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LEX LOQUITUR

A NEWSLETTER SUMMARIZING LATEST COURT RULINGS

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Preface

Dear Reader,

Courts "rule". They actually do. Significance, application and implication of such rulings needs to be understood and appreciated.

Lex Loquitur is an endeavor to bring to you the latest rulings from the Courts and various other judicial fora. We intend to cull out the ratio of some important rulings and summarize them for your ready reference, with our observations/ comments, if any.

We trust you will find it an interesting read.

We would, however, look forward to your feedback/comments. Do write to us at:
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Warm Regards
Team Lex Loquitur
UBR LEGAL, ADVOCATES

Matters Argued by us

1. Whether audit proceedings under Rule 5A of the Service Tax Rules can be permitted when the issue of jurisdiction is under challenge?

Marwadi Shares and Finance Ltd. v. Union of India & Ors. – SLP (C) No. 27124 of 2023 [Supreme Court]

Decision: No.

The petitioner is a registered stock broker. It received a notice for audit to be conducted by CERA. Such notice was challenged before the Hon'ble Gujarat High Court on the ground, inter alia, there is no jurisdiction to conduct audit in terms of Rule 5A of the Service Tax Rules as the same is ultra vires the provisions of the Finance Act as held by the Delhi High Court. The petiton was admitted and the audit proceedings were stayed. However, subsequently, the High Court, at the request of the Revenue, directed that the Revenue can conduct the audit but not finalise the audit report as the Supreme Court has stayed the decision of the Delhi High Court. This order was challenged in SLP before the Hon'ble Supreme Court.

The Hon'ble Supreme Court allowed the petition restoring the earlier interim order passed by the Gujarat High Court. It notes that the earlier order has been in operation since 2019; and no cause for variation of the stay order arose. It directed the High Court to decide the writ petiton on merits as expeditiously as possible.

2. Whether delay of about 2 years in filing a Sales Tax Revision Petition by the State Government can be condoned in absence of sufficient cause?

Joint Commissioner of Commercial Taxes & Anr. v. Sun Microsystems India Pvt. Ltd. (now Oracle India Pvt. Ltd.) – STRP No. 7/2024 [Karnataka High Court]

Decision: No.

The respondent is a leading supplier of software and relates services. It had inter state sales and stock transfers. The Karnataka VAT authorities sought to deny exemption on stock transfers. The KVAT Appellate Tribunal allowed the benefit to the Assessee. The Revenue field a Sales Tax Revision petition before the High Court.

The Hon'ble Karnataka High Court dismissed the revision petition filed by the Department. It held: (i) there is a delay of about 2 years in filing the said petition; (ii) the State has not provided sufficient cause for the said delay; even after approval for filing petition was accorded; (iii) one officer of the State being on medical leave cannot be a ground for the state machinery to halt; (iv) relies on judgment of Supreme Court in Sivamma and its own earlier ruling in BPCL.

Matters Argued by us

3. Whether a show cause notice issued without mandatory pre-show cause notice consultation is valid in law?

Sheesha Sky Lounge Hospitality and Services Pvt. Ltd. v. Union of India & Ors. – WP No. 2574 of 2024 [Bombay High Court]

Decision: No.

The petitioner runs a restaurant. It claimed that it was a non Ac restaurant; hence; exempt from service tax. A show cause notice came to be issued proposing to demand service tax of over Rs. 1.2 crores. The said notice was challenged before the High court; in writ; on the ground that no pre-show cause notice consultation was issued; amongst other grounds.

The Hon'ble Bombay High Court set aside the show cause notice and allowed the petition. it held: (i) CBEC Master Circular dated 10 March 2017 and CBIC Circular dated 19 November 2020 mandate such consultation; (ii) These circulars are binding on the department under Section 37B of the Central Excise Act (made applicable to service tax by Section 83 of the Finance Act); (iii) rejects departments reliance on notice isssued to chartered accountant of thr petitioner to come and explain the differences; cannot be equated with pre-scn consultation; (iv) follows its earlier ruling in Rochem Case;(v) directs department to issue pre-scn; excluding the period for which petition was pending; bonafide; before the court.

