
# THE INDIAN ARBITRATION LAW: TOWARDS A NEW JURISPRUDENCE

SUMEET KACHWAHA*

*Appointments; Awards; Commercial arbitration; Default powers; Grounds for appeal; India; Public policy*

India opened a fresh chapter in its law of arbitration by enacting a legislation based on the UNCITRAL Model Law 1985 and the UNCITRAL Rules 1976. The Arbitration and Conciliation Act (the Act) came into force in January 1996.[1]

The theme of this article is to explore the emerging jurisprudence in Indian arbitration law, essentially as a result of recent judicial pronouncements.

## Background to the Indian Act

The Statement of Objects and Reasons to the Act declared in a forthright manner that the earlier Arbitration Act (of 1940) had "become outdated" and there was need to have an Act, "more responsive to contemporary requirements". It added: "Our economic reforms may not become fully effective if the law dealing with settlement of both domestic and international commercial disputes remains out of tune."

Among the main objectives of the new Act (set out in the Statement of Objects and Reasons) are "to minimize the supervisory role of courts in the arbitral process" and "to provide that every final arbitral award is enforced in the same manner as if it were a decree of the Court".

## The problem of delay

The Indian legal system is riddled with delays. Much has been written on the subject. There are about 3.4 million cases pending between the 21 High Courts of India, out of which about 0.65 million have been pending for over 10 years. Over 23 million cases are pending in other courts.[2] There are only 10.5 judges per million persons. The corresponding figure in the United Kingdom is 50.9, Australia 57.7, Canada 75.2 and the United States 107.[3]

## Pillars of the Act

Given this state of affairs a central approach of the Act is to keep the arbitral process free from court intervention. Indeed the Act contemplates only three situations where a judicial authority may intervene in arbitral proceedings. These are (1) appointment of arbitrators—where the parties envisaged method for the same fails (s.11); (2) ruling on whether the mandate of the arbitrator stands terminated owing to inability to perform his functions or failure to proceed without undue delay (s.14(2)); and (3) provide assistance in taking evidence (s.27). As would be noticed, compared with the Model Law, the Indian Law is far more restrictive in allowing court intervention.

This may be elaborated further:

Section 5 of the Act provides, through a non-obstante clause, that no judicial authority shall interfere except where so provided for.

Section 8 is a companion section. It states that a judicial authority before which an action is brought in a matter which is the subject-matter of an arbitration agreement shall refer the parties to arbitration. The only condition being that the party objecting to the court proceedings must do so no later than his first statement on the substance of the dispute. In the meanwhile, the arbitration proceedings may commence and continue with and an award rendered.

Two points are noteworthy. The first is that s.5 (departing from the Model Law) contains a non-obstante clause. Section 8 also departs from the Model Law. The corresponding provision in the Model Law (Art.8) permits the court to entertain an objection to the effect that the arbitration agreement is "null and void inoperative or incapable of being performed". These words have been omitted in s.8 of the Act. The departure is deliberate

*B.A (Hons) English Literature; LL.B—University of Delhi (1979); Partner—Kachwaha & Partners. Mr Kachwaha has been nominated as a "Highly Recommended Dispute Resolution Practitioner in India" by Global Counsel 3000 and as a "Leading Individual" by Asia Pacific Legal 500 for Dispute Resolution. Mr Kachwaha is a Co-Vice Chair of the Dispute Resolution Section of the Inter Pacific Bar Association. He is thankful to Mr. Fali S. Nariman for reviewing the draft of this article (though the views expressed herein are his own).

1. Full text of the Act available at *www.kaplegal.com.*

2. Figures furnished by the Minister of Law in Parliament in response to a question on July 9, 2004.

3. From the speech of the Chief Justice of India in December 2005 on the occasion of the Law Day.

as would be evident if s.8 is compared with s.45 of the Act which covers the same subject for offshore arbitrations. Section 45 (in contrast) states that a judicial authority when seised of an action in respect of which the parties have an arbitration agreement, shall refer the parties to arbitration—"unless it finds that the said agreement is null and void inoperative or incapable of being performed".

Hence the Indian Act empowers a judicial authority to entertain objections as to the validity or otherwise of an arbitration agreement in the case of offshore arbitrations but in the case of onshore or domestic arbitrations it is deleted.

