ELP Arbitration: Update

HIGH COURT HOLDS THAT SUBJECT ARBITRAL AWARDS SUFFER FROM THE VICE OF PERVERSITY. SUPREME COURT CONFIRMS THAT THE SUBJECT AWARDS WERE VITIATED BY "PATENT ILLEGALITY".

PATEL ENGINEERING LTD. V. NORTH EASTERN ELECTRIC POWER CORPORATION LTD. (NEEPCO)[1] (MAY 22, 2020)

FACTUAL BACKGROUND

- The grounds to challenge an arbitral award are set out in section 34 of the Arbitration and Conciliation Act, 1996 (**Act**). Amongst the grounds, public policy has always been a source of much consternation especially when the same was interpreted expansively by the judiciary in India. In 2015, the Act was amended by the Arbitration and Conciliation (Amendment) Act, 2015 (**2015 Amendment Act**). Amongst other changes, the 2015 Amendment Act introduced sub-section (2-A) in section 34 of the Act which provides that - an award arising out of an arbitration between purely domestic parties, may be set aside by the court if the court finds that the award is vitiated by "patent illegality" appearing on the face of the award. The proviso to sub-section (2-A) clarifies that an award shall not be set aside merely on the ground of erroneous application of the law or by re-appreciation of evidence.
- In the present case, the Supreme Court upheld the decision of the High Court setting aside the arbitral awards on the said ground of "patent illegality".

FACTS

Applications challenging the arbitral award under section 34 of the Act

[1] SPECIAL LEAVE PETITION (C) NOS. 3584-85 OF 2020 (Arising out of SLP(C) D No. 577 of 2020) With SPECIAL LEAVE PETITION (C) NOS. 3438-3439 OF 2020 (Arising out of SLP(C) D No. 593 of 2020) SPECIAL LEAVE PETITION (C) NOS. 3434-3435 OF 2020 (Arising out of SLP(C) D No.595 of 2020)

In the disputes between North Eastern Electric Power Corporation Ltd. (**NEEPCO**) and Patel Engineering Ltd. (**PEL**), the Ld. Sole Arbitrator passed three Arbitral Awards dated 29 March 2016, in respect of three contracts (collectively referred to as **Awards**).

Aggrieved by the Awards, NEEPCO filed three applications under section 34 of the Act (collectively referred to as **Section 34 Applications**) before the Ld. Additional Deputy Commissioner (Judicial), Shillong (**ADJ**). By a common order dated 27 April 2018 (**ADJ Order**), the Section 34 Applications were dismissed and the ADJ upheld the Awards.

Appeals under section 37 of the Act

NEEPCO filed three applications under section 37 of the Act (**Section 37 Applications**), challenging the ADJ Order before the High Court of Meghalaya at Shillong (**High Court**). By a common judgment dated February 26, 2019, the High Court *inter alia* observed that the Awards suffered from the vice of irrationality and perversity. The High Court allowed the Section 37 Applications, set aside the ADJ Order, and set aside the Awards (**Section 37 Judgment**).

SLP before Supreme Court

While PEL preferred special leave petitions before the Supreme Court against the Section 37 Judgment, the same were dismissed under a non-speaking order dated July 19, 2019 (**SC Order**).

Review Petition before the High Court

Thereafter, PEL filed Review Petitions (**Review Petitions**) before the High Court. Through the Review Petitions, PEL contended that the Section 37 Judgment suffered from error apparent on the face of the record inasmuch as it failed to consider the amendments made by the 2015 Amendment Act and that the High Court had erroneously applied precedents which were no longer good law. By an order dated October 10, 2019, the High Court dismissed the Review Petitions (**Order**) and held in favor of NEEPCO.

Aggrieved by the dismissal of the Review Petitions, PEL preferred three Special Leave Petitions (**SLPs**) before the Supreme Court arising from the Order.

OBSERVATIONS AND FINDINGS

Maintainability of the Review Petitions before the High Court

At the threshold, NEEPCO submitted that the SLPs against the Order were not maintainable.

Relying upon *Bussa Overseas*[2] and *Durga Shankar Mehta*[3], PEL submitted that although Order 47 Rule 7 of the Code of Civil Procedure,1908 (**CPC**) bars an appeal against the order of the court rejecting the review, this does not curtail the plenary jurisdiction under Article 136 of the Constitution of India by taking recourse to the provisions in the CPC. PEL further submitted that the SC Order was a non-speaking order and hence the Review Petitions were tenable and ipso facto, the SLPs were maintainable.

Rebutting this, NEEPCO submitted that the Supreme Court heard the matter at length before passing the SC Order. Further, while the SC Order is a non-speaking order, PEL had raised all the issues therein and cannot be allowed to reagitate the matter by filing a review petition.

