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# THE PUBLIC POLICY DOCTRINE IN ARBITRATION: A PRIMER ON ITS EFFECT ON CHALLENGES AND ENFORCEMENT OF AWARDS

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**Abstract**

*Arbitration law in India is principally governed under the Arbitration and Conciliation Act, 1996 (the "Act") (as amended in 2015). The aim and object of the Statute is to foster an environment wherein alternative modes of dispute settlement, such as arbitration, negotiation and mediation are given full effect to and judicial intervention in such modes of dispute resolution are kept at a bare minimum. The Act therefore delineates permissible instances wherein the intervention of the Courts would be warranted.*

*This paper aims to analyse one such permissible instance under the Act – that of setting aside and challenge to an arbitral award on the ground of Public Policy. The interpretation of the term Public Policy has come under severe judicial scrutiny, often resulting in contradictory and ambiguous interpretations being applied to the doctrine by the Courts.*

*Part I of this paper traces the development of the doctrine under the pre-1996 regime and its peripheral, yet gradual intrusion under the Act. Part II analyses the 'broad' and 'narrow' view of Public Policy, as given effect to by the Courts and traces its impact on the enforcement of domestic awards and the challenge to foreign arbitral awards. Part III interprets a host of judicial decisions starting from Saw Pipes and Renusagar to Associate Builders and Shri Lal Mahal. Part IV captures the amendments brought in the 1996 Act by the 2015 Amendments introduced by the Parliament. Part V concludes by positing that the recent judicial trends suggest that the narrow view of Public Policy is being favoured by*

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*the Courts which in essence will allow India to market and develop itself as a global hub of arbitration, for prospective investors and litigants alike.*

## I. Introduction

Arbitration and Conciliation (or Mediation) have evolved as effective mechanisms of alternative dispute resolution in India, providing parties with a forum for settlement of their disputes, without having to invest their resources in protracted litigation before the Civil Courts in India. However, the awards rendered through such alternate means of dispute resolution are subject to the review of the civil courts *inter alia* on the grounds of it being violative of the Public Policy of the country.

An arbitral award made under Part I (awards made in an India-seated Arbitration) of the Arbitration and Conciliation Act, 1996 (the "Act") can be challenged under Section 34 (2) (a) and (b) of the Act which is derived from Article 34 of the UNICITRAL Model Law. Therefore, the objective of this paper is to trace the development of the public policy doctrine in arbitration and reflect upon its use as a ground for challenging or setting aside an arbitral award.

### A. PUBLIC POLICY IN THE PRE-1996 LANDSCAPE

*The Arbitration (Protocol and Convention) Act, 1937*

The doctrine of Public Policy was initially codified in The Arbitration (Protocol and Convention) Act, 1937 (the "Protocol and Convention Act"). Under the provisions of the Act, a foreign award would not be enforced if it contradicted the *public policy* or the *law of India*.[1] The Foreign Awards (Recognition and Enforcement) Act, 1961 (the "Foreign Awards Act") also provided for the non-enforcement of a foreign award if it was

[1] The Arbitration (Protocol and Convention) Act 1937 § 7.

contrary to the public policy of India[2] and was derived from Article V(2)(b) of the New York Convention which read as follows:

> *"V (2) -Recognition and enforcement of an arbitral award may also be refused if the competent authority in the country where recognition and enforcement is sought finds that: (b) The recognition or enforcement of the award would be contrary to the public policy of that country".*

Therefore, upon a conspective reading of both these Acts, the provision in Section 7 of the Protocol and Convention Act rendering a foreign award unenforceable merely upon it being contrary to the *law of India*, was no longer considered to be a valid ground for resisting the enforcement of an award under the New York Convention. The grounds for the unenforceability of a Foreign Award, though constricted, did not however have an effect on the public policy doctrine firmly entrenched in respect of foreign awards.

*The Arbitration Act, 1940*

The Arbitration Act, 1940 (the "1940 Act") dealt with arbitrations seated in India. The Supreme Court[3] while lamenting upon the inefficacy of the Act to establish Arbitration as a viable mode of dispute settlement observed as follows:

> *"…The way in which the proceedings under the Act are conducted and without an exception challenged in Courts, has made lawyers laugh and legal philosophers weep. Experience shows and law reports bear ample testimony that the proceedings under the Act have become highly technical accompanied by unending prolixity, at every stage providing a legal trap to the unwary. Informal forum chosen by the parties for expeditious disposal of their disputes has by the*

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2 The Foreign Awards (Recognition and Enforcement) Act 1961 § 7(i)(b)(ii).