Section 16 of the Act (corresponding to Art.16 of the Model Law) is another key provision of the Act. This section provides that the arbitral tribunal may rule on its own jurisdiction including with respect to the existence or validity of the arbitration agreement. Further, the arbitration clause shall be treated as independent of the underlying contract and a decision that the contract is null and void shall not entail *ipso jure* the invalidity of the arbitration clause. Where the arbitral tribunal rejects an objection to its jurisdiction, it shall continue with the arbitral proceedings and make the award. Any challenge to the award would be available at that stage. If, on the other hand, the arbitral tribunal accepts the plea as to its lack of jurisdiction, an appeal shall lie to a court of law. This provision again marks a significant departure from the Model Law which contemplates recourse to a court from a decision of the arbitral tribunal rejecting a challenge to its jurisdiction also.[4]

The Indian legislature's keenness to keep the courts out of the arbitral process thus becomes evident with every step of the legislation.

Given the delays plaguing the legal system, it would seem that the two fundamental pillars of the Act are ss.8 and 16. Any dilution of these provisions would lead to unscrupulous litigants taking advantage and enmeshing the parties in never-ending frustrating court procedures.

## Two judgments

Two judgments of the Supreme Court of India have shaken the foundation of the law as it existed till recently. These are *ONGC v Saw Pipes*[5]—a decision of a bench of two Hon. Judges, and *S.B.P & Co v Patel Engineering*[6]—a decision of a bench of seven Hon. Judges, with a dissent.

### *The Saw Pipes case*

Following the Model Law the Indian Act provides for a limited recourse to challenge against an arbitral award. The grounds on which a domestic award can be challenged are set forth in s.34 of the Act which is based on Art.34 of the Model Law.[7] To paraphrase, an award can be set aside only if:

(1) the party making the application was under some incapacity; or
(2) the arbitration agreement was not valid under the law agreed to by the parties (or applicable law); or
(3) the party making the application was not given proper notice of the appointment of the arbitrator or of the arbitral proceedings or was otherwise unable to present his case; or
(4) the award deals with a dispute not contemplated by or falling within the terms of submissions to arbitration or it contains decisions beyond the scope of the submissions to arbitration; or
(5) the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties; or
(6) the subject-matter of the dispute was not capable of settlement by arbitration; or
(7) the arbitral award is in conflict with the public policy of India.

Section 34 (deviating somewhat from the Model Law) goes on to add an "Explanation" in relation to the ground of public policy to clarify that an award would be in conflict with the public policy of India if the same was affected by fraud or corruption or was in violation of the confidential requirements attached to the conciliation proceedings provisions contained in the Act.

The limited grounds of challenge provided for under s.34 are universally recognised. It is well accepted that the courts have no power to get into the merits of the dispute. However this basic proposition was put to test and suffered a setback in the case of *ONGC v Saw Pipes Ltd* (*Saw Pipes*). Here an award was challenged on the ground that the arbitral tribunal had incorrectly applied the law of the land in rejecting a claim for liquidated damages. The court had thus to decide whether it had jurisdiction under s.34 to set aside an award on the ground that it is "patently illegal, or in contravention of the provisions of the Act, or any other substantive law, governing the parties or is against the terms of the contract".[8]

The Supreme Court in *Saw Pipes* came to the conclusion that the impugned award was legally flawed in so far as it allowed liquidated damages on an incorrect view of the law. In the process it held, as a matter of law (and through judicial lawmaking) that an award can also be challenged on the ground that it contravenes "the provisions of the Act or any other substantive law governing the parties or is against the terms of the contract".[9] Further, the judgment expanded the concept of public policy to add that the award would be contrary to public policy if it is "patently illegal". An earlier Supreme Court decision, of a larger bench, in the case of *Renu Sagar Power Co v General Electric Corp*,[10] had construed the ground of "public policy" narrowly as confined to the "fundamental

4. s.37.
5. 2003 (5) S.C.C. 705.
6. 2005 (9) S.C.A.L.E. 1.
7. Enforcement of a foreign award can be resisted on the New York Convention grounds (s.45).
8. Above fn.5, 713.
9. Above fn.5, 744–745.
10. [1994] Suppl. S.C.C. 644.

policy of Indian law or the interest of India or justice or morality". The Supreme Court in *Saw Pipes* distinguished *Renu Sagar* on the ground that the said judgment was in the context of a foreign award. The reason given was that in foreign arbitration, the award would be subject to being set aside or suspended by the competent authority under the relevant law of that country, whereas in domestic arbitration there is no such recourse and the award attains finality[11] (thus the need for greater judicial scrutiny).