4. Whether High Court has power to condone delay beyond Section 54 of the CGST Act for refund claim?

Assistant Commissioner of Central Taxes & Ors. v. M/s Merck Life Science Pvt. Ltd. – WA No. 110 of 2026 c/w connected matters [Karnataka High Court]

Decision: Yes.

The petitioner is exporting services to foreign principal. It paid IGST on such services. Later; it realised it was an "intermediary" and hence; it paid local tax (CGST + SGST). It filed claim for refund of IGST paid under mistake of law. Refund was rejected as time barred. Hence; writ petition came to be filed. The Ld. Single Judge allowed the writ petition: (i) holding refund ought to be granted; (ii) time limit under section 54 is directory and not mandatory. Hence; intra court appeal by the Revenue.

The Hon'ble Karnataka High Court held that: (i) time limit under section 54 is mandatory and not directory; (ii) however; the High court under Article 226 of the Constitution of India has power to condone delay; (iii) the state cannot unjustly enrich itself when tax was paid twice in terms of Article 265 of the Constitution; (v) refers to Supreme Court decision in Salonah Tea; (vi) in the facts of the present case; the delay was rightly condoned and directs the revenue to process the refund claim in 60 day.

5. Whether benefit under SVLDR Scheme can be denied on account of delay in payment due to technical issues and procedural irregularities?

Himtaj Ayurvedic Udyog Kendra v. Union of India & Ors. – WP No. 3262 of 2024- [Bombay High Court]

Decision: No.

The petitioner is manufacturer of "Himtaj Ayurvedic Oil". There was demand of central excise duty was raised. It filed declaration under the SVLDR Scheme. Form 3 was issued calling upon the petitioner to make payment. Lockdown was imposed due to COVID 19 pandemic. The time for payment was extended up to 30.06.2020 under the Scheme. The petitioner made the payment; however; it was returned by the bank as challan had expired. It generated a fresh challan on 15.07.2020 and made the payment. However, SVLDRS form 4 (discharge certificate) was not issued on the ground that the payment was not made in time and entity name was "Imtaj" in the challan. Hence, the petition came to be filed.

The Hon'ble Bombay High Court allowed the petition and directs the department to issue Form SVLDRS-4. It held: (i) the object of the scheme has to be considered; (ii) the eligibility of the petitioner is not disputed and hence, the payment could not be made for technical reasons; (iii) procedural irregularities cannot come in way of substantive justice; (iv) payment under SVLDRS challan or service tax challan would not make a difference as long as money was received by the Respondents; (v) follows judgment in the case of Innovative and Arjun Rampal; (vi) distinguishes Supreme Court judgment in the case Yashi Construction.

6. Whether bank accounts can be attached under Section 226(3) of the Income-tax Act without considering the assessee's representation?

Computer Graphics Pvt. Ltd. v. Union of India & Ors. – W.P. No. 10768 of 2026 [Madras High Court]

Decision: No.

The petitioner is a manufacturer. The income tax department, based on CIC data; was of the view that some TDS dues for 2007-2008 to 2024-2025. The petitioner replied stating that no dues were pending excepting some interest portion. However; the bank accounts of the petitioner came to be attached under section 226(3) of the Income Tax Act (garnishee proceedings). Hence; petition was filed.

The Hon'ble Madras High Court disposed off the petition by directing the department to consider the representation of the petitioner and pass a detailed speaking order. A hearing should be granted to the petitioner. In the mean time; the recovery proceedings would be kept in abeyance.

7. Whether criminal proceedings under IPC and GVAT Act can be sustained against directors without arraigning the company and after substantial delay?

Smt. Jyosnaben Wd/o Bhupatrai Shah & Ors. v. State of Gujarat & Ors. – R/Criminal Misc. Application No. 5869 of 2021 c/w connected matters [Gujarat High Court]

Decision: Proceedings stayed.

The Sales Tax Department filed FIR with Valsad Police Station against directors of the company for failure to pay VAT dues of over Rs.180 crores. FIR was lodged under section 406,420 of Indian Penal Code read with section 85(1)(d), 85(1)(g) and Section 86(1) and (2) of the Gujarat Value Added Tax Act. A quashing petition was filed under section 482 of the Cr. P. C. seeking quashing of the FIR.

