender company did not contain a provision for arbitration; and that except the said letter dated 27.10.1995, the appellant did not execute any document or issue any communication. An arbitration agreement between the lender on the one hand and the borrower and one of the guarantors on the other, cannot be deemed or construed to be an arbitration agreement in respect of another guarantor who was not a party to the arbitration agreement. Therefore, there was no arbitration agreement as defined under Section 7(4)(a) or (b) of the Act, in so far as appellant was concerned, though there was an arbitration agreement as defined under Section 7(4)(a) of the Act in regard to the borrower company and third respondent. As the letter dated 27.10.1995 did not refer to any document containing an arbitration clause, there was also no arbitration agreement between lender company and the appellant as contemplated under Section 7(5) of the Act. [Para 8] [218-A-H; 219-A-D]

1.3. To constitute an arbitration agreement under Section 7(4)(c) of the Act, what is required is a statement of claim containing a specific allegation about the existence of an arbitration agreement by the applicant and 'non-denial' thereof by the other party. An 'allegation' is an assertion or declaration about a fact and also refers to the narration of a transaction. The statement of claim filed by the lender company before the arbitrator does not contain an allegation or assertion of an arbitration agreement with the appellant. Nor has the appellant accepted the existence of any arbitration agreement by not denying such arbitration agreement in the defence filed before the arbitrator. On the other hand, the appellant had specifically contended before the arbitrator that there was no arbitration agreement between them and, therefore, the arbitrator did not have jurisdiction. The

A words 'statements of claim and defence' occurring in Section 7(4)(c) of the Act, are not restricted to the statement of claim and defence filed before the arbitrator. If there is an assertion of existence of an arbitration agreement in any suit, petition or application filed before
B any court, and if there is no denial thereof in the defence/ counter/written statement thereto filed by the other party to such suit, petition or application, then it can be said that there is an "exchange of statements of claim and defence" for the purposes of Section 7(4)(c) of the Act. It
C follows that if in the application filed under Section 11 of the Act, the applicant asserts the existence of an arbitration agreement with each of the respondents and if the respondents do not deny the said assertion, in their statement of defence, the court can proceed on the basis that there is an arbitration agreement in writing between
D the parties. In the instant case, the application filed by the lender company under Section 11 of the Act referred to the loan agreement containing the arbitration clause, which was executed by the borrower company and the third respondent as borrower and guarantor in favour of
E the lender company. The said application did not allege or refer to the existence of any arbitration agreement between the lender company and the appellant. There was absolutely no reference to any agreement between the lender company and the appellant or the existence
F of any arbitration agreement between them. If there was no reference to the existence of any arbitration agreement with appellant, the question of the appellant accepting such arbitration agreement by 'non-denial' did not arise. [Paras 10, 11, 13] [220-A-E; 223-B-C]

G 1.4. The Designate of the Chief Justice, in his order dated 23.5.2000 appointing the arbitrator, had observed that there was no dispute regarding the existence of the arbitration agreement. The arbitrator had held that in view of the positive finding of the Designate of the Chief
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Justice about the existence of an arbitration agreement notwithstanding the fact that the letter of guarantee did not refer to the loan agreement which was executed subsequently, it could not be said that there was no arbitration agreement between the parties. The arbitrator ought to have considered and decided the objections of the appellant that he was not a party to the arbitration agreement on merits, instead of referring to the order of the Designate of the Chief Justice appointing the arbitrator. During the relevant period, the law was that the orders under Section 11 of the Act were administrative orders and that the Designate of the Chief Justice appointing an arbitrator was not adjudicating on any disputed question of fact, including the existence of any valid arbitration agreement; and that the arbitrator was required to decide about the existence of arbitration agreement and the arbitrability. [Para 15] [222-F-H; 223-A-D]

