

AWARDS OF INTEREST IN ARBITRATION

by

Sundra Rajoo

Chartered Arbitrator, Architect and Town Planner

B Sc (HBP) Hons (USM)

LLB Hons (London)

Grad Dip in Architecture (TCAE)

Grad Dip in Urban and Regional Planning (TSIT)

M Sc in Construction Law and Arbitration (With Merit)(LMU)

M Phil in Law (Manchester)

APAM, APPM, FMIArb, FCIArb, FSIArb, FICA, MAE, ARAIA

Synopsis

This article deals with the entitlement of a successful claimant in arbitration proceedings (including a respondent who succeeds in a counterclaim) to have included in the award an amount in respect of interest on the principle sum awarded in his favour; and with the accumulation of interest on the award itself from the date of the award until the date of payment. Generally, interest from the date of the award until the date of payment is purely statutory whereas the arbitrator's power to award interest generally is based on contract or claim by way of proof of special damages.

Introduction

The House of Lords in *London, Chaltam & Dover Railway Co v South Eastern Railway Co*¹ held that 'at common law, in the absence of any agreement or statutory provisions for the payment of interest, a court has no power to award interest, simple or compound, by way of damages for the detention (that is, the late payment) of a debt'. Based on this ratio decidendi, there is no right of action to recover interest, as damages or otherwise, upon any monies (whether debts or damages) for any period in which such monies are wrongfully withheld.

While the House of Lords in *President of India v La Pintada Cia Navigacion SA*² recognized the injustice inherent in the rule, it nevertheless affirmed that the rule was too well settled to be departed from other than by legislation. The court explained that the ratio applied only to claims for interest by way of general damages, and did not extend to claims for special damages. The rule in *London, Chaltam & Dover Railway Co v South Eastern Railway Co*³ has, therefore, survived. It is, however, subject to a number of exceptions.

On the other hand, the general rule at common law established in *Page v Newman*⁴ was that an arbitrator had no inherent jurisdiction to award interest, nor had he any such jurisdiction arising from statute. He derived such jurisdiction from an implied term by a submission to arbitration that the arbitrator should have power to decide the issues on the subject of the reference according to the law which would be applied in the courts.⁵

Statutory provision as in s 21

Section 21 of the Arbitration Act 1952 (Revised 1972) contains the statutory basis for the power of an arbitrator to award interest under an arbitration award:

A sum directed to be paid by an award shall, unless the award otherwise directs, carry interest as from the date of the award at the same rate as a judgment debt.

Order 42 r 12 of the Rules of the High Court 1980 provides:

Every judgment debt shall carry interest at the rate of 8 per centum per annum or at such other rate not exceeding the rate aforesaid as the court directs (unless the rate has been otherwise agreed upon between the parties), such interest to be calculated from the date of judgment until the judgment is satisfied.

There is a similar provision in the Subordinate Court Rules 1980.⁶

The exercise of the arbitrator's discretion

While the arbitrator is given a discretion under s 21 of the Arbitration Act 1952 (revised 1972) whether to award interest, he ought to normally award it. Mustill MJ and Boyd SC in *The Law and Practice of Commercial Arbitration in England* (2nd Ed, 1989) at p 394 state that if the arbitrator decides not to award interest, he should explain his reasons for doing so in his award. His power to award interest is discretionary, and he has to exercise his discretion judicially.

In the words of Oliver LJ in *Techno-Impex v Gebr Van Weelde Scheepvaartkantoor BV*,⁷ the exercise of the arbitrator's discretion involves,

... what is regarded as a basic implied term that the arbitrator shall decide in accordance with the rights of the parties under English law ... the arbitrator's power to award interest ... is a matter of substantive law and not merely a rule of practice which the arbitrator can disregard at his discretion.

Interest can only be awarded if the arbitrator awards a principal sum.⁸ The entitlement to interest under s 21 is not dependent on proof of loss. It may be awarded, for example, on damages for the loss of goods even where there is no evidence of loss of use or loss of profits.⁹

Rate of interest applicable

When the arbitrator awards interest, he must do so at the rate applicable to a judgment debt. He has no power to alter the rate. In referring to the equivalent section of the English Arbitration Act 1950, the House of Lords in *Timber Shipping Co SA v London & Overseas Freighters Ltd*¹⁰ held that an arbitrator had the discretion only to decide whether his award should or should not carry interest, but he could not determine the rate at which it should do so. He could only award interest as from the date of the award at the same rate as a judgment debt.