3 Guru Nanak Foundation v. Rattan Singh, (1981) 4 SCC 634, 635.

> *decisions of the Courts been clothed with 'legalese' of unforeseeable complexity."*

However, it would be pertinent to note that the public policy doctrine did not manifest itself as an impediment to the enforcement of an award under the provisions of the 1940 Act. The Courts primarily restricted the grounds of challenge to an arbitral award to *error apparent on the face of the award,*[4] misconduct of the arbitrator or the proceedings,[5] making of the arbitral award after the proceedings had become invalid or were superseded[6] or cases where the award was improperly procured or was otherwise invalid.[7] There were however a few decisions where setting aside of an award for misconduct of the arbitrator was premised on the notion that an arbitrator is bound to act in accordance with the public policy of India.[8] The Bombay High Court also held that even though arbitrators were not bound by strict rules of procedure or evidence; *such of the rules of evidence which were based on fundamental principles of justice and public policy* applied to arbitral proceedings as non-observance of the same would lead to substantial injustice being perpetrated.[9] To apply the public policy doctrine for setting aside of an arbitral award under the 1940 Act, the Courts thus applied a twofold test:

a. If the arbitrator had knowledge of the illegality of the contract entered into between the parties; and

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4 Union of India v. A.L. Rallia Ram, AIR 1963 SC 1685.
5 The Arbitration Act 1940 § 30 (a).
6 The Arbitration Act 1940 § 30 (b).
7 The Arbitration Act 1940 § 30 (c).
8 HMG Engineering Pvt. Ltd, (2000) 1 Bom CR 221; M/S. Kochhar Construction Co. v. Union of India & Anr, ILR (1987) 1 Del 571, ¶24; Fertilizer Corporation of India Ltd. v. Bharat Painters, AIR 1986 Orissa 82, ¶6; Abhai Singh v. Sanjay Singh, AIR 1989 All 214, ¶20.
9 Aboobaker Latif v. Reception Committee of the 48th Indian National Congress, AIR 1937 Bom 410, ¶12.

b. Having knowledge of the illegality of the contract, nevertheless proceeded to deliver an award in relation to disputes arising out of the contract.[10]

## B. PUBLIC POLICY UNDER THE 1996 ACT

With the enactment of the 1996 Act, the law governing Indian arbitrations and enforcement of Foreign Awards were brought under the ambit of a single statute, repealing the erstwhile 1940 Act, the Protocol and Convention Act and the Foreign Awards Act. The scheme of the 1996 Act is as follows:

- Part I dealing with India seated arbitrations;
- Part II dealing with enforcement and recognition of foreign awards falling under the New York Convention and the Geneva Convention; and
- Part III dealing with Conciliation.

Part I of the Act further divides India seated arbitrations into the following two categories:

- Where the parties to the dispute are both Indian (domestic arbitration); and
- Where *at least* one of the parties to the dispute is a foreign citizen, a body corporate or entity whose central management and control is exercised from outside India or by the Government of a foreign country (international commercial arbitration).[11]

*The UNICITRAL Model Law: Introducing Public Policy under the 1996 Act*

It would be pertinent to note that Part I of the 1996 Act is effectively a reproduction of the UNCITRAL Model Law on International Commercial Arbitration (the "UNCITRAL Model

[10] ITC Limited v. George Joseph Fernandes & Anr, (1989) 2 SCC 1, ¶26.
[11] Arbitration and Conciliation Act 1996 § 2(1)(f)

Law"). Article 34 of the UNCITRAL Model Law, setting out the provisions for a challenge to an award before a national court, mirrors the grounds set out in Article V of the New York Convention for the refusal of the enforcement of a foreign award.[12] Therefore, Section 34 of the 1996 Act, which is modelled on Article 34 of the UNCITRAL Model Law, and Section 48 of the 1996 Act, which is modelled on Article V of the New York Convention, both contain a reference to the ground of 'public policy' to challenge an award or seek refusal of enforcement, respectively.

Section 48 of the 1996 Act (Part II) allows parties to object to the enforcement of a foreign award made under the New York Convention on grounds of Public Policy.[13] Additionally, Section 57 of the Act (Part II) provides for the non-enforcement of a Geneva Convention Award on grounds of Public Policy and the award conflicting with the *principles of the law of the country*.[14]

## II. Judicial Interpretation of Public Policy: The Broad & Narrow View

The Public Policy Doctrine has judicially been pigeon-holed into the *broad* view and the *narrow* view. The narrow view espouses a restricted interpretation of the Public Policy doctrine calling for Courts to exercise caution in creating new heads of Public Policy whereas the broad view undertakes a contextual approach to the Public Policy doctrine, leaving it open to be amended and modified on a case to case basis.