Hence the *ratio* of *ONGC v Saw Pipes* in so far as the expansion of public policy is concerned would be confined only to domestic awards. The expansion of s.34 to include "patent illegality" may also arguably not apply to foreign awards since this interpretation was premised on certain provisions of the Act applicable to domestic arbitral proceedings alone. Thus foreign awards may be saved from the expanded interpretation of the said judgment.

*ONGC v Saw Pipes* makes a significant dent in the jurisprudence of arbitration in India and has come in for some sharp criticism.

One can do no better than to quote the eminent jurist and lawyer Mr F. S. Nariman who said that the judgment has

> "virtually set at naught the entire Arbitration and Conciliation Act of 1996...
>
> To have introduced—by judicial innovation—a fresh ground of challenge and placed it under the head of 'Public Policy' was first contrary to the established doctrine of precedent—the decision of a bench of three judges being binding on a bench of two judges. It was also contrary to the plain intent of the new 1996 law, namely the need for finality in alternative methods of dispute resolution without court interference.
>
> If courts continue to hold that they have the last word on facts and on law—notwithstanding consensual agreements to refer matters necessarily involving facts and law to adjudication by arbitration—the 1996 Act might as well be scrapped.
>
> The Division Bench decision of the two judges of the court has altered the entire road-map of arbitration law and put the clock back to where we started under the old 1940 Act."[12]

## The Patel Engineering judgment

This judgment of the Supreme Court[13] concerns s.11 of the Act, which provides for court intervention where the parties' envisaged mechanism for constituting the arbitral tribunal breaks down or where no mechanism is provided for and the parties cannot agree upon the same. In such an event s.11 provides that the Chief Justice of a High Court, in the case of domestic arbitration, or the Chief Justice of the Supreme Court of India, in the case of international commercial arbitration, may be petitioned for making the appointment.

A question arose as to whether the Chief Justice is required to carry out his duty of appointment in an administrative or in a judicial capacity. If the Chief Justice is required to discharge his functions in a judicial capacity, a judicial procedure would have to be followed which would necessarily entail delay and the decision might tend to embarrass the arbitrator's jurisdiction to decide the same issues independently. Through a series of judgments, the issue was finally settled (or so it seemed) by a Constitution Bench of the Supreme Court (i.e. a bench comprising of five judges) in the case of *Konkan Railway Corp v Rani Construction Pvt Ltd.*[14] Here the court upheld several earlier Supreme Court judgments and unanimously held that the function of appointment is administrative in nature and not judicial. It held that one of the objects of the law is to have the arbitral tribunal constituted as expeditiously as possible. Somewhat controversially, the court went on to hold that even formal pleadings for this purpose would not be required and the opposite party would need to be only notified "so that it may know of it and may if it so choose, assist the Chief Justice or his designate in the nomination of an arbitrator".[15]

The controversy did not rest there. The Supreme Court of India constituted a seven-judge bench to reconsider the *Konkan Railways* case. This was in the case of *S.B.P. & Co v Patel Engineering.*[16] By a 6:1 majority, the court in *Patel Engineering* overruled *Konkan Railways* and held that the power exercised by the Chief Justice of the High Court or the Chief Justice of India under s.11 is not an administrative power. It is a judicial power. The court took this simple proposition further and ended up fashioning a new law of arbitration. The court began with the interpretation of s.11(7) of the Act, which provides that a decision by the Chief Justice (in relation to the act of appointment) is "final". The question was, is it final for the limited purposes seemingly envisaged by the section, namely the act of appointment, or would s.11(7) take away the arbitral tribunals "Competence–Competence" powers enshrined in s.16 of the Act (discussed below). The Supreme Court went on to hold that as a corollary to the decision being judicial, the appointment would be final for all purposes, and the arbitral tribunal's powers to determine its own competence "including ruling on any objections with respect to the existence or validity of the arbitration agreement"[17] would stand curtailed. Where the tribunal has been constituted through recourse to the Chief Justice under s.11, the tribunal would be disabled from ruling on the issue if the Chief Justice (in the process of appointment) has made a ruling on the same.