Lord Morris of Borth-y-Gest at p 21 explained his reasoning:

Are the words wide enough not merely to give a discretion to an arbitrator to decide whether the award will carry interest but give him a general discretion to direct that his award should carry interest at whatever rate he chooses to fix? In my view they are not ... The arbitrator has a veto by the exercise of which he may direct that the award will not carry interest at all. Unless he so directs, the award will automatically carry interest at the same rate as a judgment debt ... if a general discretion were being conferred there would have been no necessity to make any reference at all to a judgment debt.

The court in *Rocco Giuseppe & Figli v Tradax Export SA*¹¹ refused to order a change in the rate of interest on an arbitration award. It held that equivalent s 20 of the English Arbitration Act 1950 had specified a mandatory rate of interest which abrogated any surviving power of the court to award otherwise on an arbitration award.

When does interest start to accrue?

Based on the Arbitration Act 1952 (Revised 1972), it would seem that an arbitrator has no power to grant interest effective from a date earlier than that of the award date. Section 21 only provides for interest from the date of the award on any sum that is directed to be paid by the award which is to carry interest at the same rate as a judgment debt. As such, there appears to be a lacuna in the statute as regards the right of a successful party in a reference to arbitration to receive interest in respect of the period before the arbitrator makes his award. This anomaly is detrimental to the construction, shipping and insurance industries using arbitration for the resolution of their disputes.

Section 11 of the Civil Law Act 1956 allows the courts to grant interest on a judgment debt beginning from the date of the cause of action:

In any proceedings tried in any court for the recovery of debt or damages the court may, if it thinks fit, order that there shall be included in the sum for which judgment is given interest at such rate as it thinks fit on the whole or any part of the debt or damages for the whole or any part of the period between the date when the cause of action arose and the date of judgment:

Provided that nothing in this section —

- (a) shall authorize the giving of interest upon interest;
- (b) shall apply in relation to any debt upon which interest is payable as of right whether by virtue of any agreement or otherwise; or
- (c) shall affect the damages recoverable for the dishonour of a bill of exchange.

Mustill MJ and Boyd SC in *The Law and Practice of Commercial Arbitration in England* (1st edn, 1982) at p 345–346 drew an analogy with the powers of the High Court that the arbitrator has implied power to award interest up to the date of award at such rate as he thinks fit on any award ordering the payment of a sum of money. Such power can be exercised provided a prima facie case has been made out on the entitlement to such an award.

Walton A, in *Russell on the Law of Arbitration* (19th edn, 1979) at p 356 speaking of an arbitrator's power to award interest up to the date of the award: 'it was always considered

that he had power to do so, by virtue of his implied authority to follow the ordinary rules of law.’

Lord Wilberforce in *General Tyre & Rubber Co v Firestone Tyre & Rubber Co Ltd*¹² explained the basic principle of why interest is awarded:

Interest is not awarded as punishment against a wrongdoer for withholding payments which should have been made. It is awarded because it is only just that the person who has been deprived of the use of the money due to him should be paid interest on that money for the period during which he was deprived of its enjoyment.

The object of such an award is not penalize the losing party but to compensate the successful party for not having had the benefit of the money between the date when it ought to have been paid and the date of the award or earlier payment.¹³

This approach is consonant with the position taken by Lord Denning in *Panchaud Freres SA v Pagnan and Fratelli*¹⁴ when he remitted the award back for the arbitrators to reconsider interest as they erred on a matter of principle. He explained at p 411 that:

In a commercial transaction, if the plaintiff has been out of his money for a period, the usual order is that the defendant should pay interest for the time for which the sum has been outstanding. No exception should be made except for good reason.

The court in *Lian Hup Manufacturing Co Sdn Bhd v Unitata Bhd*¹⁵ adopted the above position of empowering the arbitrator to award pre-award interest (that is, interest on amounts awarded from the date of the cause of action to the date of the award). Dato’ Zakaria Yatim J (as he then was) held that the arbitrator’s power is derived from the submission to him, which impliedly gave him the power to decide all matters in difference according to the existing law of contract, exercising every right and discretionary remedy given to a court of law. He relied on the case of *Chandris v Isbrandtsen-Moller Co Inc*¹⁶ in which the English Court of Appeal held that independent of statute, the arbitrator had inherent procedural powers derived from the common law analogous to those possessed by a judge when trying an action in the High Court.

