Proposed amendments & judicial pronouncements in Arbitration

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Chief Justice Warren E. Burger of US Supreme Court

- “The obligation of the legal profession is….to serve as healers of human conflicts…..we should provide mechanisms that can produce an acceptable result in the shortest possible time, with the least possible expense, with the minimum stress on the participants. That is what justice is all about”.

Introduction

- **The Pre-1996 Position (1940 Act):** This Act was largely premised on mistrust of the arbitral process and afforded multiple opportunities to litigants to approach the court for intervention. Coupled with a sluggish judicial system, this led to delays rendering arbitrations inefficient and unattractive.
- **The 1996 Act:** The 1996 Arbitration Act based on the UNCITRAL on International Commercial Arbitration and the Arbitration Rules of the United Nations Commission on International Trade Law 1976 was enacted.
- The Statement of Objects and Reasons to the Act said that the old Act had 'become outdated' and there was need to have an Act 'more responsive to contemporary requirements'. Amongst the main objectives of the 1996 Act were '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.
- However, this objective of quick alternative dispute resolution frequently stands frustrated.

Issues faced:

- High costs and delays: Thus, making it no better than either the earlier regime which it was intended to replace.
- After the award, a challenge under section 34 makes the award inexecutable and such petitions remain pending for several years.
- Proceedings in arbitrations are becoming a replica of court proceedings

I. Proposed Amendments

The Law Commission of India has brought out Report No. 246 in August 2014, **recommending various amendments** to the Arbitration & Conciliation Act, 1996. Chapter III of the Report contains the proposed amendments.

1. INSTITUTIONAL ARBITRATION IN INDIA

- It is one in which a specialized institution with a permanent character intervenes and assumes the functions of aiding and administering the arbitral process, as provided by the rules of such institution.

- The Commission therefore, recommended the addition of Explanation 2 to section 11(6A) of the Act with the hope that High Courts and the Supreme Court, while acting in the exercise of their jurisdiction under section 11 of the Act will take steps to encourage the parties to refer their disputes to institutionalised arbitration.

- Similarly, the Commission seeks to accord legislative sanction to rules of institutional arbitration which recognise the concept of an "emergency arbitrator" – and the same has been done by broadening the definition of an "arbitral tribunal" under section 2(d).

- The Government may also consider formation of a specialised body, like an Arbitral Commission of India, which has representation from all the stakeholders of arbitration and which could be entrusted with the task of, *inter alia, encouraging the spread of institutional arbitration in the country.*

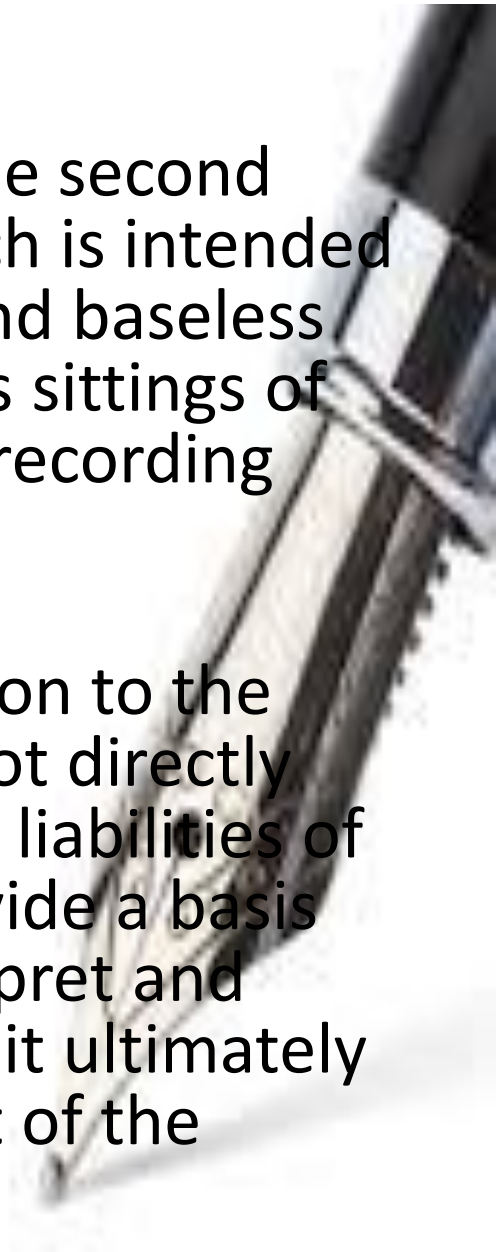
2. **FEES OF ARBITRATORS**

- Unilateral and disproportionate fixation of fees by several arbitrators.

