

THE TEST OF PATENT ILLEGALITY

The term "**patent illegality**" was explained in detail and brought within the scope of *public policy of India* for the first time by the Apex Court in *ONGC Vs. SAW Pipes* [(2003) 5 SCC 705]. However with the amendments to Section 34 of the Arbitration & Conciliation Act, 1996 (*hereinafter referred to as the said Act*), made by the Arbitration and Conciliation Amendment Act, 2015, with effect from 23rd October, 2015, the expansion of the term *public policy of India* as interpreted by Courts previously has been done away with. The Law Commission examined and submitted its 246th Report on "Amendments to the Arbitration and Conciliation Act, 1996" in August, 2014 and recommended various amendments in the said Act. The proposed amendments were intended to facilitate and encourage Alternative Dispute Mechanism, especially arbitration, for settlement of disputes in a more user-friendly, cost effective and expeditious disposal of cases since India is committed to improve its legal framework to obviate in disposal of cases. The 246th Report of the Law Commission recommended considerable changes to Section 34 of the said Act. The 246th Law Commission Report proposed amendments to the said Act, narrowing down the grounds of challenge the Arbitral Award, apart from providing for appointment of independent, impartial and neutral arbitrators, amongst several other amendments. The judgment in *ONGC's case* stated supra along with the judgment in *ONGC v. Western Geco International Ltd.* (2014) 9 SCC 263 : (AIR 2015 SC 363) has been expressly done away with. Both Sections 34 and 48 of the said Act have been brought back to the position of law contained in *Renusagar Power Plant Co. Ltd. v. General Electric Co.* (1994) Supp (1) SCC 644 : (AIR 1994 SC 860), where "public policy" will now include only two of the three grounds set out therein, i.e., "*fundamental policy of Indian law*" and "*justice or morality*" in addition to *the ground where making of the award was induced or affected by fraud or corruption or was in violation of Section 75 or Section 81 as provided in Section 34 of the*



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amended Act . The ground relating to "the interest of India" stated in the said Judgment is no longer available as valid ground. "Fundamental policy of Indian law" is now to be understood as laid down in *Renusagar (supra)*. Meaning of "Justice or morality" has been tightened and is now to be understood as only basic notions of justice and morality i.e., such notions as would shock the conscience of the Court as understood in *Associate Builders v. Delhi Development Authority (2015) 3 SCC 49 : (AIR 2015 SC 620)*. The main object of the amendment of 2015 is to speed up the arbitration process and to minimize the intervention of the Courts which would ultimately ease doing business in India.

By the amendment of 2015, Explanation as appearing in clause (b) in sub-section (2) of Section 34 of the said Act has been substituted by the new Explanations and Sub-Section 2A has been inserted in Section 34 of the said Act. Amended clause (b) (ii) of Section 34 (2) reads as follow :

“(ii) the arbitral award is in conflict with the public policy of India.

Explanation 1.—For the avoidance of any doubt, it is clarified that an award is in conflict with the public policy of India, only if,—

- (i) the making of the award was induced or affected by fraud or corruption or was in violation of section 75 or section 81; or***
- (ii) it is in contravention with the fundamental policy of Indian law; or***
- (iii) it is in conflict with the most basic notions of morality or justice.***

Explanation 2.—For the avoidance of doubt, the test as to whether there is a contravention with the fundamental policy of Indian law shall not entail a review on the merits of the dispute.”

Newly inserted sub-Section 2A read as follow;

“(2A) An arbitral award arising out of arbitrations other than international commercial arbitrations, may also 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.

Provided that an award shall not be set aside merely on the ground of an erroneous application of the law or by reappreciating evidence.”

Amendment of 2015 clearly defines the term *public policy of India* and has introduced a new ground, namely Section 34(2A) for setting aside domestic arbitral awards on the ground of patent illegality but the term patent illegality has not been defined. This ground will be applicable only to arbitrations taking place in India and not to International Commercial Arbitrations as can be make out from the wording of the section which says “other than International commercial arbitration”.

The Apex Court in the case of ***Ssangyong Engineering & Construction Co. Ltd. Vs. National Highways Authority of India (NHAI)*** (AIR 2019 SC 5041) has exhaustively dealt with the expression *patent illegality* and which acts of the Arbitral Tribunal would come within the purview of *patent illegality*. It is made clear by virtue of the amendment of 2015 as well as the Apex Court that the said expression can no longer form a part of the elaborated definition of public policy given by the Courts previously.

The Apex Court in Ssangyong Engineering's case stated supra has held that the additional ground made available for setting aside a domestic arbitral award under Sub-section (2A), added by the Amendment Act, 2015, to Section 34, refers to such illegality as goes to the root of the matter but which does not amount to mere erroneous application of the law. For the sake of clarity, the Court has held that the contravention of a statute not linked to public policy or public interest, which is not subsumed within *the fundamental policy of Indian law* cannot be brought in by the backdoor when it comes to setting aside an award on the ground of patent illegality.

It is clear from the amendment of 2015 that re-appreciation of evidence, which is what an appellate court is permitted to do, cannot be permitted under the ground of patent illegality appearing on the face of the award.

Previously, the Apex Court in the case of Associated Builders had held that "Patent Illegality" would include: a) fraud or corruption; b) contravention of substantive law, which goes to the root of the matter; c) error of law by the arbitrator; d) contravention of the Act itself; e) where the arbitrator fails to consider the terms of the contract and usages of the trade as required under Section 28(3) of the said Act; and f) if arbitrator does not give reasons for his decision. The Apex Court in Ssangyong Engineering's case stated supra has relied upon the findings given in the case of *Associate Builders referred to supra, to some extent* and has held that if an arbitrator gives no reasons for an award and contravenes Section 31(3) of the said Act, that would certainly amount to a patent illegality on the face of the award.

The Court further relying upon the said judgement has held that a finding based on no evidence at all or an award which ignores vital evidence in arriving at its decision would be perverse and liable to be set aside on the ground of patent illegality. Additionally, a finding based on documents taken behind the back of the parties by the arbitrator would also qualify as a decision based on no evidence inasmuch as such decision is not based on evidence led by the parties, and therefore, would also have to be characterised as perverse.

As it appears to be obvious from language of Section 34 (2A) the Apex Court in Ssangyong Engineering's case stated supra has also stated that the ground of *patent illegality* under Section 34(2A) of the said Act, would not be available in the case of an international

commercial arbitration. The aforesaid aspects are a bird's view of the Apex Court's decision in Ssangyong Engineering's case in so far as the applicability of *patent illegality* is concerned.

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