In the *Gherulal* case,[15] the Supreme Court observed that "*though the heads are not closed and though theoretically it might be permissible to*

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12 ANTON G. MAURER, THE PUBLIC POLICY EXCEPTION UNDER THE NEW YORK CONVENTION 59 (Huntington, New York: Juris 2013).

13 Arbitration and Conciliation Act 1996 § 48(2)(b).

14 Arbitration and Conciliation Act 1996 § 57(iii).

15 Gherulal Parakh v. Mahadeodas Maiya & Ors, AIR 1959 SC 781, ¶21, 23 & 30.

*evolve a new head under exceptional circumstances of a changing world it is advisable in the interest of stability of society not to make any attempt to discover new heads in these days."* In *Kedar Nath Motwani vs. Prahlad Rai,*[16] the Court however clarified that the enforcement of a contract would be deemed to be against the Public Policy of India only if the illegality went to the root of the contract.

The broad view of the Public Policy doctrine, however, gained currency with the Supreme Court's ruling in the *Muralidhar* case,[17] wherein the Court observed that "*what constituted public policy earlier might not constitute public policy now, hence the development of new fields of public policy was imperative. Public policy does not remain static in any given community. It may vary from generation to generation and even in the same generation. Public policy would be almost useless if it were to remain in fixed moulds for all time."* In *Central Inland Water Transport,*[18] observing that adopting a narrow view of the Public Policy doctrine would countenance judicial law making, the Court held that "*public policy connotes some matter which concerns the public good and the public interest. The concept of what is good for the public or in public interest or what would be harmful or injurious to the public good or interest has varied from time to time."* This view was further strengthened in *Rattan Chand Hira Chand,*[19] where the Supreme Court decided that an injury to public interest would depend upon the context in which it is made and any contract which had a tendency to injure public interest was one against public policy. Although it was the legislature's duty to keep pace with the changing paradigms of society, it was the duty of the Courts to step in upon the Legislature's failure to

16 Kedar Nath Motwani v. Prahlad Rai, AIR 1960 SC 213.

17 Muralidhar Aggarwal & Anr v. State of Uttar Pradesh & Ors, (1974) 2 SCC 472, ¶28 – 32.

18 Central Inland Water Transport Corporation Ltd. v. Brojo Nath Ganguly, (1986) 3 SCC 156, ¶92.

19 Rattan Chand Hira Chand v. Askar Nawaz Jung (Dead) by LRS and Ors., (1991) 3 SCC 67, ¶19 & 23.

fill the lacuna and to decide what they felt is against the Public Policy of the country.

However, there was a fundamental divergence once again from the broad view when the Courts in the *Zoroastrian Cooperative Housing Society Case*[20] refused to intervene in the formation of a society limiting membership to people of a particular religion. Premising its arguments on the *Gherulal* principle (supra), the Court upheld the sanctity of the contract entered into between the parties and held that *an agreement otherwise legal could not be held to be void unless it resulted in the performance of an unlawful act.*

## A. THE IMPACT OF PUBLIC POLICY ON ENFORCEMENT OF FOREIGN AWARDS

The enforcement of foreign awards under the 1996 Act are governed under the principles enshrined in the Geneva Convention and the New York Convention. While the illegality of the contract forms the principal ground for non-enforcement of a foreign award under the Geneva Convention,[21] violation of the Public Policy of the country where the award is sought to be enforced is the principal criterion required under the New York Convention.[22] It would be pertinent to note at this point in time that India was one of the first countries to ratify the New York Convention and incorporate its provisions within its own municipal laws, by virtue of the enactment of the Foreign Awards (Recognition and Enforcement) Act, 1961.

In *Renusagar Power Company Ltd. vs. General Electric Company,* [23] the Supreme Court adopted the narrow view of the Public Policy and

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[20] Zoroastrian Co-operative Housing Society v. District Registrar, Coop. Societies (Urban), (2005) 5 SCC 632, ¶26 & 38.

[21] David Taylor & Son v. Barnett Trading Co, (1953) 1 WLR 562, ¶563.

[22] Deutsche Schachtbauund Tiefbohrgesellschaft mbH v. Ras Al-Khaimah National Oil Co, [1987] 2 All ER 769.

[23] Renusagar Power Company Ltd. v. General Electric Company, (1994) Supp 1 SCC 644, ¶63 & 66.

held that "*public policy*" would mean the *doctrine of public policy as applied by the Court in India and not international public policy*." Placing reliance on the objects and reasons of the Foreign Awards Act, the Court reasoned that facilitation of international trade and commerce would be severely affected if the broad view of Public Policy was sought to be enforced. The Courts set out certain tests to determine when a foreign award can be said to fall foul of the Public Policy doctrine in order for the court to refuse its enforcement:

- If the award contradicted the fundamental policy of Indian law;
- If the award was vitiated by virtue of it affecting the interests of India; and
- If the award was against the basic tenets of justice and morality.