- The subject of fees of arbitrators has been the subject of the lament of the Supreme Court in *Union of India v. Singh Builders Syndicate, (2009) 4 SCC 523.*

- Commission has recommended a model schedule of fees and has empowered the High Court to frame appropriate rules for fixation of fees for arbitrators and for which purpose it may take the said model schedule of fees into account.

3. **CONDUCT OF ARBITRAL PROCEEDINGS**



- Commission has proposed addition of the second proviso to section 24 (1) to the Act, which is intended to discourage the practice of frequent and baseless adjournments, and to ensure continuous sittings of the arbitral tribunal for the purposes of recording evidence and for argument.

- Commission has also proposed an addition to the preamble of the Act: While this would not directly affect the defined substantive rights and liabilities of parties in terms of the Act, it would provide a basis for Arbitral Tribunals and Courts to interpret and work the provisions of the Act such that it ultimately achieves those objectives for the benefit of the ultimate users of arbitration.

4. JUDICIARY AND ARBITRATION

- It is thought in some quarters that judicial intervention is anathema to arbitration, and this view is not alien to a section of the arbitration community even in India. The Commission however, does not subscribe to this view. The Commission recognizes that the judicial machinery provides essential support for the arbitral process. The paradox of arbitration, as noted by a leading academic on the subject, is that it seeks the co-operation of the very public authorities from which it wants to free itself.

- the Commission has strived to adopt a middle path to find an appropriate balance between judicial intervention and judicial restraint.

5. DELAYS IN COURTS, BEFORE THE TRIBUNAL AND INVESTMENT TREATY RISK

- Judicial intervention in arbitration proceedings adds significantly to the delays in the arbitration process and ultimately negates the benefits of arbitration

- Dedicated benches for arbitration related cases: eg. Delhi High Court has a separate bench.

- The Commission also believes that one of the methods to provide relief against frivolous and misconceived actions is to implement a regime for actual costs as is implemented in the UK and also other jurisdictions, and which finds its place in the proposed section 6A to the Act.

- Amendment in section 11: Delegate the power of appointment (being a non-judicial act) to specialized, external persons or institutions.

- The Commission has further recommended an amendment to section 11 (7) so that decisions of the High Court (regarding existence/nullity of the arbitration agreement) are final where an arbitrator has been *appointed, and as such are* non-appealable.

5. DELAYS IN COURTS, BEFORE THE TRIBUNAL AND INVESTMENT TREATY RISK (contd..)

- Further proposes the addition of section 11 (13), which requires the Court to make an endeavor to dispose of the matter within sixty days from the service of notice on the opposite party.

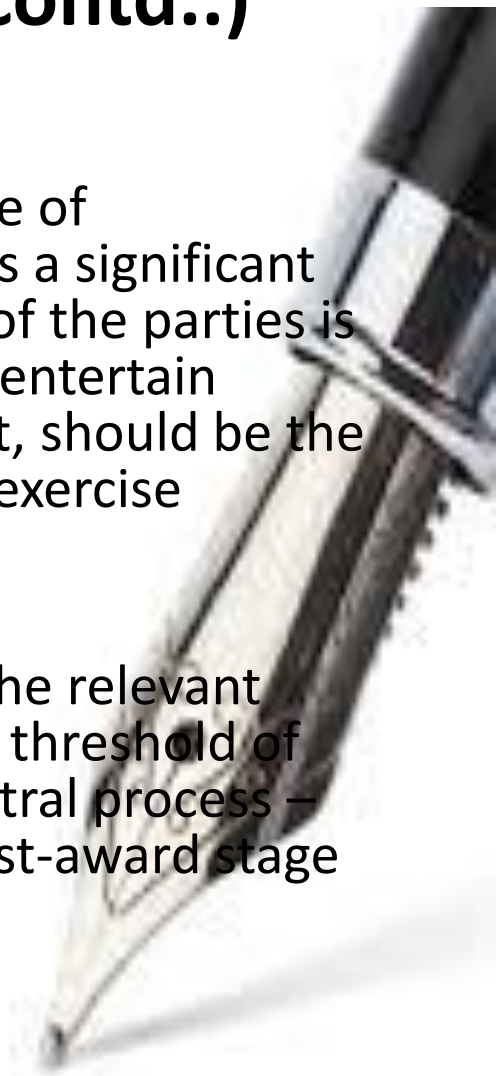
- Commission proposes the addition of sections 34 (5) and 48 (4) which would require that an application under those sections shall be disposed off expeditiously and in any event within a period of one year from the date of service of notice