SBP & Co. v. Patel Engineering Ltd. **(2005) 8 SCC 618 – referred to.**

2. When the appellant gave the guarantee letter dated 27.10.1995, he could not be imputed with the knowledge that the loan agreements which were to be executed in future (on 28.10.1995 and 6.11.1995) would contain an arbitration clause. Further, the appellant did not state in his letter dated 27.10.1995 that he would be bound by the terms of loan agreement/s that may be executed by the borrower. Therefore, the question of appellant impliedly agreeing to the arbitration clause did not arise. The apprehension of the lender company that an anomalous situation may arise if there are two proceedings (one arbitration proceedings against the borrower and one guarantor and a suit against another guarantor), is not a relevant consideration as any such anomalous situation, if it arises, would be the own-making of the lender company, as that is the consequence of its failure to

A **require the appellant to join in the execution of the loan agreements. Having made only one of the guarantors to execute the loan agreements and having failed to get the appellant to execute the loan agreements, the lender company cannot contend that the appellant who did not**
B **sign the loan agreements containing the arbitration clause should also be deemed to be a party to the arbitration and be bound by the awards. The issue is not one of convenience and expediency. The issue is whether there was an arbitration agreement with the**
C **appellant. As there was no arbitration agreement between the parties (the lender company and the appellant), the impleading of appellant as a respondent in the arbitration proceedings and the award against the appellant in such arbitration cannot be sustained. As a consequence, both**
D **the arbitration awards, as against the appellant are liable to be set aside. If the lender company wants to enforce the alleged guarantee of the appellant, it is open to the first respondent to do so in accordance with law. [Paras 17-19] [224-C-H; 225-A-B]**

E **Case Law Reference:**

(2005) 8 SCC 618 referred to Para 15

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 9224 of 2010.

F From the Judgment & Order dated 22.05.2006 of the High Court of Delhi at New Delhi in O.M.P. No. 319 of 2002.

WITH

Civil Appeal No. 9225 of 2010.

G

Dr. Rajeev Dhawan, Gaurav Kejriwal, Keshav Mohan for the Appellant.

S.P. Kalra, Rajiv Kapoor, Sumit Kumar for the Respondents.

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The Judgment of the Court was delivered by

R.V.RAVEENDRAN, J. 1. Leave granted. These appeals involve the question whether a guarantor for a loan, who is not a party to the loan agreement containing the arbitration agreement executed between the lender and borrower, can be made a party to a reference to arbitration in regard to a dispute relating to repayment of such loan and subjected to the arbitration award.

2. The second respondent company is a borrower from the first respondent. Third respondent is the Managing Director of the second respondent. The appellant, father of the third respondent, was a Director of the second respondent. The second respondent (also referred to as 'borrower') after repaying an earlier loan taken from the first respondent (also referred to as the 'lender'), sought a fresh loan of Rs.75 lakhs. The first respondent sanctioned the loan. The appellant by letter dated 27.10.1995 in his capacity as a Director of the second respondent, stood guarantee for the loan of Rs.75 lakhs sanctioned by the first respondent.

3. A loan agreement dated 28.10.1995 was entered between the lender, the borrower, and the third respondent as the guarantor, in regard to the lending of a sum of Rs.50 lakhs. The agreement provided that the amount advanced had to be repaid within three months with interest at 20% per annum and if there was default, the borrower was liable to pay a compound interest at the rate of 5% per month with quarterly rests. Clause 18 of the said loan agreement provided for settlement of disputes by arbitration. In addition to the loan agreement, the borrower executed an on demand promissory note for the amount borrowed and the third respondent executed a Deed of Guarantee guaranteeing repayment of the loan amount with interest. Similarly, a tripartite loan agreement was entered in respect of a loan of Rs.2500,000/- on 6.11.1995, among the first respondent, second respondent and third respondent followed by a promissory note by second respondent and deed

A of Guarantee by third respondent. The appellant was not a party to the loan agreements nor did he execute any separate deeds of guarantee or other document in favour of the first respondent. The loan agreements did not refer to the letter of guarantee by the appellant.

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4. The lender issued a notice through counsel demanding payment and proposing to refer the claims against the borrower and its guarantors for arbitration. This was followed by two applications by the lender under section 11 of the Arbitration and Conciliation Act, 1996 ('Act' for short) for appointment of C an Arbitrator. The borrower, its Managing Director-cum-Guarantor, and the appellant were impleaded as respondents in the said application.