After hearing both parties, the Supreme Court held that it was not necessary to explore the question of maintainability of the SLPs preferred against the Order.

Section 34 of the Act, as amended by the 2015 Amendment Act applies to the present case

PEL contended that the Section 37 Judgment suffered from error apparent on the face of the record since (i) the High Court in the Section 37 Judgment erroneously applied the provisions as applicable prior to the Amendment Act, 2015 and (ii) relied upon the decisions in *Saw Pipes Ltd.*[4] and *Western Geco*[5], which are no longer good law after the 2015

[2] *Bussa Overseas and Properties Private Limited and Another v. Union of India and Another,* (2016) 4 SCC 696
[3] *Durga Shankar Mehta v. Thakur Raghuraj Singh and Others,* (1955) 1 SCR 267
[4] *Oil & Natural Gas Corporation Ltd. v. Saw Pipes Ltd.* (2003) 5 SCC 705
[5] *Oil & Natural Gas Corporation Ltd. v. Western Geco International Limited*, (2014) 9 SCC 263

Amendment Act. Relying upon *HRD Corporation*[6] and *Ssangyong Engineering*[7], PEL submitted that there was an error on the face of the record and therefore, the Review Petitions were justified.

The Supreme Court observed that pursuant to *BCCI*[8], in Section 34 petitions that are filed after October 23, 2015 i.e. date on which the 2015 Amendment Act came into force, the 2015 Amendment Act would apply. In the present case, admittedly, the Awards were dated March 29, 2016 and the Section 34 Applications were filed after the 2015 Amendment Act. Therefore, the provisions of the 2015 Amendment Act would apply to the present case.

The Awards were vitiated by Patent Illegality

With reference to the ground of "patent illegality", the Supreme Court traced the jurisprudence on the interpretation of patent illegality.

Prior to the 2015 Amendment Act, in the context of a domestic award, in *Saw Pipes,* the Supreme Court had extended a wider interpretation to the 'public policy of India' in section 34(2)(b)(ii) in Part I of the Act and introduced the ground of "patent illegality" for setting aside an award. In *Saw Pipes*, the Supreme Court held that an award would be "patently illegal" if it is contrary to - the substantive provisions of law; or the provisions of the Act; or the terms of the contract.

Thereafter, in *Western Geco*, the Supreme Court further expanded public policy to include (i) fidelity in judicial approach to the determination, (ii) adherence to principles of natural justice and (iii) the award cannot be perverse and irrational.

In *Associate Builders*[9], the Supreme Court observed that "patent illegality" was now a fourth head created under the ground of public policy and which, in an applicable case, could result in the setting aside of an award.

As there was a lot of criticism on the ever-expanding scope of public policy, the Law Commission in its 246th Report[10] recommended a narrower approach to the phrase. Distinguishing between international commercial arbitrations seated in India and arbitrations between purely domestic parties, the Law Commission recommended the insertion of the ground of "patent illegality" for setting aside an award arising out of an arbitration between purely domestic parties. This was given effect to through the insertion of clause (2A) in Section 34 of the Act.

Following the 2015 Amendment Act, in *Ssangyong Engineering*, an award in an international commercial arbitration seated in India was challenged before the Supreme Court. In the said case, the Supreme Court noted that –

- The expansive interpretation given to "public policy of India" in the *Saw Pipes* and *Western Geco* cases had been done away with although the principle of natural justice was retained,
- Inasmuch as awards between purely domestic parties are concerned, an additional ground of "patent illegality" was now available under sub-section (2A) to Section 34. However, re- appreciation of evidence was not permitted under the ground of "patent illegality" appearing on the face of the award;
- The ground of "patent illegality" was only available for all challenges filed after the coming into force of the 2015 Amendment Act;
- As held in *Associate Builders*, the construction of the terms of a contract is primarily for an arbitrator to decide, unless the arbitrator construes a contract in a manner which no fair minded or reasonable person would take i.e. if the view taken by the arbitrator is not even a possible view to take.
- "patent illegality" would include a perverse and irrational decision.

Examining the case at hand, and the jurisprudence as developed over time, the Supreme Court stated that the present case arose out of a domestic award between two Indian entities. Hence, the ground of patent illegality was a ground available under the statute for setting aside a domestic award. If the decision of the arbitrator is found to be perverse, or, so irrational that no reasonable person would have arrived at the same; or, the construction of the contract is such that no fair or reasonable person would take; or, that the view of the arbitrator is not even a possible view, the award would be set aside.

