IN THE SUPREME COURT OF THE DEMOCRATIC SOCIALIST REPUBLIC OF SRI LANKA

In the matter of an Appeal to the Supreme Court from the judgement of the High Court of Western Province (holden in Colombo) exercising Civil/Commercial jurisdiction dated 17/10/2013 in terms of the provisions of the High Court of Provinces (Special Provisions) Act No. 10 of 1996.

SC/ CHC / APPEAL / 56 / 2014

Eric Peiris,

No. 2A, Cemetery Road,

Minuwangoda.

PLAINTIFF

Vs

Sri Lanka Insurance Corporation Ltd,

No.21, Vauxhall Street,

Colombo 02.

DEFENDANT

AND NOW BETWEEN

Eric Peiris,

No. 2A, Cemetery Road,

Minuwangoda.

PLAINTIFF - APPELLANT

Vs

Sri Lanka Insurance Corporation Ltd,

No.21, Vauxhall Street,

Colombo 02.

DEFENDANT - RESPONDENT

BEFORE : Vijith Malalgoda, PC. J

A.H.M.D. Nawaz, J

Shiran Gooneratne, J

COUNSEL : Chathura Galhena with Manoja Gunawardena and Namal Madhushanka for the Plaintiff -Appellant.

Harsha Amarasekara, PC. with Shehan Gunawardena and Nadun Dissanayake for the Defendant-Respondent.

ARGUED ON : **28.02.2022**

DECIDED ON : **22.08.2024**

A. H. M. D. Nawaz, J.

1. This appeal stems from an action instituted in the Commercial High Court, despite the presence of an arbitration agreement within the primary contract (Fire Insurance Policy) between the Plaintiff-Appellant and the Defendant-Respondent. The central issue in this appeal is whether a party to an arbitration agreement can establish an independent cause of action based on the correspondence exchanged between the parties, as argued by the Plaintiff-Appellant in this case.

2. In other words, the Plaintiff-Appellant, Eric Peiris, insisted that the proceedings be entertained and continued in the Commercial High Court, while the Defendant-Respondent, Sri Lanka Insurance Co. Ltd. (SLIC), opposed the action, citing the arbitration agreement in the fire insurance policy.

3. The learned Commercial High Court Judge after having taken evidence upheld the objection raised by the Sri Lanka Insurance Cooperation and concluded that there was no jurisdiction conferred on the court as a result of the arbitration agreement.

4. In essence, the arbitration agreement in the main contract—the fire insurance policy—competes for recognition in this case against a separate contract that the Plaintiff-Appellant claims emerged from the correspondences, thereby providing the basis for a court action.

5. At the very outset, let me outline the basis of the Plaintiff's claim to a separate contract that provides the cause of action. This separate contract is claimed to be constituted by a letter marked '**P1,**' dated March 18, 2008, in which the Defendant-Respondent, Sri Lanka Insurance Corporation, offered to pay a sum of Rs. 8,195,162 in full and final settlement of the amount due under the fire insurance policy. I must observe that the Plaintiff-Appellant assigns different classifications to the letter '**P1.**' While '**P1**' itself uses the term "offer to pay," the Plaintiff-Appellant characterizes it as an agreement, asserting that a breach of this agreement constitutes the cause of action.

6. At this stage, it is pertinent to refer to the facts of the case. The business entity known as M/S Peiris Press, designated as the insured in the fire insurance policy, entered into the contract of insurance for its industrial business premises, which included the building, along with fixtures and fittings, and two printing machines located in Minuwangoda.

7. The printing machinery had been mortgaged to Hatton National Bank (HNB), Minuwangoda, and HNB's name appears in the Fire Insurance

Policy as the mortgagee, likely due to the mortgage of the two printing machines in exchange for some financial accommodations. This contract of insurance was apparently entered into on September 18, 2007. This insurance contract contains a separate and distinct arbitration agreement, which reads as follows:

> *"If any difference arises as to the amount of any loss or damage such difference shall independently of all other questions be referred to the decision of an arbitrator, to be appointed in writing by the parties in differences..."*

8. Thus, it is evident that the parties have consensually agreed to refer any differences regarding the amount of any loss or damage to arbitration. The backdrop of the current dispute between the parties involves a fire outbreak, which resulted in loss and damage to some of the Plaintiff's machinery. In response, Sri Lanka Insurance Corporation, by a letter marked '**P1**' and dated March 18, 2008, offered M/S Peiris Press a sum of Rs. 8,195,162 as compensation for the loss and damage incurred by the partnership, of which the Plaintiff, Eric Peiris, was a partner.

9. In the following month, on April 21, 2008, events took a different turn. The Defendant-Respondent, SLIC, sent a letter marked '**P2**,' in which they claimed that although the initial estimate of the loss was Rs. 8,495,162, it later became apparent that the actual loss would have been significantly lower. Specifically, they noted that the maximum value of the Heidelberg

Printing machine damaged in the fire was only Rs. 1,100,000. In other words, the letter '**P2**' alleged that the value of the Heidelberg Printing machine had been significantly overestimated at the time of taking the insurance policy, suggesting an attempt to unjustly enrich the partnership. This allegation was a central point in the letter dated April 21, 2008.