The Hon'ble Gujarat High Court admitted the petiton and stayed the proceedings pursuant to the FIR. It noted that the FIR has been filed belatedly (in February, 2021) for non payment of taxes from 2009 to 2013. In the FIR, the company was not arraigned as a party. Finally, notes decision of the Supreme Court in case Delhi Race Club to hold that section 420 and 406 cannot be invoked simultaneously.

Matters Argued by us

8. Whether administrative and support services provided to overseas group entities qualify as "intermediary services" and disentitle refund of ITC?

Lubrizol Advance Materials India Pvt. Ltd. v. Union of India & Ors. – W.P. No. 987 of 2026 [Bombay High Court]

Decision: No.

The petitioner is a leading supplier of lubricants. It is providing administrative and sales related support services to its group entity located outside India. It claimed that the services are exported in terms of section 2(6) of the IGST Act. It claimed refund of accumulated input tax credit under section 54 of the CGST Act read with Rule 89 of the Rules. Refund was rejected holding that the petitioner is an "intermediary" under section 13(8)(b) of the Act. Hence; petition was filed.

The Hon'ble Bombay High Court set aside the order and allowed the petition. It held: (i) in the petitioners own case; under the service tax regime; it has been held that the petitioner is not an "intermediary"; (ii) similar issue has been decided in Sundyne Pumps and Vistex Asia case; (ii) in that case the High Court examined the agreement and held that the Indian subsidiary was not an "agent"; (iii) accordingly; remands the matter back to the appellant original adjudicating authority to examine the issue again.

9. Whether management fees and incentive income earned by an Asset Reconstruction Company (ARC) are taxable under "banking and financial services"?

Asset Reconstruction Company (India) Ltd. v. Principal Commissioner, CGST & Central Excise – Service Tax Appeal No. 86649 of 2017 [CESTAT, Mumbai]

Decision: No.

The appellant is the largest Asset Reconstruction Company in India. It is registered as an NBFC. It floats a "trust" for liquidation of NPAs of banks. It issues security receipts (SR) in terms of section 7 and 7A of the SARFESAI Act. It receives management fees for managing the trust as the trustee. It also earns a management incentive upside on liquidation of assets. The service tax department sought to levy service tax on the above receipts under "banking or financial" service. A demand of over Rs.50 crores along with interest and equivalent penalty was confirmed. Hence, appeal.

Hon'ble CESTAT, Mumbai set aside the order and allowed the appeal. It held: (i) for the period prior to 01.07.2012; the appellant is not providing any banking service or recovery agent service as it is undertaking a statutory function; (ii) applying the principle of "ejusdem generis" and circular dated issued by CBIC holds that it is not a banking or financial institution; (iii) for the period post negative list; holds that there is consideration; however; service is not provided from one "person" to another as trust and trustee are not different persons; (iv) follows the "mutuality principle" enunciated by the Suprem Court in Saturday Club case; (v) holds that there is no suppression of facts as the issue is one of interpretation and audit had clarified that there is no service provided to any other person; (vi) remands matter back for decision on management incentive upside in light of Supreme Court ruling.

10. Whether duty can be demanded from "persons" other than the exporter (person chargeable) under Section 11A of the Central Excise Act?

Prashant Rajnikant Mehta & Anr. v. Commissioner of Central Excise, Mumbai-I – Excise Appeal Nos. 85764 & 85765 of 2014 c/w Excise Appeal No. 85821 of 2014 [CESTAT, Mumbai]

Decision: No.

TThe appellants are individuals. M/s Baranala International, an exporter, had claimed duty drawback on export of goods. It was alleged that drawback was fraudulently claimed as no goods were actually exported. Accordingly, demand of drawback exceeding Rs. 20 crores along with interest and penalty was confirmed against the appellants on the ground that they were the "mastermind" and "ultimate beneficiaries". No penalty was imposed on M/s Baranala International. Both the appellants and the Revenue filed appeals.