- In addition, a new Explanation has been proposed to section 23 of the Act in order to ensure that counter claims and set off can be adjudicated upon by an arbitrator without seeking a separate/new reference by the respondent, provided that the same falls within the scope of the arbitration agreement

5. DELAYS IN COURTS, BEFORE THE TRIBUNAL AND INVESTMENT TREATY RISK (contd..)

- The amendments proposed to section 48: In the case of international commercial arbitrations, where there is a significant foreign element to the transaction and at least one of the parties is foreign, the relevant “Court” which is competent to entertain proceedings arising out of the arbitration agreement, should be the High Court, even where such a High Court does not exercise ordinary original jurisdiction.

- Another problem that is sought to be addressed in the relevant amendments proposed to the Act, is to increase the threshold of judicial intervention at the various stages of the arbitral process – including the pre-arbitral (sections 8 and 11) and post-award stage (section 34).



6. **SCOPE AND NATURE OF PRE-ARBITRAL JUDICIAL INTERVENTION**

- The Act recognizes situations where the intervention of the Court is envisaged at the pre-arbitral stage, i.e. prior to the constitution of the arbitral tribunal, which includes sections 8, 9, 11 in the case of Part I arbitrations and section 45 in the case of Part II arbitrations.

- Supreme Court in *Shin Etsu Chemicals Co. Ltd. v Aksh Optifibre, (2005) 7 SCC 234, (in the context of section 45 of the Act) ruled in favour of looking at the issues/controversy* ***only prima facie****.*

- The Commission has recommended amendments to sections 8 and 11 of the 1996 Act. The *scope of the judicial intervention is only restricted to situations where the Court/Judicial Authority finds that the arbitration agreement does not exist or is null and void.*

6. SCOPE AND NATURE OF PRE-ARBITRAL JUDICIAL INTERVENTION (contd..)

- If the judicial authority is of the opinion that prima facie the arbitration agreement exists, then it shall refer the dispute to arbitration, and leave the existence of the arbitration agreement to be finally determined by the arbitral tribunal. However, if the judicial authority concludes that the agreement does not exist, then the conclusion will be final and not prima facie. The amendment also envisages that there shall be a conclusive determination as to whether the arbitration agreement is null and void.

- In the event that the judicial authority refers the dispute to arbitration and/or appoints an arbitrator, under sections 8 and 11 respectively, such a decision will be final and non-appealable. An appeal can be maintained under section 37 only in the event of refusal to refer parties to arbitration, or refusal to appoint an arbitrator.

7. SETTING ASIDE OF DOMESTIC AWARDS AND RECOGNITION/ENFORCEMENT OF FOREIGN AWARDS

- Section 34 of the Act deals with setting aside a domestic award and a domestic award resulting from an international commercial arbitration whereas section 48 deals with conditions for enforcement of foreign awards. The Act, as it is presently drafted, treats all three types of awards as same.

- The legitimacy of judicial intervention in the case of a purely domestic award is far more than in case of other awards.