Further, the Supreme Court (in *Patel Engineering*) sought to interpret s.8 of the Act. It went on to observe (by an obiter) that when a matter is brought before a judicial authority, and an objection is raised that the court does not have jurisdiction owing to an arbitration agreement between the parties, the said judicial authority would be

11. Above fn.5, 723.
12. From transcript of speech delivered by Mr F. S. Nariman at the inaugural session of "Legal Reforms in Infrastructure", New Delhi, May 2, 2003.
13. *S.B.P & Co v Patel Engineering Ltd*, above fn.6.
14. 2002 (2) S.C.C. 388.
15. *ibid.*, 406.
16. Above fn.6.
17. s.16.

policy of Indian law or the interest of India or justice or morality". The Supreme Court in *Saw Pipes* distinguished *Renu Sagar* on the ground that the said judgment was in the context of a foreign award. The reason given was that in foreign arbitration, the award would be subject to being set aside or suspended by the competent authority under the relevant law of that country, whereas in domestic arbitration there is no such recourse and the award attains finality[11] (thus the need for greater judicial scrutiny).

Hence the *ratio* of *ONGC v Saw Pipes* in so far as the expansion of public policy is concerned would be confined only to domestic awards. The expansion of s.34 to include "patent illegality" may also arguably not apply to foreign awards since this interpretation was premised on certain provisions of the Act applicable to domestic arbitral proceedings alone. Thus foreign awards may be saved from the expanded interpretation of the said judgment.

*ONGC v Saw Pipes* makes a significant dent in the jurisprudence of arbitration in India and has come in for some sharp criticism.

One can do no better than to quote the eminent jurist and lawyer Mr F. S. Nariman who said that the judgment has

> "virtually set at naught the entire Arbitration and Conciliation Act of 1996...
>
> To have introduced—by judicial innovation—a fresh ground of challenge and placed it under the head of 'Public Policy' was first contrary to the established doctrine of precedent—the decision of a bench of three judges being binding on a bench of two judges. It was also contrary to the plain intent of the new 1996 law, namely the need for finality in alternative methods of dispute resolution without court interference.
>
> If courts continue to hold that they have the last word on facts and on law—notwithstanding consensual agreements to refer matters necessarily involving facts and law to adjudication by arbitration—the 1996 Act might as well be scrapped.
>
> The Division Bench decision of the two judges of the court has altered the entire road-map of arbitration law and put the clock back to where we started under the old 1940 Act."[12]

## The Patel Engineering judgment

This judgment of the Supreme Court[13] concerns s.11 of the Act, which provides for court intervention where the parties' envisaged mechanism for constituting the arbitral tribunal breaks down or where no mechanism is provided for and the parties cannot agree upon the same. In such an event s.11 provides that the Chief Justice of a High Court, in the case of domestic arbitration, or the Chief Justice of the Supreme Court of India, in the case of international commercial arbitration, may be petitioned for making the appointment.

A question arose as to whether the Chief Justice is required to carry out his duty of appointment in an administrative or in a judicial capacity. If the Chief Justice is required to discharge his functions in a judicial capacity, a judicial procedure would have to be followed which would necessarily entail delay and the decision might tend to embarrass the arbitrator's jurisdiction to decide the same issues independently. Through a series of judgments, the issue was finally settled (or so it seemed) by a Constitution Bench of the Supreme Court (i.e. a bench comprising of five judges) in the case of *Konkan Railway Corp v Rani Construction Pvt Ltd.*[14] Here the court upheld several earlier Supreme Court judgments and unanimously held that the function of appointment is administrative in nature and not judicial. It held that one of the objects of the law is to have the arbitral tribunal constituted as expeditiously as possible. Somewhat controversially, the court went on to hold that even formal pleadings for this purpose would not be required and the opposite party would need to be only notified "so that it may know of it and may if it so choose, assist the Chief Justice or his designate in the nomination of an arbitrator".[15]