The Hon'ble CESTAT, Mumbai set aside the order and allowed the appeals of the appellants while dismissing the Revenue's appeal. It held:
(i) Section 11A of the Central Excise Act provides for recovery from the "person chargeable" with duty, i.e., the exporter who was granted the drawback (M/s Baranala International); (ii) in the earlier round, the Tribunal had already held that demand can be raised only against the exporter/proprietor and not against third parties; (iii) since the appellants were neither the exporter nor the persons chargeable with duty, proceedings under Section 11A cannot be sustained against them; (iv) Rule 209 and Rule 209A of the Central Excise Rules provide for penalty only where confiscation of goods is involved; (v) in absence of any proposal or finding regarding confiscation of goods, penalty cannot be imposed either on the appellants or on the proprietor of Baranala International; (vi) consequently, demand and penalties against the appellants were set aside and Revenue's appeal seeking penalty was dismissed.

11. Whether "total CENVAT credit" under Rule 6(3A) includes only common credit or entire credit for the purpose of reversal in case of trading activity?

Castrol India Ltd. v. Commissioner of Central Excise & Service Tax, Raigad – Excise Appeal No. 86319 of 2016 [CESTAT, Mumbai]

Decision: No.

The appellant is a leading manufacturer of lubricants. It is also engaged in trading of similar products. It availed cenvat credit on inputs under Rule 3(1) of the Cenvat Credit Rules. It reversed pro rata credit relating to trading under rule 6(3) of the said rules. However; the Department was of the view that it should reverse "total cenvat credit" in terms of formula provided under Rule 6(3A) of the Rules. A demand of over Rs.1 crore was confirmed along with interest and penalties. Hence; appeal.

Hon'ble CESTAT, Mumbai set aside the order and allowed the appeal. It held: (i) cenvat credit is availed on pro rata basis and proportionate reversal for trading activity amounts to maintenance of separate records under Rule 6; (ii) Rule 6(3) only provides for options for complying with bar under Rule 6(1); (iii) the term "total cenvat credit" in formula provided under Rule 6(3A) refers to only common credit; (iv) follows its earlier decision in case of Reliance Industries and allows the appeal.

12. Whether the expression "for use" in an exemption notification is to be interpreted as intended use or actual end use or not?

Rashtriya Chemicals and Fertilizers Ltd. v. Commissioner of Central Excise & Service Tax (LTU) - Civil Appeal Nos. 2219-2220 of 2013 c/w SLP (C) No. 21441 of 2013 [Supreme Court]

Decision: Yes.

The appellant, a fertilizer manufacturer, procured Naphtha at nil rate of duty under exemption notifications on the condition that it was "for use" in the manufacture of fertilizer. The Department alleged that part of the Naphtha was used in generation of steam and electricity which was further used in non-fertilizer products, and hence denied exemption and demanded duty along with penalty. The matter travelled through multiple rounds of litigation before reaching the Supreme Court.

The Hon'ble Supreme Court allowed the appeals. It held: (i) the expression "for use" is to be interpreted as "intended for use", and not actual end-use in a strict or literal sense; (ii) once it is established that goods were procured with a genuine intention for the specified purpose, the benefit of exemption cannot be denied merely because of incidental or intermediate usage outcomes; (iii) exemption notifications linked to purpose must be construed in light of the objective of encouraging such use; (iv) where inputs are used in an integrated process (e.g., common steam generation), inability to trace exact end-use does not defeat the exemption; (v) reliance placed on earlier judgments including Dalmia Dadri Cement and SAILI.

13. Whether refund of tax can be granted to an assessee when the incidence of tax has already been passed on to consumers?

Union of India & Anr. v. Torrent Power Ltd. –SLP (C) No. 13084 of 2025 [Supreme Court]

Decision: No.

The respondent, a power company, had collected GST on ocean freight from its consumers pursuant to a notification which was later declared unconstitutional. Upon refund becoming due, the Gujarat High Court permitted the assessee to retain the refund in a separate account and pass on the benefit to consumers through tariff adjustments. Aggrieved, the Revenue filed an appeal before the Supreme Court.