- Therefore, the Commission has recommended addition of section 34 (2A) to deal with purely domestic awards, which may also be set aside by the Court if the Court finds that such award is vitiated by "patent illegality appearing on the face of the award." In order to provide a balance and to avoid excessive intervention, it is clarified in the proposed *proviso to the proposed section 34 (2A) that such "an award shall not be set aside merely on the ground of an erroneous application of the law or by re-appreciating evidence."*

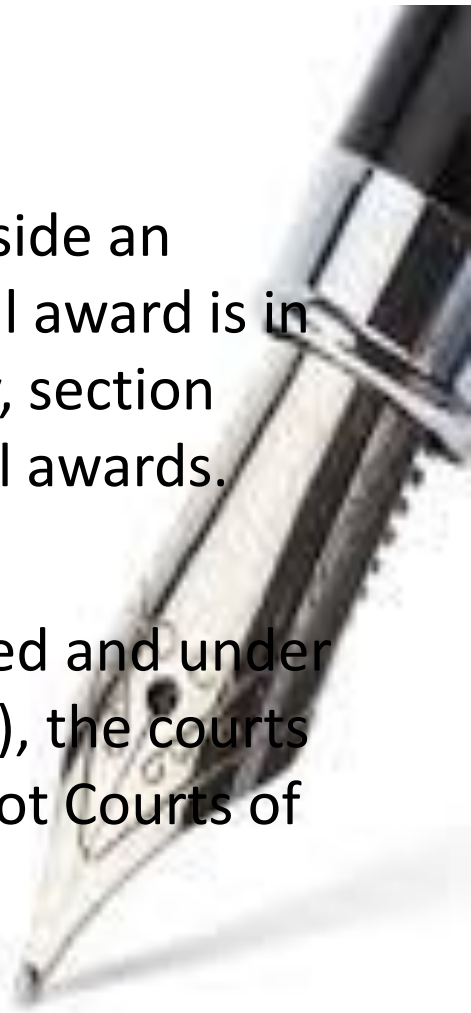
Public Policy- Section 34

- Object of the Act: Ensure speedy disposal with minimum court intervention.

- Section 34(2)(b)(ii) provides that court can set aside an arbitral award if the court finds that ''the arbitral award is in conflict with the public policy of India''. Similarly, section 48(2)(b) provides same in case of foreign arbitral awards.

- Challenge: The term ''public policy'' is not defined and under UNCITRAL Model (from where sec. 34 is derived), the courts were supposed to act as Courts of Review and not Courts of Appeal.

- However, over the period a very wide interpretation has been given to the above term.



Public Policy- Judicial Interpretation

- Supreme Court in **Renusagar Power Co. Ltd. vs. General Electric Co. [(1994** SCC supp. (1) 644] gave narrow interpretation to term ‘’public policy’’.

- Subsequently, SC in **ONGC Ltd. vs. Saw Pipes Ltd. (2003** 5 SCC 705) expanded its definition to include cases of ‘’patent illegality’’.

- **Criticism**: Eminent jurist/ Advocate Fali Nariman adversely commented on above judgment.

- **International view**: Enforcement of foreign awards is regulated by New York Convention (article V(2)(b) and same was incorporated in section 48 of the Act and so Act should be interpreted in consonance with the objectives of NYC that is that the term ‘’public policy’’ must be construed narrowly.

Public Policy- Judicial Interpretation (contd..)

- This international view was reflected in Delhi HC decision in Glencore Grain Rotterdam BV vs. Shivnath Rai Harnarain (India) Co. [2008 94) ARB LR 497 (Delhi)].

- However, SC in Phulchand exports Ltd. v OOO Patriot (2011 11 SCALE 475) followed the 'Saw Pipes'' view of expanded interpretation.

- Thereafter, SC overruled above decision in Sgri Lal Mahal Ltd. vs. Progetto Grano Spa (2014 2 SCC 433) following the narrow interpretation in ''Renusagar'' decision.

- Accordingly, 246th report provided for the same narrow approach by inserting an explanation to section 23((2)(b)(ii) and inserting new provision section 34(2A).