His Lordship explained at p 54,

Under s 11 of the Civil Law Act 1956, the court has the discretionary power to award interest for the recovery of any debt or damages. See *Evergrip Prestressing Sdn Bhd v Ken Construction & Trading Sdn Bhd*. In my view, the arbitrator in the present case has the same power as that of the court to award interest at such rate as he thinks fit. Since it was within the discretionary power of the arbitrator to award interest in this case, the court would not interfere with the exercise of his discretionary power.

More recently, Faiza Thamby Chik J in *Raja Lope & Tan Co v Malayan Flour Mills Bhd*¹⁷ followed the above approach when he held that the act of submission to arbitration confers upon the arbitrator the implied power to award interest. The court went on to rule that the arbitrator erred in law when he said that the arbitration clause was not wide enough to confer power to direct pre-award interest to be paid. The award was remitted back to the arbitrator with direction to award interest at 8% on damages from the date

when such payment represented by damages ought to have been made to the date of payment.

Therefore, the arbitrator ought ordinarily to award interest; if he does not do so, he should give his reasons for doing so in his award. It is prima facie misconduct to award a sum of money without awarding interest for delay in payment. Unless the award contains a sufficient explanation for not awarding interest, it will be remitted back to the arbitrator for the question of interest to be reconsidered.¹⁸

It may be viewed that the positions of a judge and an arbitrator are distinguishable and that any analogy to equate the two is misleading. However, in line with commercial reality, the cases of *Lian Hup Manufacturing Co Sdn Bhd v Unitata Bhd*¹⁹ and *Raja Lope & Tan Co v Malayan Flour Mills Bhd*²⁰ reaffirm the long established principle that the powers of arbitrators in this regard (as in others) are co-extensive with, and no wider than, those of the courts.

Whether compound interest is payable

Section 11 of the Civil Law Act 1956 states that nothing in the section shall authorize the giving of interest upon interest (ie compound interest). Section 11, however, goes on to add that it shall not apply in relation to any debt upon which interest is payable as of right by virtue of any agreement or otherwise.

If s 21 of the Arbitration Act 1952 (Revised 1972) were to be read together with O 42 r 12 of the Rules of the High Court 1980 and O 29 r 42 of the Subordinate Court Rules 1980 relating to judgment interest, there is a suggestion that the arbitrator may appear to have statutory power to give compound interest on an arbitration award. This will arise in the situation where the contract in issue contains a term to the effect that either party is entitled to be paid compound interest in respect of any action for the recovery of damages against each other, arising from the breach of contract.

Pawancheek Marican in his article, 'The Arbitrator's Power to Award Interest' [1997] 1 MLJ lxxix at lxxii quotes the view of Professor Vincent Powell-Smith that this may not be the correct position. After examining the cases of *Chandris v Isbrandtsen-Moller Co Inc*,²¹ *London, Chaltam & Dover Railway Co v South Eastern Railway Co*²² and *President of India v La Pintada Cia Navigacion SA*,²³ he concludes that the power to award compound interest in s 11 of the Civil Law Act 1956 is given only to the ordinary courts and not an arbitrator. The arbitrator can only award simple interest.

Interest under contract

Generally the law relating to contractual interest is unaffected by the Arbitration Act 1952 (Revised 1972). Where a contract provides for interest to be paid on any monies outstanding, the interest may be claimed and awarded as a liquidated sum. For example, the CIBD Standard Form of Contract for Building Works (2000 Ed) provide for interest to run if payment by the employer is not made in due time to the contractor: see cl 42.9. Clauses 34.4 (vi) and (vii) of the PAM 1998 Form of Building Contract provide that the

arbitrator is given express powers to award pre-award and post-award interest at whatever rates and whatever rests he considers just.

Under such a circumstance, interest under s 21 of the Act cannot be awarded for a period during which interest on the principal sum is due under a contract term.²⁴

Interest as loss and expense under building contracts and as special damages

The arbitrator is allowed to award interest as 'loss and expense' under building contracts and interest as special damages. The two types of interest are distinct. Interest as 'loss and expense' under building contracts arise as entitlements in contract while interest as special damages arise as entitlements for damages for breach of contract. Both types are considered together because they have each derived support from the other in the course of their development, and raise similar considerations.

