
Bombay High Court Upholds Arbitration Agreement Using Business Efficacy Test

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Introduction

In a recent decision in *Lords Inn Hotels and Resorts v. Pushpam Resorts LLP*¹, the Bombay High Court has addressed a fundamental question in arbitration law, *i.e.*, whether an arbitration agreement can be inferred from an ambiguous contract. The judgment applies the business efficacy test to determine whether the parties had a binding arbitration agreement despite the absence of an explicitly worded arbitration clause. The ruling has significant implications for commercial agreements, reinforcing the principle that party autonomy in dispute resolution must be respected, even if the agreement is inartfully drafted. In this article, we navigate through the facts of the case and the findings of the High Court.

Brief Facts

The dispute arose from a Resort Management Agreement ("**Agreement**") dated 10.02.2021 entered between Lords Inn Hotels and Pushpam Resorts LLP. Under this Agreement, Lords Inn was responsible for managing a resort owned by Pushpam in Karjat. However, disputes between the parties led to Pushpam terminating the Agreement on 08.10.2024, effective 15.12.2024. Lords Inn contested the termination, citing breaches by Pushpam and invoking an arbitration clause allegedly contained in the Agreement. Pushpam, however, argued that no valid arbitration agreement existed in terms of Section 7 of the Arbitration and Conciliation Act, 1996 ("**Arbitration Act**").

The dispute led to two proceedings before the Bombay High Court. Firstly, a petition under Section 9 of the Arbitration Act, seeking interim relief to prevent Lords Inn's removal from the resort. Secondly, an application under Section 11, seeking the appointment of an arbitrator. The crux of the dispute revolved around whether the Agreement contained a valid arbitration clause, as Lords Inn contended, or whether the contract failed to meet the statutory requirements of Section 7 of the Arbitration Act.

Lords Inn's Arguments

Lords Inn contended that the Agreement, when read as a whole, demonstrated an intent to resolve disputes through arbitration. It relied on Article XXIV, which referred to an "*Arbitration Clause below*". Although no separate arbitration clause was found, it argued that this reference itself signified the parties' intent to arbitrate. Lords Inn also pointed to other sections of the Agreement, which also mentioned arbitration in specific contexts, further reinforcing the existence of an arbitration agreement.

¹ 2025:BHC-OS:2178.

Lords Inn invoked the business efficacy test, asserting that commercial contracts should be interpreted in a manner that gives effect to the parties' intent rather than invalidating the same due to drafting-related errors.

Pushpam's Arguments

Pushpam argued that the Agreement did not contain a valid arbitration clause and that mere references to arbitration in scattered sections were insufficient to satisfy the requirements of Section 7 of the Arbitration Act. It highlighted that early drafts of the contract had contained a separate arbitration clause (Article XXV), which was later removed in final negotiations. This, as per Pushpam, indicated a deliberate decision by the parties to exclude arbitration. Pushpam also contended that the absence of a clearly defined arbitration clause made it legally untenable to enforce arbitration proceedings.

High Court's Analysis and Conclusion

On Section 7 of the Arbitration Act

The High Court examined Section 7, which defines an arbitration agreement and requires it to be in writing. The High Court held that an arbitration agreement must be explicit and not merely inferred from scattered references to arbitration within a contract.

On the Ambiguity in the Contract and the Business Efficacy Test

Recognising the evident ambiguity, the High Court applied the business efficacy test, a principle used to ascertain implied contractual terms. The five-part test examines whether:

- (i) The implied term is reasonable and equitable;
- (ii) It is necessary for business efficacy;
- (iii) It is so obvious that it "*goes without saying*";
- (iv) It can be clearly expressed; and
- (v) It does not contradict any express term of the contract.

The High Court found that, based on the negotiation history, both parties initially considered arbitration but later removed the detailed arbitration clause while still retaining references to arbitration elsewhere in the contract. The omission of the arbitration clause appeared to be a drafting oversight rather than an intentional exclusion of arbitration.

On the Role of Extrinsic Evidence

The High Court also considered email correspondence and multiple drafts exchanged between the parties before execution of the final agreement. These exchanges demonstrated that the parties initially intended to arbitrate all disputes but inadvertently omitted the final arbitration clause in the executed version.

Decision of the Court

Applying the business efficacy test, the High Court held that the parties' intention to arbitrate was discernible despite the missing arbitration clause. It ruled in favor of Lords Inn and appointed an arbitrator under Section 11. It also directed that the pending Section 9 petition be treated as an application under Section 17, allowing the arbitral tribunal to decide on interim relief.

Comment

The High Court's reliance on the business efficacy test aligns with global arbitration jurisprudence, which prioritises commercial intent over strict formalities. The "*substance over form*" approach ensures that arbitration agreements are not invalidated due to technical deficiencies in drafting.

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