5. The High Court of Delhi by two orders dated 23.5.2000 D appointed a retired Judge of the High Court as the sole arbitrator. The arbitrations ended in two awards dated 1.5.2002. The first award directed respondents 2 and 3 and appellant to pay Rs.93,23,288/- (that is Rs.50 lakhs with interest at 20% up to the date of the appointment of arbitrator) with interest at 18% E per annum from 24.5.2000. Similarly the second award directed respondents 2 and 3 and appellant to pay Rs.46,49,315/- (that is Rs.25 lakhs with interest at 20% upto the date of appointment of arbitrator) with interest at 18% per annum from 24.5.2000. The two arbitration awards were challenged by the appellant F by filing applications under section 34 of the Act (OMP No.319/2002 and 322/2002). The second and third respondents also challenged the awards in OMP No.320/2002 and 321/2002. A learned single Judge of the Delhi High Court by a common order dated 22.5.2006 dismissed the said applications. The G said common order dated 22.5.2006, insofar as it dismisses OMP 319/2002 and 322/2002, is challenged by the appellant in this appeals by special leave.

6. The following contentions are urged by the appellant :

H (i) The appellant was not a party to the tripartite loan

agreements executed among respondents 1, 2 and 3 (that is the lender, the borrower and borrower's Managing Director-cum-Guarantor) containing the arbitration clause. He had merely given a short letter dated 27.10.1995 standing guarantee for a loan of Rs.75 lakhs sanctioned by the first respondent. As there was no arbitration agreement between the first respondent and appellant, the claim against the appellant could not be referred to arbitration, nor could any award be made against him. The awards against the appellant were therefore liable to be set aside under section 34(2)(a)(ii) of the Act.

(ii) The appellant had merely given a letter dated 27.10.1995 indicating his willingness to stand guarantee, but he did not execute the loan agreement or any deed of guarantee, as it was decided that the third respondent would be the guarantor instead of appellant. Consequently, the third respondent executed the loan agreement as guarantor as also a deed of Guarantee. Therefore, the appellant was not a guarantor and is not liable.

(iii) Even assuming without conceding that there was an arbitration agreement between the appellant and first respondent, and that he was liable in respect of the loan amount, there could be no award for interest against him as he had not agreed to guarantee the payment of interest.

Re : Contention (i)

7. Section 2(b) defines "arbitration agreement' as an agreement referred to in section 7 of the Act. Section 2(h) defines "party" as party to an arbitration agreement. Section 7 of the Act defines an 'arbitration agreement'. Sub-section (1) of Section 7 defines an arbitration agreement as an agreement by the parties to submit to arbitration all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not. Sub-section (2) provides that an arbitration agreement may be in

A the form of an arbitration clause in a contract or in the form of a separate agreement. Sub-section (3) requires an arbitration agreement to be in writing. Sub-section (4) explains as to when an arbitration agreement could be said to be in writing, that is : (a) a document signed by the parties; (b) an exchange of
B letters, telex, telegrams or other means of telecommunication which provide a record of the arbitration agreement; or (c) an exchange of statements of claim and defence in which the existence of the arbitration agreement is alleged by one party and not denied by the other. Sub-section (5) provides that the
C reference in a contract to a document containing an arbitration clause constitutes an arbitration agreement if the contract is in writing and the reference is such as to make that arbitration clause a part of the contract. Thus there can be reference to arbitration only if there is an arbitration agreement between the
D parties. The Act makes it clear that an Arbitrator can be appointed under the Act at the instance of a party to an arbitration agreement only in respect of disputes with another party to the arbitration agreement. If there is a dispute between a party to an arbitration agreement, with other parties to the
E arbitration agreement as also non-parties to the arbitration agreement, reference to arbitration or appointment of arbitrator can be only with respect to the parties to the arbitration agreement and not the non-parties.