A distinction was also drawn between the award itself and the enforcement of the award, noting that the public policy doctrine applied only at the enforcement stage of the award and precluded the Courts from undertaking a review of the merits of the award[24]. The application of the public policy doctrine for the non-enforcement of a Foreign Award would thus be valid only if it fell afoul of any of limbs of the three-pronged test as laid down in *Renusagar*[25] and if the Public Policy that was being infringed upon, was the *Public Policy of India and not of any other foreign country*[26].

## B. THE IMPACT OF PUBLIC POLICY ON DOMESTIC AWARDS

Upon the enactment of the 1996 Act, the Courts had a general tendency to apply the narrow view even to Part I arbitrations.[27]

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24 *Id* at ¶34 – 36.
25 Id at ¶66.
26 Smita Conductors Ltd. v. Euro Alloys Ltd, (2001) 7 SCC 728, ¶12.
27 Olympus Superstructure v. Meena Khetan AIR 1999 SC 2102; Narayan Lohia v. Nikunj Lohia AIR 2002 SC 1139.

In *Konkan Railway,*[28] the Court categorically observed that "*the statement of Objects and Reasons of the Act clearly enunciates that the main objective of the legislature was to minimize the supervisory role of Courts in the arbitral process* and that *under the new law the grounds on which an award of an arbitration could be challenged before the Court have been severely cut down*." Similarly, the Bombay High Court, in the *Vijaya Bank*[29]case, had held that a mere mistake in applying the substantive law of India to an award would not incur the Public Policy objection to its enforcement. The narrow view of the Public Policy doctrine, as enunciated in *Renusagar* was thus imported even in cases of Part I arbitrations.

## III. *Saw Pipes* - Nullifying The Narrow View of Public Policy for Part I Arbitrations

In 2004, the Supreme Court in *ONGC Ltd. vs. Saw Pipes Ltd*,[30] distinguished between domestic and foreign awards with respect to public policy. While considering a challenge under Section 34 of the Act to a Part I award, the Supreme Court held that the narrower concept of public policy enunciated in *Renusagar* was only applicable to foreign awards and not Part I awards. Apart from the three heads of public policy laid down in *Renusagar,* the Supreme Court interpreted public policy to include "patent illegality" and held that an award can be set aside if it is *patently illegal and if such illegality went to the root of the matter or was so unfair and unreasonable that it shocked the conscience of the Court*.[31] Therefore, it was held that patent illegality would include considerations such as whether an award was based on an erroneous proposition of law or erroneous application of the law or was against the terms of the contract.[32] The court relied on section 28(1)(a) of the 1996

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28 Konkan Railway Co. Ltd. v. Mehul Construction Co, (2000) 7 SCC 201, ¶4.
29 Vijaya Bank v. Maker Development Services Pvt. Ltd, (2001) 3 Bom. CR 652, ¶21 & 35.
30 ONGC Ltd. V Saw Pipes Ltd., (2003) 5 SCC 705 ¶28.
31 *Id.* at ¶31.
32 *Id.* at ¶55.

Act to justify its interference with the award. The Supreme Court held that the meaning of the term *public policy was wide enough in the case of domestic awards, to even incorporate a ground of "patent illegality"*.[33] In my view, the Supreme Court in *Saw Pipes* fundamentally misconstrued Section 28(1)(a) as a provision applicable to the jurisdiction of Courts considering challenges to awards. In reality, Section 28(1)(a) is a provision (along with Section 28(1)(b)) that governs the law to be applied by an arbitral tribunal in deciding the dispute between the parties. They were therefore both merely choice of law provisions. A new head of public policy was thus evolved, which did not take into account the Supreme Court's own caution on creating new heads of public policy without any conclusion on "*clear and incontestable harm to the public*"[34] or that such heads could only be created to prevent an "*injury to public interest or welfare.*"[35]

The phrase 'patent illegality' has been read to mean an obvious illegality based on a clear ignorance or disregard of the provisions of law.[36] *Saw Pipes* effectively first interpreted and enunciated the law regarding liquidated damages as it should be based on the specific facts and circumstances of the case, and then found the arbitral tribunal's application of this (new) law to be erroneous. This process is inconsistent with ascertaining that a finding suffered from *"patent illegality"* and suggests that the Supreme Court did not exclude mere *"error of law"* or even *"error in application of the law"* when it referred to *"patent illegality"*. Introducing patent illegality has unforeseen consequences especially with respect to international commercial arbitration where foreign law is a

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33 *Id.* at ¶22.