The Hon'ble Supreme Court allowed the appeal. It held: (i) Section 54(5) of the CGST Act mandates that refund shall be credited to the Consumer Welfare Fund, unless covered by exceptions under Section 54(8); (ii) refund can be paid to the applicant only if it is established that the incidence of tax has not been passed on to any other person; (iii) in the present case, it was an admitted fact that the tax burden was passed on to consumers; hence, refund cannot be granted to the assessee; (iv) the High Court's mechanism of creating a separate account and adjusting tariffs is not contemplated under the statute and is therefore impermissible; (v) redistribution of refund to past consumers is impractical and unworkable; hence, the refund amount must be credited to the Consumer Welfare Fund.

14. Whether Input Tax Credit can be denied to a bona fide purchaser due to default of the supplier under Section 16(2)(c) and Rule 36(4) of the CGST Act?

Instakart Services Private Limited v. Union of India & Ors. – W.P. No. 4917 of 2021 [Karnataka High Court]

Decision: No.

The petitioner, a logistics service provider, challenged the constitutional validity of Section 16(2)(c) of the CGST/KGST Act and Rule 36(4), contending that these provisions impose an impossible burden on the recipient to ensure that the supplier has deposited tax and filed returns. It was argued that ITC cannot be denied to a bona fide purchaser for supplier's default.

The Hon'ble Karnataka High Court allowed the petition (by reading down the provisions). It held: (i) Section 16(2)(c) and Rule 36(4) cannot be applied in a manner that denies ITC to bona fide recipients who have complied with all other conditions; (ii) the law cannot compel a taxpayer to do the impossible, i.e., ensuring compliance by the supplier which is beyond the recipient's control;(iii) benefit of ITC is a vested / substantive right and cannot be denied due to supplier's default, absent fraud or collusion; (iv) reliance placed on judgments including On Quest Merchandising, Arise India, Rajesh Jain, etc., affirming that purchasing dealers cannot be penalized for supplier's failure; (v) provisions were read down to protect bona fide purchasers, instead of being struck down; (vi) Revenue is free to proceed against the defaulting supplier, but not deny ITC to the recipient in genuine transactions.

15. Whether use of similar packaging elements amounts to use of "brand name" for denying exemption under Notification No. 2/2017-CT (Rate)?

Narasus Saarathy Enterprises Pvt. Ltd. v. Additional Commissioner of GST & Central Excise – W.P. No. 6069 of 2025 [Madras High Court]

Decision: No.

The petitioner was engaged in manufacture of wheat products such as atta, maida, sooji, etc. It paid GST on goods sold under a registered brand but claimed exemption for goods supplied in unit containers without enforceable brand rights. The petitioner had also filed an affidavit relinquishing actionable claim over the brand name as per the exemption notification. The Department alleged that similarities in packaging (design, colour scheme, farmer graphics, abbreviations, etc.) constituted brand usage and issued a show cause notice under Section 74 for FY 2017-22 demanding Rs. 2.6 crores.

The Hon'ble Madras High Court allowed the petition and quashed the demand. It held: (i) similar packaging features do not automatically amount to use of a "brand name"; (ii) the decisive test is the existence of an enforceable right or actionable claim over the brand name; (iii) once the assessee has relinquished brand rights by affidavit, exemption cannot be denied; (iv) mandatory declarations under FSSAI and Legal Metrology laws (including manufacturer name) cannot be treated as branding; (v) mere use of design, colour scheme, or generic elements does not establish a trade connection or brand ownership; (vi) invocation of extended limitation under Section 74 is unsustainable where transactions are disclosed in returns — at best, proceedings may fall under Section 73.

CONSTITUTIONAL VALIDITY

16. Whether capital gains arising from transfer of shares of a foreign company deriving substantial value from Indian assets are taxable in India?

The Authority for Advance Rulings (Income Tax) & Ors. v. Tiger Global International II Holdings & Ors. – Civil Appeal No. 262 of 2026 – [Supreme Court of India]

Decision: No.