Public Policy- The Problem Continues

- **SC in ONGC Ltd. vs. Western Geco International Ltd. (2014 9 SCC 263) in para 39 construed the term ''fundamental policy of India'' very widely incorporating the Wednesbury principle of reasonableness.**
- **Same was followed in Associates Builder vs. DDA (2014 4 ARBLR 307 SC).**

- **Such power of review of award on merits is against the international practice and the Statement of object of 1996 Act which says ''minimization of judicial intervention''.**

- **This would lead to disastrous effect as:**
  - **i. Erosion of faith in arbitration proceedings**
  - **ii. Reduction of popularity of India as arbitration destination**
  - **iii. Increase in judicial backlog**
  - **iv. Increased Investor concern**

Public Policy: Suggested Solution

- Section 34(2)(b)(ii) be substituted by the following:
- 34(2)(b)(ii) : The arbitral award is in conflict with 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:**

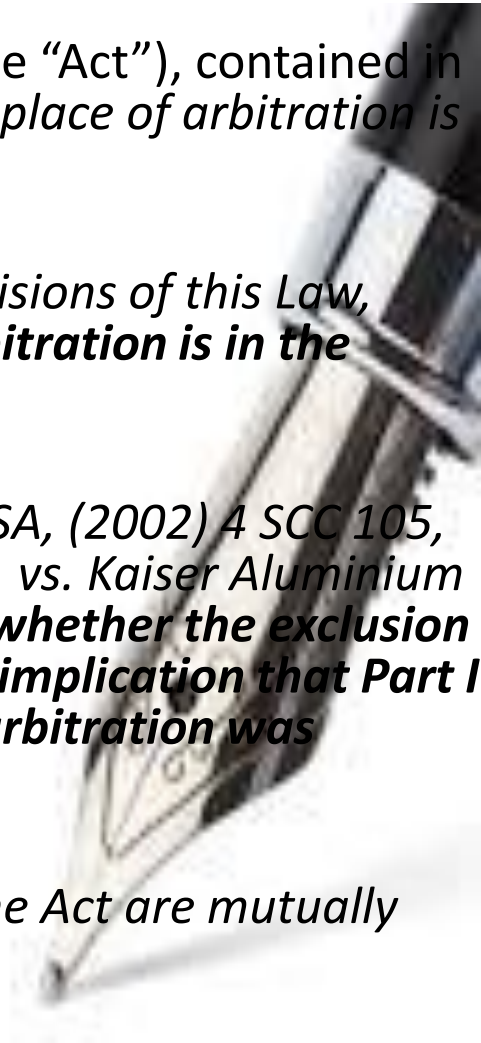
  a. making of award was induced or affected by fraud or corruption or was in violation of section 75 or 81;

  b.It is in contravention with the fundamental policy of Indian Law; or

  c.It is in conflict with most basic notions of morality or justice.
- **Explanation 2: For 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 merits of dispute.**

- **Section 34(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 law or re-appreciation of evidence.**

8. JUDICIAL INTERVENTIONS IN FOREIGN SEATED ARBITRATIONS



- Section 2(2) of the Arbitration and Conciliation Act, 1996 (the "Act"), contained in Part I of the Act, states that "*This Part shall apply where the place of arbitration is in India.*"

- Article 1(2) of the UNCITRAL Model Law provides: "*The provisions of this Law,* ***except articles 8, 9, 35 and 36, apply only if the place of arbitration is in the territory of this State***

- Supreme Court in *Bhatia International vs. Interbulk Trading SA, (2002) 4 SCC 105, and before the five-judge Bench in Bharat Aluminum and Co. vs. Kaiser Aluminium and Co., (2012) 9 SCC 552 (hereinafter called "BALCO") was* ***whether the exclusion of the word "only" from the Indian statute gave rise to the implication that Part I of the Act would apply even in some situations where the arbitration was conducted outside India.***

- The Supreme Court in *BALCO decided that Parts I and II of the Act are mutually exclusive of each other.*

- The above issues have been addressed by way of proposed Amendments to sections 2(2), 2(2A), 20, 28 and 31.