34 Gherulal Parakh v. Mahadeodas Maiya & Ors, AIR 1959 SC 781 ¶23.

35 Murlidhar Aggarwal & Anr v. State of Uttar Pradesh & Ors., (1974) 2 SCC 472 ¶30 & 31; Rattan Chand Hira Chand v. Askar Nawaz Jung (Dead) by LRS and Ors., (1991) 3 SCC 67 ¶ 17 & 19.

36 Prem Singh v. Deputy Custodian General Evacuee Property, AIR 1957 SC 804; Basappa v. Nagappa, AIR 1954 SC 440; Syed Yakoob v. K.S. Radhakrishnan, AIR 1964 SC 477.

question of fact and such mistake in application of foreign law could lead to awards being set aside on grounds of mistake of fact. A mistake of fact has never been recognized in any jurisdiction, much less in India as constituting a ground to set aside an award. Even *Saw Pipes* recognizes that a mere error of fact (or law for that matter) is not an available ground of challenge under the 1996 Act.

The second qualification introduced by *Saw Pipes* was that the illegality must go to the root of the matter. Here, the Supreme Court does not explain what is meant by an illegality going to the root of the matter. Does it mean that if the illegality forms part of the legal basis for deciding the matter, it goes to the root of the matter? In cases where there are several independent grounds for sustaining a legal decision and the illegality affects one of such grounds, does such illegality go to the root of the matter? This lacuna in the law allows parties to come forward with frivolous claims under Section 34 of the 1996 Act to resist the enforcement of the award passed against it.

In *McDermott International Inc. vs. Burn Standard Co. Ltd,*[37] the Supreme Court clarified that it only has a limited supervisory role and could only interfere with the findings in *Saw Pipes,* it being a coordinate bench ruling, when circumstances exist where such findings would shock the conscience of the court. The Supreme Court in this case broadened the scope of patent illegality given in *Saw Pipes* to include awards which could be set aside due to perversity in evidence and award vitiated by internal contradictions.[38] This line of reasoning has been repeatedly followed by subsequent judgements, thereby introducing a *patent error of law* under the head of patent illegality[39]. Even if the courts

[37] McDermott International Inc. v. Burn Standard Co. Ltd, (2006) 11 SCC 181.
[38] *Id.* at ¶65.
[39] Jagmohan Singh Gujral v. Satish Ashok Sabnis, (2004) 1 Bom CR 307; Bharat M.N. v. Satish Ashok Sabni, (2003) 6 Bom CR 257; Centrotrade Minerals & Metals Inc. v. Hindustan Copper Ltd., (2006) 11 SCC 245.

agree to not interfere with the merits of the award, the introduction of such grounds of setting aside induces a merit based review of the awards.[40] Courts have preferred using the tests laid down in *Saw Pipes* and *McDermott International Inc.* to set aside awards based on a merits review, rather than restricting its application to rare cases in which the circumstances require interference,[41] or using the "*judicial approach*" test to conduct merits reviews of awards and then if so required, to set aside awards even in the absence of a finding that the approach of the Arbitrator was arbitrary or capricious.[42]

*Western Geco: Defining Fundamental Policy of Indian Law*

The Supreme Court in *Western Geco,*[43] after having considered the position established in *Saw Pipes,* held that there was ambiguity in the meaning of the phrase 'fundamental policy of law in India' which was the first head of public policy enunciated in *Renusagar.* The Court in *Western Geco* elucidated the 'fundamental policy of law in India' to mean:

- The undertaking of a fair, bona fide, reasoned and judicial approach by the Courts *qua* the subject matter of the dispute;
- The compliance of the Court's decision with principles of natural justice; and
- The compliance of the Court's decision with the *Wednesbury principles of reasonableness.*[44]

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40 In Numaligarh Refinery Ltd. v. Daelim Industrial Co. Ltd., (2007) 8 SCC 466.

41 Centrotrade Minerals & Metals, (2006) 11 SCC 245. J.G. Engineers v. Union of India, (2011) 5 SCC 758.

42 Ogilvy & Mather Pvt. Ltd & Anr. v. Union of India, 2012 SCC OnLine Del 3364; State of West Bengal v. Bharat Vanijya Eastern Pvt. Ltd. 2017 SCC OnLine Cal 4.

43 ONGC Ltd. v. Western Geco International, (2014) 9 SCC 263, ¶35 – 39.

44 Associated Provincial Picture Houses Ltd. v. Wednesbury Corporation, (1947) 2 All ER 680 (CA).

Failure to adhere to these standards would render an award perverse and irrational, making it a legal nullity. The issue with the *Western Geco* principles arises however due to enforcement of arbitral awards now having to pass the *Wednesbury* test, again allowing the Courts to undertake a merits review of the award. Furthermore, by observing that the contours of the fundamental policy of law in India would not be necessarily restricted to the categories mentioned as above, the scope of judicial review of arbitral awards was by implication deemed to be a necessity.