It was decisively held in the English case of *FG Minter Ltd v Welsh Health Technical Services Organisation*²⁵ that, provided that the requisite notices under the contract have been given, a contractor can recover as 'direct loss and/or expense' under cl 24(1) of the JCT Form 1963 (similar to cl 24(1) of the PAM/ISM 1969 Form of Building Contract) the interest cost of financing the execution of variations and late instructions issued by the architect under the contract. The loss of interest was a direct result of the defendant's breach of contract and was recoverable. The term 'direct loss and/or expense' was treated as having the same meaning as 'damage which flows naturally from the breach'. Therefore, the claim for finance charges can be pursued based on s 74 of the Contracts Act 1950 which is essentially similar to the English common law rule on damages as laid down by *Hadley v Baxendale*.²⁶

The decision in *FG Minter* turned essentially on the construction of the contract. The real question was whether or not the architect was required to take finance costs into account in ascertaining adjustments to the contract sum. The *FG Minter* decision is not a true exception to the rule in *London, Chatham & Dover Railway Co*. It is an illustration of the principle that parties are free to contract in whatever terms they choose, and the courts will enforce their bargain.

The *FG Minter* decision was further applied in *Rees & Kirby v Swansea City Council*²⁷ where the facts were similar but more complicated. Robert Goff LJ explained that financing charges could be awarded on the basis of compound interest instead of simple interest if it could be shown that the actual costs to the contractor was interest on his overdraft which could be compounded. He explained at p 23:

Now here, it seems to me, we must adopt a realistic approach. We must bear in mind, moreover, that what we are considering here is a debt due under a contract; this is not a claim to interest under the Law Reform Act, but a claim in respect of loss or expense in which a contractor has been involved by reason of certain specific events. The respondents, like (I imagine) most building contractors, operated over the relevant period on the basis of a substantial overdraft at their bank, and their claim in respect of financing charges consists of a claim in respect of interest paid by them to the bank on the relevant amount during that period. It is notorious that banks do themselves, when calculating interest on overdrafts, operate on the basis of periodic rests; on the basis of the principle stated by the Court of Appeal in *Minter's* case, which we here have to apply,

I for my part can see no reason why that fact should not be taken into account when calculating the respondent's claim for loss or expense in the present case.

The court then left it to the parties to agree on the rates at which interest was to be calculated but directed that regard be had to the rates charged by the contractor's bank upon its overdraft, and to the periodic rests applicable to the account. The contractor was contending for quarterly rests, which the court did not rule out.

A claim for finance charges can also be supported by the case of *Woon Hoe Kan & Sons Sdn Bhd v Bandar Raya Development Bhd*.²⁸ The main issue in this case was what rate of interest should apply where there was an agreement to pay interest. Harun J (as he then was) held that interest was, in any event, payable under s 74 of the Contracts Act 1950 if there was a breach of contract. In particular, the court referred to illustration (n) to s 74 of the Contracts Act 1950 which is as follows:

A contracts to pay a sum of money to B on a day specified. A does not pay the money on that day. B, in consequence of not receiving the money on that day, is unable to pay his debts and is totally ruined. A is not liable to make good to B anything except the principal sum he contracted to pay, together with interest up to the day of payment.

The defendant in *Wadsworth v Lydall*²⁹ wrongfully delayed payment of a sum of money to the plaintiff. In the circumstances, the court held that it was foreseeable that the plaintiff would be forced in consequence to borrow money in order to complete a transaction. The actual interest charges incurred by the plaintiff on his borrowing were recoverable from the defendant as special damages. The rule in *London, Chaltam & Dover Railway Co* was distinguished on the ground that it precluded only the recovery of interest for late payment as general, not special, damages. Lord Brandon in *President of India v La Pintada Cia Navigacion SA*³⁰ approved the decision in *Wadsworth v Lydall* that the rule applied only to claims for interest by way of general damages, and did not extend to claims for special damages.

There is a distinction between general damages and special damages. Special damages must be specifically pleaded and proved. General damages need not be. Neill LJ in *President of India v Lips Maritime Corporation*³¹ considered the distinction more fully in the following words:

In the case of a claim for damages for the late payment of money the court will not determine in favour of the plaintiff (if the) damages flow from such delay 'naturally, that is, according to the usual course of things'. But a plaintiff will be able to recover damages in respect of a special loss if it is proved that the parties had knowledge of facts or circumstances from which it was reasonable to infer that delay in payment would lead to that loss.