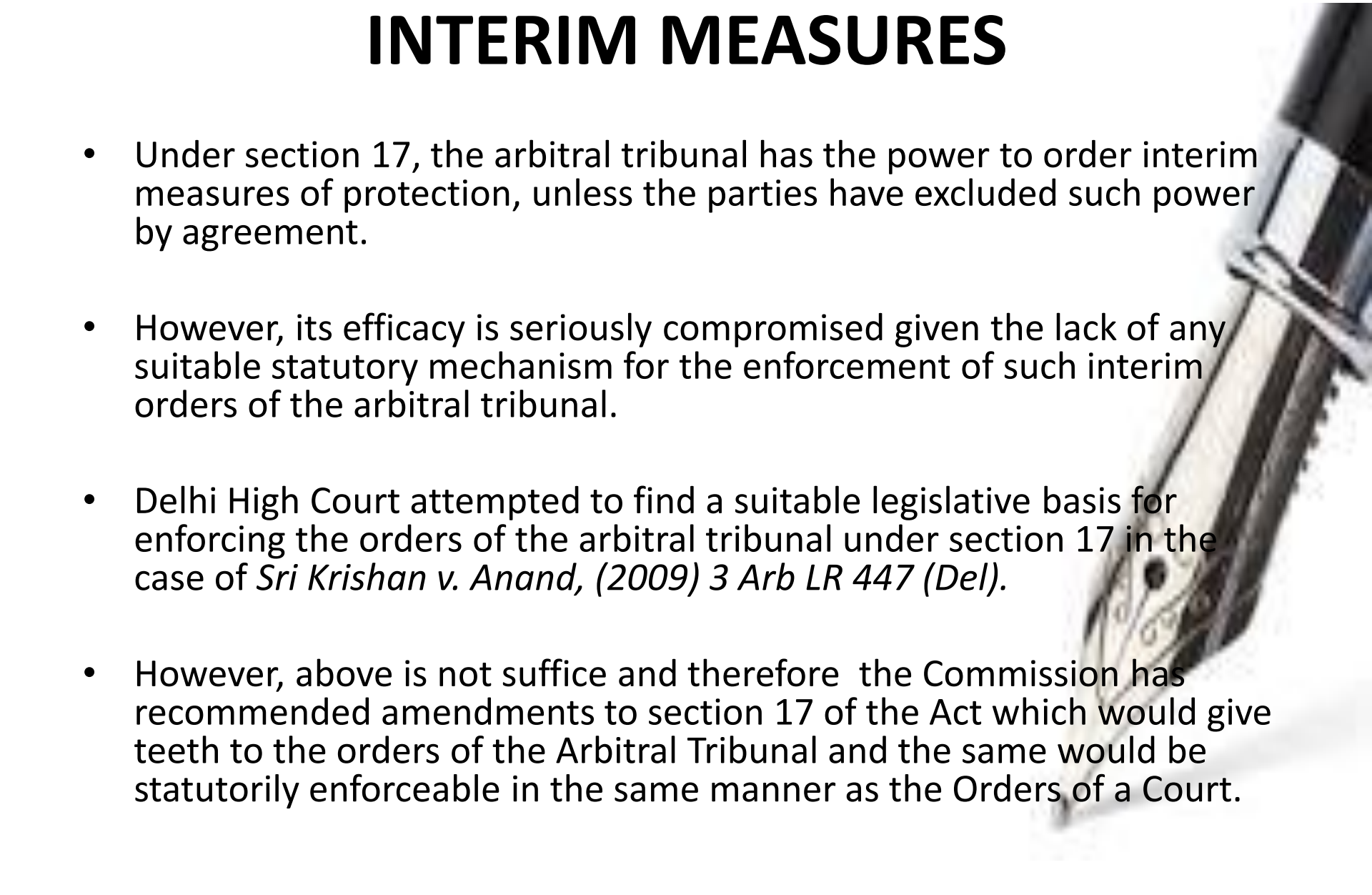
9. **AUTOMATIC STAY OF ENFORCEMENT OF THE AWARD UPON ADMISSION OF CHALLENGE**

- Presently, pendency of a section 34 petition renders an arbitral award unenforceable.

- The Supreme Court,*National Aluminum Co. Ltd. v. Pressteel & Fabrications, (2004) 1 SCC 540 has criticized the present situation.*

- In order to rectify this mischief, certain amendments have been suggested by the Commission to section 36 of the Act, which provide that the award will not become unenforceable merely upon the making of an application under section 34.

10. **POWERS OF TRIBUNAL TO ORDER INTERIM MEASURES**



- Under section 17, the arbitral tribunal has the power to order interim measures of protection, unless the parties have excluded such power by agreement.