Additionally, by importing the *Wednesbury* principles into the 1996 Act, administrative law principles of judicial review were sought to be read into the provisions of the Act, which expressly go against the object and intent of the act of keeping judicial intervention to a bare minimum.[45]

*Associate Builders: Applying Public Policy to Part I arbitrations*

Closely following the *Western Geco* ruling, the Supreme Court in *Associate Builders*[46] reiterated the grounds upon which an award can be challenged under the Act:

- Fundamental policy of Indian law which *inter alia* includes compliance with statutory provisions, application of principles of *stare decisis*, judicial approach and compliance with natural justice and *Wednesbury* principles;
- The interests of India;
- Justice (when it shocks the conscience of the Court) or Morality (primarily limited to sexual immorality contained under Section 23 of the Indian Contracts Act);
- Patent illegality affecting the root of the matter; and
- Making of the award induced by means of fraud or corruption.

45 Arbitration and Conciliation Act 1996 § 5.
46 Associate Builders v. Delhi Development Authority, AIR 2015 SC 620, ¶12.

Upon establishing the grounds for challenge of an award under Section 34 of the Act, the Court further added that it did not sit in appeal over the arbitrator's decision while applying the Public Policy doctrine and restrained itself from interfering with a 'possible view' of the arbitrator, even if the evidence was scanty or not as per legally prescribed standards.[47]

*Judicial flip-flop on application of Public Policy to Foreign Awards*

The Supreme Court in *Hindustan Zinc*[48] observed that even the enforcement of an arbitral award made under Section 48 of the Act (Part II) could be resisted on grounds of illegality of the Contract or the award itself being against the terms of the Contract. After its ruling in *Venture Global Engineering*[49] holding that a foreign award can even be challenged under Part I of the Act (Section 34), the broad view of the Public Policy doctrine as enunciated in *Saw Pipes* (supra) became applicable to the enforcement of foreign awards. It would however be pertinent to note that *Venture Global* was subsequently overruled by the Court's decision in *BALCO,*[50] although the application of BALCO was deemed to be prospective, i.e. to Arbitration agreements entered into post 6 September 2012. This view was further strengthened by another ruling of the Apex Court in *Phulchand Exports*[51] where the Court observed that the term public policy appearing in Section 48(2)(b) of the Act was similar to the expression used in Section 34 of the Act. Thus, the broad standard of review of domestic arbitral awards on grounds of Public Policy under Part I of the Act was read into enforcement of a foreign arbitral award under Part II of the Act as well.

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47 *Id.* at ¶32 – 34 & 52.
48 Hindustan Zinc Ltd. v. Friends Coal Carbonisation, (2006) 4 SCC 445, ¶14.
49 Venture Global Engg. v. Satyam Computer Services Ltd, (2008) 4 SCC 190.
50 Bharat Aluminium v. Kaiser Aluminium, (2012) 9 SCC 552.
51 Phulchand Exports Limited v. O.O.O. Patriot, (2011) 10 SCC 300, ¶16.

The Supreme Court however indulged in a course correction of sorts through its ruling in *Shri Lal Mahal*[52] by admitting its error in its previous rulings and recognized the different standards applicable for the enforcement of Awards under Part I and Part II of the Act. The Court held that Public Policy under Section 48 of the Act needed to be given a restricted meaning, as in *Renusagar* and precluded the implication of patent illegality as a ground of Public Policy as observed in *Saw Pipes*. It deviated from its position in *Venture Global* and *Phulchand Exports* and held that an 'error' in a foreign award did not constitute a violation of Public Policy. Therefore, the broad interpretation given to the term 'fundamental policy of Indian Law' in *Western Geco* would not apply to a Part II arbitration, even though the expression 'in conflict with the public policy of India' finds mention in both Part I and Part II of the Act.

## IV. The 2015 Amendments to the Arbitration Act

The amendment to the 1996 Act introduced in 2015 solidified the narrow approach to the Public Policy doctrine for both a challenge to an arbitral award under Section 34 (Part I) of the Act and the enforcement of a foreign award under Section 48 (Part II) of the Act. Sections 34(2) and 48(2) carry an explanation appended to them, stating that an award would be deemed to be against Public Policy only if:

- The making of the award was induced or affected by fraud or corruption or was in violation of Section 75 or 81;
- It is in contravention with the fundamental policy of Indian law; or
- It is in conflict with the most basic notions of morality or justice.

[52] Shri Lal Mahal v. Progetto Grana Spa, (2014) 2 SCC 433.

