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CONTRACTUAL AND STATUTORY LIMITS OF INTEREST IN ARBITRATION

The Supreme Court (“**SC**”) in *Larsen & Toubro* case¹ examined whether an arbitral tribunal can make pre-award/*pendente lite* interest despite an express contractual bar. Also, whether post-award interest is governed by the contract or Section 31(7) of the Arbitration and Conciliation Act, 1996 (“**Act**”).

Brief Facts.

Union of India and North Central Railway (“**Appellants**”) entered a turnkey contract with Larsen & Toubro Limited (“**L&T**”) for an engineering project. It was significantly delayed, leading to disputes regarding payments and claims. L&T invoked arbitration under Clause 64 of the General Conditions of Contract (“**GCC**”), and the Arbitral Tribunal (“**AT**”) awarded L&T the full claim along with conditional post-award interest at 12% per annum. The Appellants challenged the award, which was dismissed by the Commercial Court (“**CC**”), and thereafter before the High Court (“**HC**”), which also upheld the award. Aggrieved, the Appellants approached the SC.

Appellants’ Contentions.

- Clauses 16(3) and 64(5) of the GCC impose an absolute prohibition on interest, including on “*amounts payable to the contractor under the contract.*”²
- The AT could not award interest in any form, including by labelling it as “*compensation.*”³
- Section 31(7)(a)⁴ subordinates the arbitrator’s power to the contract, and once interest is barred, it cannot be granted.⁵

L&T’s Contentions.

- Clause 16(3) applies only to earnest money and security deposits and must be read narrowly using the principle of *ejusdem generis*.⁶

¹ *Union of India & Ors v. Larsen & Toubro Limited* | 2026 LiveLaw (SC) 214 | Click [here](#) to read the full Judgement.

² Paragraph No. 15 and 18 of the Judgement.

³ Paragraph No. 17 of the Judgement.

⁴ Section 31(7)(a) of the Act allows the Arbitral Tribunal to award reasonable pre-award interest, unless parties agree otherwise.

⁵ Paragraph No. 20 and 21 of the Judgement.

⁶ Paragraph No. 24 of the Judgement.

- Clause 64(5) bars interest only till the date of award and does not affect admitted claims or post-award interest.⁷
- Post-award interest is statutorily mandated under Section 31(7)(b) and cannot be excluded by contract.⁸

Judgement & Reasoning:

The SC:

- Emphasized that under Section 31(7)(a), the arbitrator’s power to award interest is subject to party’s agreement, and where the contract bars interest, such bar is binding.⁹
- Rejected the *ejusdem generis* argument, holding that the expression “amounts payable to the contractor under the contract” is “*independent, distinct and of wide amplitude*” and cannot be read narrowly.¹⁰
- Relied on *Bright Power Projects case*¹¹ and *Manraj Enterprises case*¹² to reiterate that where parties have agreed that no interest shall be payable, the arbitrator “*has no power to award interest, contrary to the terms of the agreement,*” even if termed as compensation.
- Affirmed the principle in *Railway Administration case*¹³ that contractual bars on interest bind the arbitral tribunal, and interest cannot be awarded for the pre-award period.
- Distinguished between earlier decisions such as *Ambica Construction case*¹⁴ and *Raveechee & Co. case*¹⁵, noting that they were rendered under the Arbitration Act, 1940 and are not applicable to the regime under the present Act.
- Found that the AT committed a serious error in awarding pre-award/*pendente lite* interest despite the contractual prohibition and that the CC and HC erred in upholding such interest, even within the limited scope of Sections 34 and 37 of the Act. ¹⁶
- Distinguished pre-award and post-award interest, relying on *R.P. Garg case*¹⁷ to hold that Section 31(7)(b) operates independently and is not subject to contractual exclusion unless expressly provided.¹⁸
- Upheld the grant of post-award interest as consistent with the statutory framework, noting that it ensures timely compliance and compensates delayed payment.¹⁹

⁷ Paragraph No. 25 of the Judgement.

⁸ Paragraph No. 27 of the Judgement.

⁹ Paragraph No. 45 of the Judgement.

¹⁰ Paragraph No. 29 of the Judgement.

¹¹ *Union of India v. Bright Power Projects (India) (P) Ltd* | (2015) 9 SCC 695.

¹² *Union of India v. Manraj Enterprises* | (2022) 2 SCC 331.

¹³ *Sree Kamatchi Amman Constructions v. Railway Administration* | (2010) 8 SCC 767.

¹⁴ *Ambica Construction v. Union of India* | (2017) 14 SCC 323.

¹⁵ *Raveechee & Co. v. Union of India* | (2018) 7 SCC SCC 664.

¹⁶ Paragraph No. 52 and 53 of the Judgement.

¹⁷ *R.P. Garg v. Chief General Manager* | 2024 SCC OnLine SC 2928.

¹⁸ Paragraphs No. 55 and 56 of the Judgement.

¹⁹ Paragraphs No. 57 and 58 of the Judgement.

- Modified, relying on *Gayatri Balasamy* case²⁰, the rate of post-award interest from 12% to 8% per annum, holding that courts may adjust such rates to ensure fair compensation.²¹

Hence, the SC partly allowed the appeal, set aside the arbitral award to the extent it granted pre-award/*pendente lite* interest and modified the rate of post-award interest from 12% to 8% per annum, while otherwise upholding the award.²²

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²⁰ *Gayatri Balasamy v. ISG Novasoft Technologies Ltd* | (2025) 7 SCC 1.

²¹ Paragraphs No. 59 and 60 of the Judgement.

²² Paragraphs No. 60 – 62 of the Judgement.