8. There is no dispute that the loan agreements among the
F first respondent (lender), the second respondent (borrower) and the third respondent (guarantor) contained a provision for arbitration. The said provision for arbitration is extracted below:

> "In the event of any dispute, question or difference *arising out of or in connection with this agreement* and the
G *respective rights and obligations of the parties hereunder*, the same shall be referred to the arbitration in accordance with the provisions of the Arbitration Act, 1940."

But the appellant was not a party to the same. In fact appellant's
H letter of guarantee for Rs.75 lakhs was given on 27.10.1995,

prior to the dates of the two loan agreements. It is also not in dispute that the letter dated 27.10.1995 given by appellant to the first respondent did not contain a provision for arbitration; and that except the said letter dated 27.10.1995, the appellant did not execute any document or issue any communication. An arbitration agreement between the lender on the one hand and the borrower and one of the guarantors on the other, cannot be deemed or construed to be an arbitration agreement in respect of another guarantor who was not a party to the arbitration agreement. Therefore, there was no arbitration agreement as defined under section 7(4)(a) or (b) of the Act, in so far as appellant was concerned, though there was an arbitration agreement as defined under section 7(4)(a) of the Act in regard to the second and third respondents. As the letter dated 27.10.1995 does not refer to any document containing an arbitration clause, there is also no arbitration agreement between first respondent and appellant as contemplated under section 7(5) of the Act.

9. What therefore remains to be considered is whether there is an arbitration agreement as contemplated under section 7(4)(c) of the Act, which provides that an arbitration agreement in writing can be said to exist, if it is contained in an exchange of statements of claim and defence in which the existence of the arbitration agreement is alleged by one party and not denied by the other. The statement of claim filed by the first respondent before the arbitrator does not contain an allegation or assertion of an arbitration agreement between the first respondent and appellant. Nor has the appellant accepted the existence of any arbitration agreement by not denying such arbitration agreement in the defence filed before the arbitrator. On the other hand, the appellant specifically contended before the arbitrator that there was no arbitration agreement between them (first respondent and appellant) and therefore the arbitrator did not have jurisdiction.

10. But the words, 'statements of claim and defence'

A occurring in section 7(4)(c) of the Act, are not restricted to the statement of claim and defence filed before the arbitrator. If there is an assertion of existence of an arbitration agreement in any suit, petition or application filed before any court, and if there is no denial thereof in the defence/counter/written B statement thereto filed by the other party to such suit, petition or application, then it can be said that there is an "exchange of statements of claim and defence" for the purposes of section 7(4)(c) of the Act. It follows that if in the application filed under section 11 of the Act, the applicant asserts the existence of an C arbitration agreement with each of the respondents and if the respondents do not deny the said assertion, in their statement of defence, the court can proceed on the basis that there is an arbitration agreement in writing between the parties.

11. The question therefore is whether in this case, the D application under section 11 of the Act had alleged the existence of an arbitration agreement between first respondent and appellant and such allegation was accepted by non-denial thereof, by the appellant. The application filed by the first respondent under section 11 of the Act referred to the loan E agreement containing the arbitration clause, which was executed by respondents 2 and 3 as borrower and guarantor in favour of the first respondent. The application specifically relied upon the provisions of clause 18 of the loan agreement as the arbitration agreement under which appointment of an F arbitrator was sought. Significantly, the application under section 11 of the Act did not allege or refer to the existence of any arbitration agreement between the first respondent and the appellant. The only averment found in the entire application with reference to the document executed by the appellant is G extracted below:

> "Respondent No.3 vide his letter dated 27.10.95 guaranteed the repayment of the total amount of loan i.e. Rs.75,00,000 (Rupees Seventy Five Lakhs) sanctioned by the Petitioner to Respondent No.1. Copy of the letter dated

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27.10.95 from Respondent No.3 guaranteeing repayment of loans is annexed herewith and marked as "ANNEXURE-C". A

(Note: The term 'petitioner' refers to the lender, respondent No.1 refers to the borrower and respondent No.3 refers to the appellant). B

Except the aforesaid averment, there is absolutely no reference to any agreement between the first respondent and the appellant or the existence of any arbitration agreement between them. Therefore the application filed by the first respondent C under section 11 of the Act referring to the loan agreement with respondents 2 and 3 containing the arbitration agreement cannot be considered or construed to be an allegation of existence of an arbitration agreement between first respondent and appellant. If there was no reference to the existence of D any arbitration agreement with appellant, the question of the appellant accepting such arbitration agreement by 'non-denial' does not arise.