In the case of domestic arbitration i.e. an India-seated arbitration between two Indian parties, Sub Section 2A to Section 34 was inserted to permit review of an award on the grounds of 'patent illegality appearing on the face of the award'. However, the provision of patent illegality (which in itself is a clear reference to *Saw Pipes*) introduced under Section 34 has now been qualified by the following safeguards:

- The patent illegality firstly must be 'on the face of the award' – meaning that an issue of law cannot be re-determined or extrapolated by the Courts and the illegality must flow expressly from the award; the Courts cannot imply or infer the illegality of an Award.
- Re-appreciation or reinterpretation of an issue of law has been strictly barred vide the *proviso* to Section 34 prohibiting the setting aside of an award merely on the ground of an 'erroneous application of the law'.

The Supreme Court, however, in a clarificatory ruling[53] dispelled all doubts regarding the interpretation of the Public Policy doctrine under the amended regime, holding that the 2015 amendments have done away with the position of law as enunciated in *Saw Pipes* and *Western Geco* and that *both sections 34 and 48 have been brought back to the position of law in Renusagar* (the narrow view).

## V. Recent Judicial Trends

Recent judgements have used the doctrine of public policy to settle, or at least try to settle, the issue of two Indian Parties choosing a foreign seat of arbitration. After *BALCO* and *Reliance Industries*,[54] the Supreme Court in *Sasan Power Ltd. vs. North*

[53] HRD Corporation (Marcus Oil and Chemical Division) v. Gail (India) Limited (formerly Gas Authority of India Ltd.), 2017 SCC OnLine SC 1024.

[54] Reliance Industries v. Union of India (2014) 7 SCC 603.

*American Coal Corporation India Pvt. Ltd,*[55] got the opportunity to settle the issue of seat of arbitration between two parties domiciled in India, and whether such foreign seated arbitration is contrary to the Public Policy of India. However, the Court did not conclusively decide on the issue even though the Madhya Pradesh High Court[56] dealt with the said issue, before it came up in appeal to the Supreme Court. The Madhya Pradesh High Court in *Sasan*, under section 45 of the Act, refused to rely on the decision of the Supreme Court in *TDM Infrastructure (P) Ltd. vs. UE Development India (P)*,[57] and the Bombay High Court in *Addhar Mercantile Private Limited vs. Shree Jagdamba Agrico Exports Pvt. Ltd*,[58] and instead relied on *Atlas Export Industries vs. Kotak & Company*.[59]

In *TDM Infrastructure*[60] and *Addhar Mercantile*[61], the Supreme Court of India, and the High Court of Bombay respectively, held that two Indian parties cannot be permitted to choose a foreign seat of arbitration as it would essentially lead to a departure from Indian law and would be in contravention of the public policy of India. However, in *Atlas Export*, a division bench of the Supreme Court of India, adjudicating under the erstwhile 1940 Act, held that when the parties have willingly agreed to enter into an arbitration agreement and designated a foreign seat of arbitration, the agreement *ipso facto* does not become void for contravening Public Policy.[62] The Madhya Pradesh High Court, concurring with the position taken in *Atlas Export* held that merely because

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55 Sasan Power Ltd. v. North American Coal Corporation India Pvt. Ltd, (2016) 10 SCC 813.

56 Sasan Power Ltd. v. North American Coal Corporation India Pvt. Ltd, 2015 SCC Online M.P. 7417.

57 TDM Infrastructure (P) Ltd. v. UE Development India (P), (2008) 14 SCC 271.

58 Addhar Mercantile Private Limited v Shree Jagdamba Agrico Exports Pvt. Ltd, 2015 SCC OnLine Bom 7752.

59 Atlas Export Industries v. Kotak & Company, (1999) 7 SCC 61.

60 *TDM Infrastructure*, (2008) 14 SCC 271 ¶23.

61 *Addhar Mercantile*, 2015 SCC OnLine Bom 7752 ¶8.

62 *Atlas Export*, (1999) 7 SCC 61, ¶10 & 11.

two Indian companies have entered into an arbitration agreement which was to be held in a foreign country cannot by itself be enough to nullify the arbitration agreement, since it does not contravene the Public Policy of India.[63] Therefore, Indian parties are free to arbitrate outside India and an award rendered in this process would be governed by Part II of the Act.