So, if the claimant pleads and can prove that he has suffered special damages as a result of the respondent's failure to perform his obligation under a contract, such damages can be claimed provided it is not too remote, as covered under s 74(1) of the Malaysian Contracts Act 1950. It is open to the claimant to expressly plead his claim for interest as special damages and go on to prove it. For example, the contractor in *Department of Environment for Northern Ireland v Farrans (Construction) Ltd*³² was awarded special

damages interest paid on borrowings he was obliged to make in consequence of the employer's wrongful deduction from interim payments of liquidated damages. The deductions were later released to the contractor before the proceedings were commenced. The editors of the Building Law Reports in their commentary at p 6–7, have doubts on the correctness of this decision:

Such losses are ones which are difficult to estimate accurately and for that reason might also be regarded as falling within the category of 'general damages' rather than 'special damages' ... On that basis they would appear to be caught by the common law rule against the recovery of interest as damages for breach of contract to pay a sum of money. Interest would only be awarded by a court or arbitrator if and when there was a judgment or award for the principal sum and not where the principal sum had already been paid to the plaintiff or claimant.

Showing interest in the award

Where interest is awarded, the award should expressly state the interest awarded under that head. If a successful party had claimed statutory interest but the arbitrator had, for some reason, taken the unusual step of exercising his discretion not to award interest, he should state his reasons. Failure to do so may lead to a charge of misconduct on the arbitrator's part.

If in making his award, an arbitrator overlooks to award interest, the error may be pointed out to him. He may correct the award under the 'slip rule' as in s 18 of the Arbitration Act 1952 (Revised 1972).³³

Conclusion

The way to enforce an arbitration award is to enter judgment in terms of the award, with leave of the High Court under s 27 of the Arbitration Act 1952 (Revised 1972), whereupon it may be enforced as a judgment of the court. The defendant in *Coastal States Trading (UK) Ltd v Mebro Mineraloel-Handelsgesellschaft GmbH*³⁴ had eventually paid the amount of the award, but not the interest upon it which had accumulated prior to payment.

The court held that in granting leave to enter judgment in terms of the award, it could award interest upon the interest which had accumulated up to the date of payment of the principle sum awarded by the arbitrator. The defendant objected on the basis that it amounted to interest upon interest. The court rejected the argument. It held that the accumulated interest was treated as a debt, irrespective of how it arose.

1 [1893] AC 104.

2 [1985] 1 AC 104.

3 [1983] AC 104.

4 (1829) 9 B&C 378.

5 See *Chandris v Isbrandtsen-Moller Co Inc* [1951] 1 KB 240; *Techno-Implex v Gebr Van Weelde Scheepvaartkantoor BV* [1981] 2 WLR 821; *President of India v La Pintada Cia Navigacion SA* [1985] 1 AC 104.

6 See O 29 r 12.

7 [1981] 2 All ER 669.

8 See *Allison v Kiteley* [1995] CILL 1016.

9 See *Metal Box Ltd v Curry Ltd* [1988] 1 All ER 341.
10 [1972] AC 1.
11 [1984] 1 WLR 742.
12 [1975] 2 All ER 173 at 192.
13 See also *Kemp v Tolland* [1956] 2 Lloyd's Rep 681 at 691.
14 [1974] 1 Lloyd's Rep 394.
15 [1994] 2 MLJ 51.
16 [1951] 1 KB 240.
17 [2000] 6 MLJ 228 at 239.
18 See *Raja Lope & Tan Co v Malayan Flour Mills Bhd* [2000] 6 MLJ 228; *Along Construction (S) Pte Ltd v United Boulevard Pte Ltd* [1995] 1 SLR 548; *Government Insurance Office (NSW) v Atkinson-Leighton Joint Venture*(1980) 55 ALJR 212; *PJ Van Der Zijden Wildhandel NV v Tucker and Corss Ltd* [1976] 1 Lloyd's Rep 341; *Thos P Gonzales Corp v FR Waring (International) (Pty) Ltd* [1978] 1 Lloyd's Rep 494 at 505; *Warinco AG v Andre & Cie SA* [1979] 2 Lloyd's Rep 298.
19 [1994] 2 MLJ 51.
20 [2000] 6 MLJ 228.
21 [1951] 1 KB 240.
22 [1893] AC 104.
23 [1985] 1 AC 104.
24 See *Secretary of State for Transport v Birse-Farr* (1993) 9 Const LJ 213; *Royal Borough of Kingston-upon-Thames v Amec Civil Engineering Ltd* (1994) 10 Const LJ 225.
25 (1980) 13 BLR 1.
26 (1854) 9 Ex 341.
27 (1985) 30 BLR 1.
28 [1973] 1 MLJ 60.
29 [1981] 2 All ER 401.
30 [1985] 1 AC 104.
31 [1987] 1 Lloyd's Rep 131.
32 (1981) 19 BLR 8.
33 See *Pancommerce SA v Veecheema BV* [1983] 2 Lloyd's Rep 304.
34 [1986] 1 Lloyd's Rep 465.