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Examining the Validity of Unilateral Option Clauses in India: A Brief Overview

Nishanth Vasanth, Rishabh Raheja (NALSAR University of Law) · Friday, October 20th, 2017 · Young ICCA

The decision of the Singapore Court of Appeal in *Wilson Taylor Asia Pacific Pte Ltd v. Dyna-Jet Pte Ltd* ([2017] SGCA 32) added another chapter to the debate on the validity of unilateral option clauses (or 'sole option clauses') in contracts. The Singapore Court of Appeal reaffirmed the Singapore High Court's decision to uphold the validity of a unilateral option clause, thus adding to the varying decisions on this question across jurisdictions since 2010. During this period, courts in the UK, Italy and Spain have upheld such clauses as valid, while those in France, Russia, Bulgaria, Dubai and Poland have struck down such clauses. In this context, the authors consider the challenges faced by unilateral option clauses in various Indian courts.

What are unilateral option clauses and why are they controversial?

A unilateral option clause is a dispute resolution clause which confers an exclusive right to elect a specific dispute resolution method, i.e., it provides the option of resorting to arbitration or litigation; however, this option is conferred upon only one party. Courts have had to consider whether they should uphold such clauses in the interest of party autonomy or intervene due to public policy considerations.

In the Clifford Chance Unilateral Option Clauses – 2017 Survey, it is noted that courts in the UK and several other Common Law jurisdictions have upheld unilateral option clauses as they represent the bargain of the parties, irrespective of the advantage the clause confers on one side. On the other hand, some jurisdictions such as Russia and Poland have found such clauses to violate the parties' equality of arms and procedural rights, reading these as 'bilateral' and not 'unilateral' option clauses. There have been other jurisdictions such as Bulgaria, China, and some US State courts, where these clauses have been wholly invalidated on public policy grounds of 'morality', 'good faith', 'fairness' and 'unconscionability'. Some other grounds include the absence of a potestative condition, legal uncertainty, and lack of consideration.

Position in India:

Decisions on the validity of unilateral option clauses have been few and far between in India, with the only notable decisions being rendered by the Delhi and Madras High Courts (HC):

1. In *Bhartia Cutler Hammer v. AVN Tubes* (1995 (33) DRJ 672), the Delhi HC held that a party could not have an exclusive right to initiate arbitration as the Indian Arbitration and Conciliation Act, 1996, presupposed that there must be a mutual arbitration agreement between the parties, and an opportunity for bilateral invocation. Notwithstanding parties' express consent to such a clause, it would not be deemed a valid arbitration agreement.

2. In *Emmsons International Ltd. v. Metal Distributors* (2005 (80) DRJ 256), the Delhi HC arrived at the same conclusion as in Bhartia Cutler, based on different reasoning. The court observed that unilateral option clauses were void as they restrained one party's recourse to legal proceedings, in contravention of Section 28 of the Indian Contract Act, 1872. The court noted additionally (without substantiation) that a unilateral clause would be void for being contrary to the public policy of India.

3. In *Lucent Technology v. ICICI Bank* (2009 SCC OnLine Del 3213), the Delhi HC again held a unilateral option clause to be invalid. The court relied on both Bhartia Cutler and Emmsons International and invoked Section 28 of the Indian Contract Act, 1872, implying that the party's right to recourse through legal proceedings had been infringed.

4. The Madras HC decided to go against the tide in *Castrol India Ltd. v. Apex Tooling Solutions* ((2015) 1 LW 961 (DB)) and did not dispute the general principle that arbitration clauses need not necessarily have mutuality. However, on the facts, the court held that the party seeking to invoke arbitration through its sole option could not do so, having failed to object, and having even participated during the preliminary stages of litigation.

5. In a slight deviation from its previous decisions, the Delhi HC in *Fuerst Day Lawson Ltd. v. Jindal Exports Ltd.* (MANU/DE/3204/2009), *upheld* the validity of a unilateral option clause. However, the impact of this decision on the position of the court is unclear, as the clause was upheld not under Indian law, but under applicable English law.