The respondents, Mauritius-based entities, held shares in Flipkart Singapore and transferred the same to a Luxembourg entity as part of a global transaction. The Revenue denied DTAA benefits alleging lack of commercial substance, treaty shopping, and tax avoidance, and the AAR rejected the applications under Section 245R(2). The High Court set aside the AAR's order and granted treaty benefits. Hence; appeal came to be filed.

The Supreme Court dismissed the appeals and upheld the High Court's decision. It held: (i) the AAR erred in rejecting the applications at the threshold under Section 245R(2) on a prima facie view of tax avoidance without adjudicating the issue on merits; (ii) Tax Residency Certificate (TRC) issued by Mauritian authorities constitutes sufficient evidence of residence and beneficial ownership for claiming DTAA benefits, unless rebutted by cogent material; (iii) mere allegation of treaty shopping or use of a holding structure is insufficient to deny treaty benefits in absence of proof of sham or lack of commercial substance; (iv) the principle of "substance over form" cannot be invoked to disregard a genuine structure without demonstrating that it is a colourable device for tax evasion; (v) gains arising from transfer of shares acquired prior to 01.04.2017 are protected under the grandfathering provisions of Article 13(3A) of the India-Mauritius DTAA; (vi) CBDT Circular Nos. 682 and 789 are binding and clarify that capital gains arising to a Mauritius resident are taxable only in Mauritius, subject to treaty conditions; (vii) indirect transfer provisions under Section 9(1)(i) do not override treaty benefits where the DTAA allocates taxing rights to the other contracting state; (viii) the "look at" test as laid down in Vodafone must be applied, requiring examination of the transaction holistically rather than by dissecting its components; (ix) GAAR provisions, though applicable prospectively, cannot be invoked in absence of a clear finding of impermissible avoidance arrangement.

17. Whether unrealized gains arising from mark-to-market valuation of forward contracts are taxable as income?

Principal Commissioner of Income-tax v. Kalyan Jewelers India Ltd. – [Kerala High Court]

Decision: No.

The assessee was engaged in business involving hedging through forward commodity derivative contracts and, in the course of its accounts, recognised gains on a mark-to-market basis in respect of such contracts. During assessment, the Assessing Officer treated the said unrealised gains as taxable income and made additions, which came to be upheld in appellate proceedings. Aggrieved the assessee preferred an appeal before the Tribunal, which allowed the appeal. Hence; appeal came to be filed before the High Court by the Revenue.

The Kerala High Court dismissed the appeal. It held: (i) gains arising from mark-to-market valuation of forward contracts are inherently fluctuating and crystallize only upon maturity or settlement of the contract; (ii) unrealised or notional gains do not constitute "real income" and cannot be subjected to tax; (iii) mere accounting entries recognizing such gains in the books do not determine taxability under the Income-tax Act; (iv) the doctrine of real income governs taxation, and income must accrue in a real sense and not merely hypothetically; (v) anticipated profits cannot be taxed, even if anticipated losses may be recognized on prudential principles; (vi) reliance was placed on judicial precedents recognizing that only real and accrued income can be brought to tax;.

18. Whether shares received pursuant to amalgamation, held as stock-in-trade, give rise to taxable business income under Section 28 of the Income-tax Act, 1961?

Jindal Equipment Leasing and Consultancy Services Ltd. v. Commissioner of Income-tax – Civil Appeal Nos. 152-155 of 2026 – [Supreme Court of India]

Decision: Yes.

The assessee held shares of a company as stock-in-trade. Pursuant to a scheme of amalgamation sanctioned by the High Courts of Andhra Pradesh and Punjab & Haryana, the shares held by the assessees in the amalgamating company stood extinguished and were replaced by shares of the amalgamated company. In the relevant assessment year, the assessees claimed that no taxable income arose on such allotment of shares, contending that the transaction did not constitute a "transfer" in terms of Section 47(vii) of the Income-tax Act, 1961. The Assessing Officer rejected the claim and brought the value of shares to tax as business income, which came to be upheld by the Commissioner. The Tribunal, however, allowed the appeals of the assessees. Aggrieved thereby, the Revenue preferred appeals before the High Court, which reversed the Tribunal's findings and held that the shares were held as stock-in-trade and the gains were taxable as business income. Hence; appeals came to be filed before the Supreme Court.