10. In the letter, Sri Lanka Insurance Corporation (SLIC) went on to state that it was repudiating the Plaintiff-Appellant's claim and rejecting any entitlement to compensation. SLIC justified this decision by asserting that there had been a breach of *uberrima fides*, the doctrine of utmost good faith, which is fundamental to the formation of any insurance contract.

11. The letter '**P2**' further informed the Plaintiff that, due to the breach of good faith, Sri Lanka Insurance Corporation was withdrawing the entire amount previously offered in '**P1.**'

12. This led to the issuance of a subsequent letter of demand, marked '**P13**' and dated February 5, 2010, which went unanswered by Sri Lanka Insurance Corporation. The non-response was subsequently argued to be an implied admission of liability, with reliance placed on the case of ***De Mel v. P. Saravanamuttu v. R. A. De Mel***[1], which has been followed by

[1] 49 N.L.R 529

many precedents, including ***Seneviratne and Others v. Lanka Orix Leasing Company Ltd.***[2]

13. However, I would venture to state that a non-response to a letter of demand, by itself, does not necessarily give rise to an inference of implied acknowledgment of liability. When the rejection of a claim has been explained with reasons in a prior correspondence, remaining silent in response to a subsequent letter of demand cannot automatically be interpreted as an admission of liability. Therefore, the inference of liability is not automatic upon a non-response to a letter of demand.

14. In '**P13,**' the letter of demand, the Plaintiff also sought a sum of Rs. 25,000,000 as damages within 14 days, in addition to the Rs. 8,495,162 that had been rejected by Sri Lanka Insurance Corporation. This demand ultimately led to the institution of legal action in the Commercial High Court on February 22, 2010. The Plaintiff prayed for a declaration that the Defendant should pay the agreed sum of Rs. 8,495,162, along with interest from February 22, 2010, until full payment. Additionally, the Plaintiff included a claim for the consequential loss of Rs. 25,000,000 in the prayer to the plaint.

15. In their answer dated November 3, 2010, the SLIC raised a preliminary objection, arguing that the court lacked jurisdiction to proceed with the

[2] (2006) 1 Sri.LR 230.

case due to the arbitration clause in the main contract (Fire Insurance Policy). This objection was made pursuant to Section 5 of the Arbitration Act No. 11 of 1995.

16. Sri Lanka Insurance Corporation raised the demur that the arbitration clause deprived the Commercial High Court of jurisdiction and, therefore, the action should be dismissed. It is important to note that while the Plaintiff conceded that the insurance contract contained an arbitration clause, he alleged that his cause of action arose independently of that arbitration agreement. In fact, the plaint specifically stated that "*the Plaintiff's present cause of action has not arisen out of the said clause.*"

17. Referring to '**P1**' and '**P2,**' the two letters sent by SLIC, the Plaintiff - Appellant attributed the cause of action to these communications. According to '**P1**,' "*the Defendant had offered to pay a sum of Rs. 8,495,162 to the Plaintiff in respect of the Plaintiff's claim.*" However, in '**P2**,' dated April 21, 2008, "*when the Defendant sought to obtain the said monies, the Plaintiff unilaterally withdrew the payment*."

18. The Plaintiff-Appellant argued that these letters, '**P1**' and '**P2,**' constituted the cause of action, entirely independent of the arbitration agreement. In other words, these two letters stood alone, unconnected to the arbitral clause. Therefore, the arbitration agreement could not denude the court of jurisdiction, as it was not triggered in this case. This was the argument

raised by the Plaintiff-Appellant in the Commercial High Court and has been consistently maintained even before this court.

19. The learned Judge of the Commercial High Court considered the evidence before ruling on the preliminary objection. At the conclusion of the trial, the learned Judge upheld the preliminary objection raised by SLIC and dismissed the Plaintiff's action. In a judgment dated October 17, 2013, the Commercial High Court Judge determined that he had no jurisdiction to decide the disputed questions of fact in the case. There were 22 issues raised by both the Appellant and SLIC, but according to the learned High Court Judge, none of these issues could be adjudicated upon due to the lack of jurisdiction in the High Court.

20. Thus, upon a perusal of the judgment, it would appear that party autonomy inherent in an arbitration agreement was given pride of place by the learned High Court Judge and it is implicit in the judgment that the dispute between the parties is not capable of being adjudicated upon in courts because the arbitral clause alone could govern the dispute between the parties. This was the view of the learned High Court Judge which is being impugned before this Court.

21. Given the specific arbitral clause which pertains to differences arising between the parties as to the quantum of loss or damage, can it be argued

that at the time of institution of the suit in the commercial High Court, there was no difference between the parties?

22. The word "difference" is defined in *The Reader's Digest Great Encyclopedic Dictionary* to mean a *disagreement in opinion, dispute or quarrel.*[3] Similarly, *The Random House Dictionary of the English language*[4] defines "difference" to include, among other things, a *dispute or quarrel*. Given that these authoritative sources clearly outline the broad meaning of "difference" to encompass disputes between parties, it is unsurprising that the word is commonly used in the same sense within arbitration clauses.