Interestingly when the matter came to the Supreme Court of India, it held that the issue of whether two nationals can be governed by a foreign arbitration does not arise and proceeded to decide the case on the nature of the agreement between the parties.[64] The court held that since the dispute has a *foreign element* present in it, the Indian nationals can be allowed to have a foreign seated arbitration.[65] The Court also held that even if an arbitration agreement is inconsistent with Section 23 of the Indian Contract Act, as being contrary to public policy, it only affects the legality of the substantive contract. It does not invalidate an arbitration agreement which is independent and severable from the underlying contract.[66]

Similarly, the Delhi High Court recently in *GMR Energy Limited vs. Doosan Power Systems India Private Limited and Ors*,[67] also referred to the judgments in *Sasan Power* and *Atlas Export* and held that two Indian parties selecting a foreign seat of arbitration does not contravene public policy. The court held that since an arbitration agreement is an independent agreement which is not dependent on the substantive agreement, the parties were therefore entitled

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63 Sasan Power Ltd. v. North American Coal Corporation India Pvt. Ltd, 2015 SCC Online M.P. 7417 ¶52.

64 Sasan Power Ltd. v. North American Coal Corporation India Pvt. Ltd, (2016) 10 SCC 813 ¶28 & 29.

65 *Id.* at ¶29.

66 *Id.* at ¶50.

67 GMR Energy Limited v. Doosan Power Systems India Private Limited and Ors, 2017 SCC OnLine Del 11625 ¶31.

to choose a foreign seat of arbitration, regardless of the contractual rights and obligations of the parties.

It would also be apposite to note at this point in time that *Venture Global* which was set aside by *BALCO* was recently agitated again before the Supreme Court upon additional facts being brought on record by the parties to the dispute. In a division bench judgment of the Supreme Court[68] where dissenting views were given by Justice Chelameswar and Justice Sapre, the matter has since been referred to a larger bench for adjudication. Interestingly, Justice Chelameswar in paragraph 127 of the judgment observes as follows:

> *"The award of an arbitral tribunal can be set aside only on the grounds specified in Section 34 of the AAC Act and no other ground. The Court cannot act as an Appellate Court to examine the legality of Award nor can it examine the merits of the claim by entering the factual arena like an Appellate Court…"*

A similar view was also expressed in *Sutlej Construction vs. The Union Territory of Chandigarh.*[69] However, this view seems to be far from being settled, as the Supreme Court of India in *Vedanta Limited vs. Shenzen Shandong Nuclear Power*[70] under Section 34 of the Act, revised the award given by the arbitral tribunal. The Supreme Court of India in the Shenzen case, modified the interest rate given by the arbitral tribunal as the same was held to be, "*arbitrary, exorbitant and had no correlation with the contemporary international rate of interests"*. However, while revising the award, the Supreme Court of India did not elaborate on why the Court was justified to interfere in the award or how such award suffers from patent illegality or was against the public policy of India. Interestingly

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68 Venture Global Engineering LLC and Ors v. Tech Mahindra Ltd and Ors, (2017) 13 SCALE 91 (SC).

69 Sutlej Construction v. The Union Territory of Chandigarh, (2017) 14 SCALE 240 (SC).

70 Vedanta Limited v Shenzen Shandong Nuclear Power, 2018 SCC Online SC 1922.

before the appeal was made to the Supreme Court of India, the Delhi High Court refused to interfere with the award as it did not satisfy the test of patent illegality enumerated in Section 34 of the Act.[71]

The recent judicial trend suggests therefore that when Indian parties have willingly entered into a foreign seated agreement, it cannot be by itself held to be contrary to the public policy. This is of particular practical significance to multi-national corporations who may contract through an Indian subsidiary, but are in essence, controlled and managed by a foreign entity. Therefore, the strict approach of determining the nature of the arbitration based purely on the country of incorporation[72] poses further issues in adopting a strict view of the issue of whether two Indian parties may select a foreign seat.

## VI. Conclusion

The interpretation of the Public Policy Doctrine in Arbitration has undergone severe scrutiny in recent times and in the absence of a statutory definition of the same, the Courts have upended the legislative process of defining the contours of the doctrine, often leading to conflicting and contradictory positions on the same. In certain instances, as has been noted above, mere infractions of Indian Laws have been held to violate Public Policy while the introduction of the 'patent illegality' principle has allowed the Courts to sit in appeal over the Arbitrator's decision.

Resolution of disputes through Arbitration primarily hinges on the principle of minimal judicial intervention. Moving forward, to ensure that India becomes a global hub of arbitration in the world, the doctrine of public policy needs to be given a restrictive meaning and more importantly needs to be properly delineated in

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71 Vedanta Limited v Shenzen Shandong Nuclear Power, 2018 SCC Online Del 10916.

72 Arbitration and Conciliation Act 1996 § 2(1)(f).

reference to its width and scope. While the recent judicial trend points to an increasingly restrictive and narrow scope of Public Policy being given effect to by the Courts, the need of the hour is in statutorily defining the contours of Public Policy to ensure that the lacuna and vacuum that currently exists in our Statute books in reference to the same does not come in the way of prospective investors and litigants from carrying out their business with ease under India's robust economic climate, or seating their arbitrations in India.