From the above decisions it would appear that the three grounds upon which unilateral clauses have been successfully challenged before the courts in India are – *lack of mutuality, public policy, and restraint of a party's right to legal proceedings*. However, the Madras HC's decision to uphold these clauses calls for closer scrutiny of these grounds. Should the Supreme Court of India examine the validity of unilateral option clauses under Indian law, some of the counter-grounds it could consider include:

1. The absence of an explicit requirement for mutuality in the Indian Arbitration and Conciliation Act, 1996. Section 7 of the Act lists out the requirements for a valid arbitration agreement and does not include the mutuality of invocation of the arbitration clause among these. At the most, the stipulation under Section 7 for there

to be an 'agreement by the parties' requires mutuality of *consent*, and not mutuality of *invocation or consideration*. While the Madras HC relied on this lack of an explicit requirement for mutuality to uphold unilateral option clauses, the Delhi HC invalidated unilateral option clauses even when the presence of mutual consent was proven. The Delhi HC's insistence on mutuality of consideration appears to stem from Section 25 of the Indian Contract Act, which invalidates agreements lacking consideration. This raises interesting questions of separability of the arbitration agreement— whether the consideration for the main agreement is sufficient for and coextensive with the arbitration agreement, or whether the arbitration agreement requires separate consideration through mutual rights of invocation? Adopting the latter approach could lead to an intriguing situation where the mutuality of consideration and invocation takes priority over the mutuality of consent to such a clause. The latter approach would also not account for a situation where the consideration for the unilateral option clause is *present in the main agreement*, through a substantive concession or benefit provided to the party without the unilateral option. These complex questions of Indian contract and arbitration law merit the careful consideration of the Supreme Court.

2. The 2015 Amendment to the Indian Arbitration and Conciliation Act, 1996, and its pro-arbitration tenor could also have an impact on the Supreme Court's approach to unilateral option clauses. Specifically, the scope of 'public policy' as a ground for challenge of awards has been defined explicitly and enumerated exhaustively under the 2015 Amendment. The Delhi HC's decisions invalidating unilateral option clauses on grounds of 'public policy' were pronounced prior to the Amendment. Thus, a re-evaluation of whether such clauses violate the recently revised ambit of public policy will be necessary. Moreover, the increasing commercial acceptance of unilateral clauses could also be a consideration under a public policy challenge in this new regime.

3. Section 28 of the Indian Contract Act, 1872, invalidates agreements in restraint of legal proceedings. The provision, however is attracted only when there is an absolute and not a partial restraint on legal proceedings. In this light, the mere provision of an option to one party does not necessarily and absolutely undermine the other party's right to approach the default forum for dispute settlement. Thus, Indian courts may have to deal with this question on a case-by-case and clause-by-clause basis, preventing misuse, delay, and equivocation from the party with the unilateral option of forum.

4. In addition to determining whether the clause in question is an absolute restraint in the terms of Section 28, another question demanding scrutiny is the stated exception to Section 28. Exception 1 to Section 28 permits an agreement to refer to arbitration – it would not be considered invalid for restraint of a party's right to pursue legal proceedings. None of the Delhi HC decisions cited above considered either the requirement for an absolute restraint, or this exception to Section 28, in invalidating unilateral option clauses. This thus calls for clarification by the Supreme Court.

Given the above considerations, the authors are optimistic that unilateral option clauses will be held valid under Indian law. The fact that the Delhi HC — which had consistently invalidated these clauses — has taken a step towards accepting these

clauses in *Fuerst Day Lawson* is indicative of a positive shift of stance. Moreover, the Delhi HC's recent reluctance to allow public policy challenges to awards in two of its decisions following the Amendment weakens the likelihood of a successful public policy challenge to unilateral option clauses. Despite these positive developments, it would be prudent for parties to avoid the incorporation of unilateral option clauses when there is a possibility that Indian courts may be involved. In the meantime, one can only hope that the Supreme Court thoroughly tests the above three grounds for challenge and arrives at a position best representative of Indian law, and most beneficial to parties.

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