The controversy did not rest there. The Supreme Court of India constituted a seven-judge bench to reconsider the *Konkan Railways* case. This was in the case of *S.B.P. & Co v Patel Engineering.*[16] By a 6:1 majority, the court in *Patel Engineering* overruled *Konkan Railways* and held that the power exercised by the Chief Justice of the High Court or the Chief Justice of India under s.11 is not an administrative power. It is a judicial power. The court took this simple proposition further and ended up fashioning a new law of arbitration. The court began with the interpretation of s.11(7) of the Act, which provides that a decision by the Chief Justice (in relation to the act of appointment) is "final". The question was, is it final for the limited purposes seemingly envisaged by the section, namely the act of appointment, or would s.11(7) take away the arbitral tribunals "Competence–Competence" powers enshrined in s.16 of the Act (discussed below). The Supreme Court went on to hold that as a corollary to the decision being judicial, the appointment would be final for all purposes, and the arbitral tribunal's powers to determine its own competence "including ruling on any objections with respect to the existence or validity of the arbitration agreement"[17] would stand curtailed. Where the tribunal has been constituted through recourse to the Chief Justice under s.11, the tribunal would be disabled from ruling on the issue if the Chief Justice (in the process of appointment) has made a ruling on the same.

Further, the Supreme Court (in *Patel Engineering*) sought to interpret s.8 of the Act. It went on to observe (by an obiter) that when a matter is brought before a judicial authority, and an objection is raised that the court does not have jurisdiction owing to an arbitration agreement between the parties, the said judicial authority would be

11. Above fn.5, 723.
12. From transcript of speech delivered by Mr F. S. Nariman at the inaugural session of "Legal Reforms in Infrastructure", New Delhi, May 2, 2003.
13. *S.B.P & Co v Patel Engineering Ltd*, above fn.6.
14. 2002 (2) S.C.C. 388.
15. *ibid.*, 406.
16. Above fn.6.
17. s.16.

entitled to "and bound to decide the jurisdictional issues raised before it".[18] In other words, a judicial authority would be bound to go into contentious issues including as to whether the arbitral agreement is "null and void, inoperative or incapable of being performed". This, it is respectfully submitted, achieves a result opposite to what the legislature intended when it dropped the words from the Model Law (Art.8) which permitted the court to go into the issue whether the agreement is null and void, inoperative or incapable of being performed. Indeed the Supreme Court in *Patel Engineering* case omitted to notice several of its own decisions including *Hindustan Petroleum Corp v Pink City Midway Petroleum*,[19] where the court had addressed precisely this issue:

> "The question then would arise: what would be the role of the civil court when an argument is raised that such an arbitration clause does not apply to the facts of the case in hand? ...
>
> The answer to this argument, in our opinion, is found in Section 16 of the Act itself. It has empowered the Arbitral Tribunal to rule on its own jurisdiction including rule on any objection with respect to the existence or validity of the arbitration agreement ...
>
> It is clear from the language of the section, as interpreted by the Constitution Bench judgment in Konkan Railway that if there is any objection as to the applicability of the arbitration clause to the facts of the case, the same will have to be raised before the Arbitral Tribunal concerned. Therefore, in our opinion, in this case the courts below ought not to have proceeded to examine the applicability of the arbitration clause to the facts of the case in hand but ought to have left that issue to be determined by the Arbitral Tribunal ... as required under Sections 8 and 16 of the Act."

The Supreme Court in fact had extensively covered the issue in relation to offshore arbitrations in *Shin-Etsu Chemical Co v Aksh Optifibre*.[20]

It may be recalled that s.45, in relation to offshore arbitrations, does permit the judicial authority to examine the issue whether the agreement is "null and void, inoperative or incapable of being performed". An issue arose in *Shin-Etsu* whether a ruling by court on the validity or otherwise of an arbitration agreement is to be on a prima facie basis or a final decision. If it were to be a final decision, it would involve a full trial and consequently years of judicial proceedings which would frustrate the arbitration agreement. Keeping this and the object of the Act in mind, the Supreme Court by a 2:1 decision held that a challenge to the arbitration agreement under s.45 on the ground that it is "null and void, inoperative or incapable of being performed" is to be determined on a prima facie basis. It said:

> "If it were to be held that the finding of the court under Section 45 should be a final, determinative conclusion, then it is obvious that, until such a pronouncement is made, the arbitral proceedings would have to be in limbo. This evidently defeats the credo and ethos of the Act, which is to enable expeditious arbitration without avoidable intervention by judicial authorities."