12. The first respondent contended that the application E under section 11 of the Act consisted of two parts, that is a preamble containing three columns - column (1) relating to the "provision under which the application was filed", column (2) relating to "Name of applicant with complete address" and column (3) relating to "Name of the other parties to the F arbitration agreement with complete address"; and the second part contained the running averments. It is submitted that the name of first respondent is shown as the applicant in column (2); and against column (3) relating to "Names of the other parties to the arbitration agreement", the names of Hitek Industries (second respondent), Prem Prakash Verma (third G respondent) and S.N. Prasad (appellant) was shown and that amounted to an allegation that the appellant was a party to the arbitration agreement.

13. To constitute an arbitration agreement under section H

A 7(4)(c) of the Act, what is required is a statement of claim containing a specific allegation about the existence of an arbitration agreement by the applicant and 'non-denial' thereof by the other party. An 'allegation' is an assertion or declaration about a fact and also refers to the narration of a transaction. B As noticed above, in the entire application under section 11 of the Act, there was no allegation as to the existence of any arbitration agreement between first respondent and the appellant. Column (3) containing "Names of other parties to arbitration agreement with addresses" cannot be considered C to be an assertion or declaration about the existence of an arbitration agreement between the first respondent and appellant. Section 7(4)(c) of the Act cannot therefore be relied upon to prove the existence of an Arbitration agreement.

14. It is of some relevance to note that in the year 1998 D when the applications under section 11 of the Act was filed and in the year 2000 when the applications were allowed, an application under section 11 of the Act was not considered to be a judicial proceeding and the order appointing an arbitrator was considered to be an administrative order. Therefore at the E relevant time, the application under section 11 of the Act and the counter if any thereto were not in the nature of 'statements of claim and defence'. Be that as it may.

15. Before the Arbitrator, the appellant specifically F contended that by relying upon the section 2(1)(h) and section 7 of the Act that he was not a party to the arbitration agreement and therefore there could be no arbitration in regard to the claim against him. The said contention was rejected by the arbitrator on the ground that the designate of the Chief Justice, in his G order dated 23.5.2000 appointing the arbitrator, had observed that the existence of arbitration agreement was not denied and there was no dispute regarding the existence of the arbitration agreement. But what was not denied was the arbitration agreement between first respondent and respondents 2 and 3. The arbitrator held that in view of the positive finding of the H

designate of the Chief Justice about the existence of an arbitrator agreement notwithstanding the fact that the letter of guarantee does not refer to the loan agreement which was executed subsequently, it could not be said that there was no arbitration agreement between the parties. The arbitrator ought to have considered and decided the objections of the appellant that he was not a party to the arbitration agreement on merits, instead of referring to the order of the designate of the Chief Justice appointing the arbitrator. As noted above, when the said application under section 11 of the Act was filed in 1998 and decided in 2000 (long prior to the decision in *SBP & Co. vs. Patel Engineering Ltd.* – (2005) 8 SCC 618,) the prevailing view was that the orders under section 11 of the Act were administrative orders and that the Designate of the Chief Justice appointing an arbitrator was not adjudicating on any disputed question of fact, including the existence of any valid arbitration agreement; and that the Arbitrator was required to decide about the existence of arbitration agreement and the arbitrability.