The Supreme Court dismissed the appeals. It held: (i) Section 47(vii) exempts transfers in amalgamation only in the context of capital assets, and does not apply where shares are held as stock-in-trade; (ii) shares held as stock-in-trade fall within the ambit of Section 28, and profits arising therefrom are chargeable as business income; (iii) amalgamation results in extinguishment of shares of the amalgamating company and substitution by shares of the amalgamated company, but such substitution, in case of stock-in-trade, can give rise to taxable business income depending on commercial realization; (iv) the test of "real income" and "commercial realisability" is crucial to determine whether income has accrued; (v) mere allotment of shares may not always result in immediate taxation; however, where the shares received are capable of valuation and realisation, taxability can arise; (vi) the concept of "transfer" under Section 2(47) is not determinative for taxation under Section 28, which is wider in scope; (vii) business income can arise even in absence of an actual sale, if there is real accrual or receipt of income in commercial terms; (viii) the distinction between capital assets and stock-in-trade is fundamental, and tax treatment differs accordingly; (ix) the Tribunal erred in treating the transaction as non-taxable merely on the basis of exemption under Section 47(vii).

19. Whether a contractual clause making the decision of one party final and excluding arbitration/court jurisdiction is valid, especially when liability is disputed?

ABS Marine Services v. The Andaman and Nicobar Administration – Civil Appeal Nos. 3658-3659 of 2022 – [Supreme Court of India]

Decision: No.

The appellant entered into a manning agreement with the respondent for providing crew on vessels. During the contract period, a vessel ran aground causing damage. The respondent imposed penalty and recovered Rs. 2.87 crores from pending dues by invoking Clause 3.20, which provided that the administration's decision on default would be final and not challengeable in any court and no arbitration would lie. The dispute was referred to arbitration and the arbitrator allowed the claim of the appellant. The High Court set aside the award holding that the dispute was an "excepted matter" and beyond arbitral jurisdiction. Hence; appeal came to be filed.

The Supreme Court held that: (i)a contractual stipulation cannot be construed so as to permit a party to adjudicate upon its own cause, as the same would be contrary to the fundamental principles of rule of law; (ii) Clause 3.20, on a proper construction, is confined to situations where liability is admitted and only the quantification of damages is in issue; (iii) where the question of liability, including allegations of wilful act, omission or negligence, is disputed, such dispute necessarily requires adjudication by an independent forum, namely an arbitral tribunal or a court of law; (iv) Clause 3.22, being couched in wide terms, encompasses all disputes arising out of the agreement, including disputes relating to liability; (v) any interpretation which has the effect of completely excluding recourse to arbitration or courts would be void, being contrary to Section 28 of the Indian Contract Act, 1872 and opposed to public policy; (vi) a construction resulting in denial of any legal remedy is impermissible, in light of the settled maxim ubi jus ibi remedium; (vii) the concept of "excepted matters" cannot be expansively interpreted so as to exclude adjudication of disputes relating to liability; (viii) the High Court exceeded its jurisdiction under Section 37 of the Arbitration and Conciliation Act, 1996 by reappreciating and reinterpreting the contractual clauses and erroneously concluding that the arbitral tribunal lacked jurisdiction.

20. Whether an arbitral award can be set aside on the ground of improper constitution of the arbitral tribunal when the arbitration clause provides an alternative mechanism for appointment of the presiding arbitrator?

Municipal Corporation of Greater Mumbai v. M/s R.V. Anderson Associates Ltd. –SLP (C) No. 23846-47 of 2025 – [Supreme Court of India]

Decision: No.

The appellant invited bids for consultancy services relating to sewage operations. Disputes arose regarding payment of dues and arbitration was invoked. As per the agreement, each party appointed a nominee arbitrator, and the presiding arbitrator was to be appointed jointly; failing which, parties could approach the Secretary General of ICSID. The co-arbitrators appointed the presiding arbitrator after expiry of 30 days. The appellant challenged the constitution of the tribunal on the ground that post expiry of 30 days, only ICSID could appoint the presiding arbitrator. The arbitral tribunal rejected the objection and passed an award. The challenge under Sections 34 and 37 was dismissed by the High Court. Hence; appeal came to be filed.