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[6] *HRD Corporation (Marcus Oil and Chemical Division) v. GAIL (India) Limted,* (2018) 12 SCC 471
[7] *Ssangyong Engineering and Construction Company Limited v. National Highways Authority of India,* (NHAI) (2019) 15 SCC 131
[8] *Board of Control for Cricket in India v. Kochi Cricket Private Limited and Others* (2018) 6 SCC 287
[9] *Associate Builders v. Delhi Development Authority,* (2015) 3 SCC 49.
[10] Available at : http://lawcommissionofindia.nic.in/reports/Report246.pdf

Examining the Section 37 Judgment, the Supreme Court observed that the High Court had held that no reasonable person could have arrived at a different conclusion while interpreting the subject clauses of the contracts, and that any other interpretation of the above clauses would definitely be irrational and in defiance of all logic. The Supreme Court agreed with the High Court's conclusion that the findings in the Awards suffered from the vice of irrationality and perversity.

The Supreme Court cautioned that although the High Court in the Section 37 Judgment referred to *Western Geco,* which is no longer good law, the High Court's conclusion had been reached by applying the reasoning that the Awards were perverse and on a holistic reading of all the terms and conditions of the contract, the view taken by the arbitrator was not a possible view. The High Court rightly followed *Associate Builders*, which was reiterated in *Ssangyong Engineering* and hence the High Court was correct in its conclusion.

CONCLUSION AND ANALYSIS

The Supreme Court held that the matter could not be re-opened by filing Review Petitions on the same grounds, which have been rightly dismissed by the High Court under the Section 37 Judgment. PEL failed to make out any error on the face of the Section 37 Judgment. Accordingly, the Supreme Court held that the High Court by the impugned Order rightly dismissed the Review Petitions and there was no ground for interference. Based on the foregoing, the SLPs were dismissed with no order as to costs.

The vast and varying interpretations of public policy as a ground for setting aside an award has always been a cause of concern for stakeholders in arbitration. The Law Commission did attempt to constrict the same. Further, for international commercial arbitrations seated in India, it carved out an exception by allowing "patent illegality" to be utilized as a ground for setting aside an award between purely domestic parties. Such ground was further circumscribed by preventing reappreciation of evidence by the setting aside court, and specifying that erroneous application was law by itself not sufficient to constitute "patent illegality".

While the Supreme Court has reiterated the fact that the ground of "patent illegality" is available only for awards between purely domestic parties, and that too only for all challenge petitions filed after the coming into force of the 2015 Amendment Act, it has not delved into what constitutes reappreciation of evidence and the bounds within which the court must operate while determining whether the award can be set aside under such a ground. A brewing cause of concern therefore is that will courts be enabled to review the ground of patent illegality on the face of the award while steering clear of an exercise of re-appreciation of evidence? This is a complicated question which needs to be addressed urgently. Our experience indicates that in a challenge to an award, invariably, the award debtor seeks a reappreciation of evidence under some or the other guise.

In India, the Act permits a challenge to the award under section 34, a round of appeal under section 37, but no further appeal thereafter. An SLP to the Supreme Court under Article 136 of the Constitution is however maintainable. In the present case, the award went through the section 34 challenge, the appeal under section 37 and an SLP under Article 136 of the Constitution. Thereafter, a review was filed before the section 37 court and then again an SLP was filed from the order rejecting the review. This gives rise to several questions, one of which is whether a review is at all maintainable against the order of a court in a section 37 proceeding. Secondly, if such review is permissible, whether an SLP from an order rejecting the review petition is at all permissible, more so when the scope of the SLP is limited to the order rejecting the review petition and not the order impugned in the review petition. The Supreme Court did not delve into these issues. Instead it went on to assess the order which set aside the award, i.e. the order in a section 37 proceeding, when such order had already been assailed in a separate, prior SLP and not been overturned. To assess whether the Order was correct inasmuch as it rejected the Review Petitions, the Supreme Court in effect held that the SLPs were maintainable and determined whether there was an error apparent on the face of the Section 37 Judgment.

In the past two months, the Supreme Court has set aside domestic awards and refused enforcement of foreign awards. In *South East Asia*[11]*,* the Supreme Court *inter alia* held that the interpretation of the contract by the tribunal therein was not a possible interpretation, and hence the award was set aside. In a petition seeking enforcement of a foreign award in

[11] *South East Asia Marine Engineering & Constructions Ltd. (SEAMEC Ltd.) v. Oil India Limited*, dated May 11, 2020 in Civil Appeal No. 673 of 2012.

NAFED[12], the Supreme Court held that enforcement of the award would be violative of the public policy of India and the award was rendered unenforceable.

Since the 2015 Amendment Act, the courts in India had adopted a policy of minimal interference with arbitral awards unless a high benchmark warranting interference had been satisfied. In fact, the judicial trends indicated that courts were aligning by a pro-arbitration approach. However, the recent string of decisions may trigger an unfavorable alarm i.e. are we now deviating from the legislature's endeavor to promote India on the map as an arbitration friendly jurisdiction?

[12] *National Agricultural Cooperative Marketing Federation of India v. Alimenta S.A.,* 2020 SCC OnLine SC 381