16. The first respondent contended that the appellant having agreed to be a guarantor for the repayment of the loan, can not avoid arbitration by contending that he was not a signatory to the loan agreement containing the arbitration clause. It was submitted that the liability of the principal debtor and guarantors was joint and several and therefore there could be only one proceeding against all of them; and that if the contention of the appellant was accepted, it would necessitate two proceedings in regard to the same loan transaction and same cause of action, that is an arbitration proceedings against the borrower and one of its guarantors (respondents 2 and 3) and a separate suit against the other guarantor (appellant). It was further submitted that multiple proceedings may lead to divergent findings and results, leading to an anomalous situation. It was also submitted that the letter dated 27.10.1995 guaranteeing the loan of Rs.75 lakhs was written by the appellant, as a Director of the borrower company; and that as

A the appellant had already given a guarantee letter dated 27.10.1995, he was not required to execute the tripartite loan agreements containing the arbitration clause; that the appellant was aware of the terms of the loan and was further aware that loan agreements with arbitration clause had to be executed; B and that therefore it should be deemed that the appellant had agreed to abide by the terms contained in the loan agreements, including the arbitration clause. We find no merit in these contentions.

C 17. When the appellant gave the guarantee letter dated 27.10.1995, he could not be imputed with the knowledge that the loan agreements which were to be executed in future (on 28.10.1995 and 6.11.1995) would contain an arbitration clause. Further, the appellant did not state in his letter dated 27.10.1995 that he would be bound by the terms of loan D agreement/s that may be executed by the borrower. Therefore the question of appellant impliedly agreeing to the arbitration clause does not arise.

18. The apprehension of the first respondent that an E anomalous situation may arise if there are two proceedings (one arbitration proceedings against the borrower and one guarantor and a suit against another guarantor), is not a relevant consideration as any such anomalous situation, if it arises, would be the own-making of the first respondent, as that is the F consequence of its failure to require the appellant to join in the execution of the loan agreements. Having made only one of the guarantors to execute the loan agreements and having failed to get the appellant to execute the loan agreements, the first respondent cannot contend that the appellant who did not sign the loan agreements containing the arbitration clause should G also be deemed to be a party to the arbitration and be bound by the awards. The issue is not one of convenience and expediency. The issue is whether there was an arbitration agreement with the appellant.

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19. As there was no arbitration agreement between the parties (the first respondent and appellant), the impleading of appellant as a respondent in the arbitration proceedings and the award against the appellant in such arbitration cannot be sustained. As a consequence, both the arbitration awards, as against the appellant are liable to be set aside. If the first respondent wants to enforce the alleged guarantee of the appellant, it is open to the first respondent to do so in accordance with law.

20. The above discussion and findings would also apply to the second loan covered by the loan agreement dated 6.11.1995, as the facts are the same.

Re : Contention (ii)

21. The appellant contended that on 27.10.1995 he was a Director of the borrower company and he had agreed to guarantee the loan of Rs.75 lakhs; that subsequently, it was decided as he would be resigning from his directorship on account of his advanced age, his son would be the guarantor; and that therefore, he did not become a guarantor by executing a deed of guarantee and he did not also execute the loan agreements. It was contended that the fact that ultimately the loan agreements were executed only among the lender (first respondent), the borrower company (2nd respondent) and the 3rd respondent (guarantor) and the further fact that third respondent alone executed the Deed of Guarantee, demonstrated that only third respondent was the guarantor and he was not a guarantor. According to him on execution of the loan agreements among respondents 1, 2 and 3, the letter dated 27.10.1995 given by him agreeing to be a guarantor ceased to be of any effect. We cannot examine these aspects in an appeal arising from a proceeding under section 11 of the Act. In a proceedings under section 11 of the Act, what is relevant is existence of arbitration agreement and not the defence on merits. Further, in view of our finding on the first

A contention, it is not necessary to examine this contention. It is open to appellant to urge this contention, if and when first respondent initiates action against him in accordance with law.

Re : Contention (iii)

B 22. It is true that where the letter of Guarantee issued by a guarantor, guarantees repayment of only the principal sum and does not guarantee the payment of any interest, he could not be made liable for the interest. But in view of our finding on the first contention, this issue does not survive for consideration.

C

Conclusion

23. In view of the above, these appeals are allowed and the impugned order of the High Court and awards of the Arbitrator are set aside in part, in so far as the appellant is D concerned.

D.G. Appeals allowed.