The Supreme Court dismissed the appeal. It held:

(i) the arbitration clause is enabling in nature and does not extinguish the power of co-arbitrators to appoint the presiding arbitrator after expiry of 30 days; (ii) recourse to ICSID is only an additional mechanism available to parties in case of impasse and is not a mandatory or exclusive mode of appointment; (iii) absence of any stipulation divesting the co-arbitrators of their power after the stipulated period indicates that such power continues; (iv) interpretation adopted by the arbitral tribunal, being a plausible view, does not warrant interference under Sections 34 or 37 of the Arbitration and Conciliation Act, 1996; (v) the scope of judicial interference in arbitral awards is limited and courts cannot substitute their own interpretation merely because another view is possible; (vi) conduct of the appellant demonstrated acquiescence, as no objection was raised at the relevant time despite knowledge of the appointment process; (vii) although a jurisdictional objection under Section 16 was raised within time, the prior conduct of the appellant is a relevant factor in construing the contractual intent; (viii) a party cannot be permitted to participate in the arbitral process without protest and subsequently challenge the constitution of the tribunal.

21. Whether counter claim not filed during CIRP and not forming part of the resolution plan can be pursued in arbitration after approval of the resolution plan?

Ujaas Energy Ltd. v. West Bengal Power Development Corporation Ltd. – SLP (Civil) No. 29651 of 2024 [Supreme Court of India]

Decision: Yes.

The appellant underwent Corporate Insolvency Resolution Process (CIRP) and a resolution plan was approved. During arbitration proceedings, the respondent raised a counterclaim which had not been filed before the Resolution Professional nor included in the resolution plan. The arbitral tribunal rejected the counterclaim. The Single Judge upheld the rejection; however, the Division Bench permitted continuation of arbitration on the counterclaim issue. Hence; appeal came to be filed.

The Supreme Court partly allowed the appeal. It held:

(i) upon approval of the resolution plan under Section 31 of the Insolvency and Bankruptcy Code, 2016, all claims not forming part of the plan stand extinguished and cannot be pursued independently; (ii) a counterclaim not lodged during CIRP and not included in the resolution plan cannot be maintained as an independent claim in arbitration; (iii) the “clean slate” principle ensures that the successful resolution applicant is not burdened with past liabilities not accounted for in the plan; (iv) however, the resolution plan must be strictly construed to ascertain whether it bars all forms of defence including set-off; (v) in absence of an express bar in the resolution plan, a limited plea of set-off can be raised as a defence in arbitration; (vi) such set-off is permissible only to the extent of defending against the claim of the corporate debtor and not for seeking any affirmative relief; (vii) the respondent cannot recover any surplus amount on the basis of such set-off, nor can it enforce the extinguished claim independently; (viii) the conduct of parties and timing of the counterclaim are relevant factors, but do not override the statutory effect of the approved resolution plan.

22. Whether earning interest on deposits constitutes a "commercial purpose"?

Sant Rohidas Leather Industries & Charmakar Development Corporation Ltd. v. Vijaya Bank – Civil Appeal No. 4841 of 2023 [Supreme Court]

Decision: No.

The appellant had placed surplus funds in a fixed deposit with the bank. A dispute arose regarding adjustment of the deposit against an alleged overdraft facility. The consumer complaint was dismissed on the ground that the transaction was for a "commercial purpose" since interest was earned. The matter reached the Supreme Court.

The Hon'ble Supreme Court held: (i) merely earning interest on a deposit does not automatically make the transaction a "commercial purpose"; (ii) what is relevant is the dominant intention / purpose test — whether the transaction has a direct nexus with profit generation; (iii) parking of surplus funds in a bank for safety, liquidity, or statutory compliance is not per se commercial; (iv) however, if deposits are used to leverage credit facilities / overdraft for business, then it may constitute a commercial purpose; (v) distinction must be drawn between passive treasury activity and active profit-oriented deployment of funds.

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