23. In fact, *Redfern and Hunter on International Arbitration*-an authoritative text on International Commercial Arbitration quite clearly states the following:

> *Given words such as 'claims', 'differences', and 'disputes' have been held by English courts to encompass a wide jurisdiction in the context of the particular agreement in question. In the United States, the words 'controversies or claims' have similarly been held to have a wide meaning, and if other words are used, it may be considered that the parties intended some limitation on the kind of disputes referred to arbitration.*[5]

[3] Volume I, 2nd Edition (1971).
[4] the unabridged edition (Random House, New York, 1960).
[5] See Ibid 7th Edition (2022) Nigel Blackaby KC, Constantine Partasides KC with Alan Redfern at para 2.75

24. In using the word 'difference' in the arbitration agreement, both parties must be taken to have used it to denote a dispute that will arise or has arisen as to quantum of loss or damage.

25. In its context, it is useful to refer to the preamble to the Arbitration Act, No. 11 of 1995, which, *inter alia*, states that one of the main objects of the enactment was to give effect to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (Done at New York, 10 June 1958; Entered into force, 7 June 1959 330 U.N.T.S. 38 (1959) also known as the "New York Convention") and to provide for matters connected therewith or incidental thereto". In this connection, it is pertinent to look at Article II paragraph 1 of the said Convention, which provides that,

> *"Each Contracting State shall recognize an agreement in writing under which the parties undertake to submit to arbitration all or* ***any differences*** *which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not, concerning a subject matter capable of settlement by arbitration*". (Emphasis added).

26. Even the New York Convention, which the Arbitration Act, No. 11 of 1995 seeks to implement, uses the phrase "any differences" in the broadest sense to signify a dispute between the parties. In this context, any "difference" regarding the quantum of loss or damage in the relevant arbitration clause

should indeed refer to any dispute that has arisen between the parties concerning the quantum of loss or damage.

27. It is axiomatic that in interpreting the provisions of the Arbitration Act, this Court has to bear in mind the obligation cast on Sri Lanka to interpret it in consonance with the New York convention. The pertinent question, therefore, is whether there was a dispute regarding the quantum of loss or damage between the Appellant and SLIC at the time the suit was instituted in court.

28. The dispute is evidenced by the letters '**P1**' and '**P2.**' While '**P1**' offered a payment of Rs. 8,495,162, '**P2**' revoked that offer. It is as clear as day that a dispute arose regarding the quantum. '**P2**' explained that the offer was being withdrawn due to a lack of utmost good faith, a principle that underpins all insurance contracts. '**P1**' and '**P2**' constitute evidence of the dispute that the parties consensually agreed to resolve through arbitration. The learned High Court Judge did not err in holding that he lacked jurisdiction to proceed with the case.

29. Indeed, Section 5 of the Arbitration Act dispensed with the distinction which was drawn by Sharvananda CJ in ***Hotel Galaxy (Pvt) Ltd v Mercantile Hotels Ltd***[6] between a bare arbitration agreement and a *Scott v Avery* clause. Under a *Scott v Avery* clause, a court does not derive

[6] (1987) 1 Sri LR 5.

jurisdiction until an arbitration award has been made. An arbitration followed by an award is a condition precedent to an action being instituted. But today under the Arbitration Act No. 11 of 1995, there is no bar to an action on the contract unless an objection is taken based on an arbitration agreement.

30. Therefore, when the Defendant-Respondent, SLIC, raised an objection pursuant to Section 5 of the Arbitration Act No. 11 of 1995, to the maintainability of the action, it was incumbent upon the learned High Court Judge to give effect to the parties' autonomous agreement to arbitrate. This obligation stands unless the matter covered by the arbitration agreement is contrary to public policy or is not capable of determination by arbitration, as outlined in Section 4 of the Arbitration Act, No. 11 of 1995.

31. The difference or dispute between the parties arose from a contract, specifically the contract of insurance, and the merits of the dispute involve a range of issues, such as whether there was a breach of *uberrima fides*, justifying the subsequent repudiation of the Appellant's claim. This dispute falls squarely within the scope of the arbitration agreement, which is neither tainted by public policy nor incapable of determination by arbitration.

32. Given the facts of the case and the nature of the dispute arising from the contract, this Court must lean in favor of upholding the arbitration clause.

Therefore, the determination made by the learned Judge of the Commercial High Court to give effect to the arbitration agreement cannot be faulted.

33. The dispute between the parties is inextricably interwoven with the contract of insurance, the breach of which—or lack thereof—had to be adjudicated through arbitration. Accordingly, I proceed to affirm the judgment of the learned Judge of the Commercial High Court dated October 17, 2013, and dismiss the appeal. The learned Judge of the Commercial High Court is directed to enter judgment accordingly.

Judge of the Supreme Court

V. K. Malalgoda, PC. J

I agree, Judge of the Supreme Court

Shiran Gooneratne, J.

I agree, Judge of the Supreme Court