Thus, even where the statute permitted judicial intervention (for offshore arbitrations) the court in *Shin Etsu* held that it could do so only on a prima facie basis, leaving it to the arbitral tribunal to take a final decision, as it is empowered to in law. *Patel Engineering* through its unguarded observations on s.8 has permitted very wide court intervention.

It will be noticed that *Patel Engineering* has brought about an entirely new interventionist role for the court, not envisaged by the Act. The new role for the court was spelt out in the judgment itself as follows[21]:

> "It is necessary to define what exactly the Chief Justice, approached with an application under Section 11 of the Act, is to decide at that stage. Obviously, he has to decide his own jurisdiction in the sense, whether the party making the motion has approached the right High Court. He has to decide whether there is an arbitration agreement, as defined in the Act and whether the person who has made the request before him, is a party to such an agreement. It is necessary to indicate that he can also decide the question whether the claim was a dead one; or a long barred claim that was sought to be resurrected and whether the parties have concluded the transaction by recording satisfaction of their mutual rights and obligations or by receiving the final payment without objection. It may not be possible at that stage, to decide whether a live claim made is one which comes within the purview of the arbitration clause. It will be appropriate to leave that question to be decided by the arbitral tribunal on taking evidence, along with the merits of the claims involved in the arbitration. The Chief Justice has to decide whether the applicant has satisfied the conditions for appointing an arbitrator under Section 11 (6) of the Act. For the purpose of taking a decision on these aspects, the Chief Justice can either proceed on the basis of affidavits and the documents produced or take such evidence or get such evidence recorded, as may be necessary."

In *Patel Engineering* the court had to resort to one more act of judicial lawmaking. Section 11(6) of the Act envisages that the Chief Justice may delegate its appointment role to "any person or institution designated by him to take the necessary measure ...". Since this was held to be a judicial power, the judgment had to go on and curtail the scope of delegation, and also to hold that the delegation could only be to another judge of the same court and not to a subordinate judge or to any institute. It was held that the Chief Justice (or any other judge designated by him) alone would be entitled to make the appointment of an arbitrator, but they could seek the opinion of an institution as to a suitable person to be nominated.

18. Above fn.6, 17 at [15].
19. (2003) 6 S.C.C. 503.
20. (2005) 7 S.C.C. 234.
21. Above fn.6, 28 at [38].

To sum up, *Patel Engineering* brings about a fundamental change in the law of arbitration. It dilutes the Competence–Competence principle enshrined in s.16 of the Act. The court can now inter alia "decide the question whether the claim was a dead one; or a long barred claim; ... or whether the parties have concluded the transaction by recording satisfaction of their mutual rights and obligations, or by receiving final payment without objection".[22] Any such determination by the court would be final. Further, *Patel Engineering* permits judicial intervention through the interpretation of s.8 (though the same had been deliberately kept out of the section). Lastly, the decision restricts the scope of delegation envisaged under s.11(7). In other words the decision alters the law as understood and applied so far.

## A new jurisprudence

The object of this article is not to extensively debate the correctness or otherwise of *Saw Pipes* or *Patel Engineering* (though in the author's submission they are both incorrect in law). This article essentially seeks to point the direction where the decisions have taken the law on the subject.

Two things are noteworthy in both *Saw Pipes* and *Patel Engineering*. The first point has already been made and that is both the judgments depart from the spirit (and through judicial lawmaking) even the letter of the law. The second and (perhaps more significant) is that both judgments disclose a lack of trust in the arbitral process.

22. *ibid.*

## Conclusion

The law of arbitration in India is very much at its crossroads. It is largely up to the Indian judiciary to step in and contain the interventionist role it has assumed for itself and have greater trust in the arbitral process. The harsh reality is that the courts are totally unequal to the task of meeting the basic expectations of the litigating community. These very courts cannot be leaned upon to salvage the perceived inadequacies of the arbitral system through their greater intervention.

The courts must take the law forward based on trust and confidence in the arbitral system.