- However, its efficacy is seriously compromised given the lack of any suitable statutory mechanism for the enforcement of such interim orders of the arbitral tribunal.

- Delhi High Court attempted to find a suitable legislative basis for enforcing the orders of the arbitral tribunal under section 17 in the case of *Sri Krishan v. Anand, (2009) 3 Arb LR 447 (Del).*

- However, above is not suffice and therefore the Commission has recommended amendments to section 17 of the Act which would give teeth to the orders of the Arbitral Tribunal and the same would be statutorily enforceable in the same manner as the Orders of a Court.

11. **ARBITRABILITY OF FRAUD AND COMPLICATED ISSUES OF FACT**

- *SC held in Bharat Rasiklal v. Gautam Rasiklal, (2012) 2 SCC 144 that when fraud is of such a nature that it vitiates the arbitration agreement, it is for the Court to decide on the validity of the arbitration agreement by determining the issue of fraud, there exists two parallel lines of judgments on the issue of whether an issue of fraud is arbitrable.*

- *The Commission believes that it is important to set this entire controversy to a rest and make issues of fraud expressly arbitrable and to this end has proposed amendments to section 16.*

12. **NEUTRALITY OF ARBITRATORS**

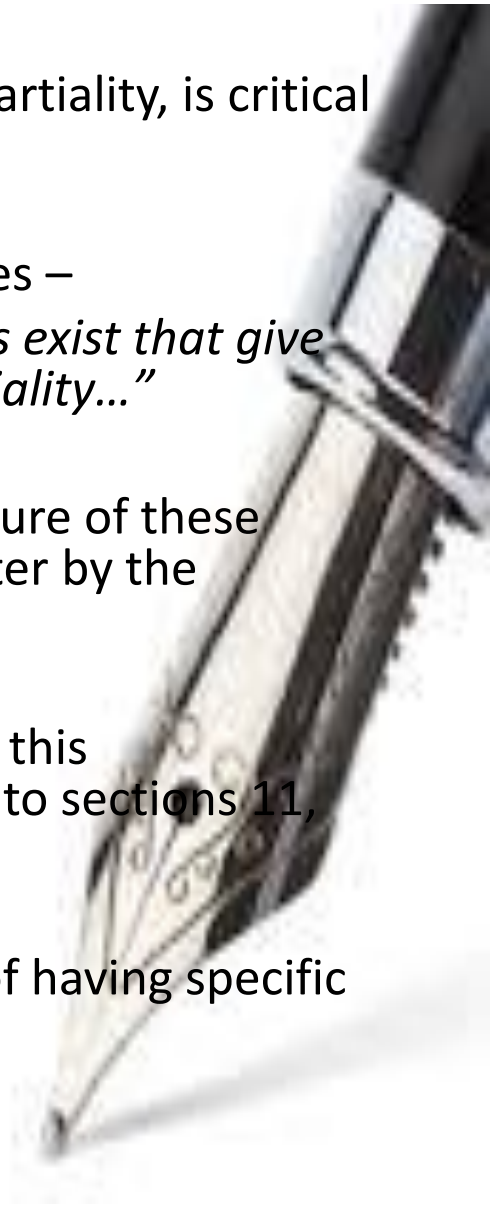
- Neutrality of arbitrators, viz. their independence and impartiality, is critical to the entire process.

- Test for neutrality is set out in section 12(3) which provides –
- *"An arbitrator may be challenged only if (a) circumstances exist that give rise to justifiable doubts as to his independence or impartiality…"*

- The balance between procedural fairness and binding nature of these contracts, appears to have been tilted in favour of the latter by the Supreme Court.

- Large scale amendments have been suggested to address this fundamental issue of neutrality of arbitrators particularly to sections 11, 12 and 14 of the Act.

- Further, the Commission has proposed the requirement of having specific disclosures by the arbitrator.



II. Latest Judicial Pronouncements

Reliance Industries Limited and Anr. Vs. Union of India (UOI) (2014)7 SCC 603

- Issue: Whether foreign arbitration law or Indian law was applicable on basis of public policy for determining question of arbitrability of claim?

- Finding: Applicability of Part I of Act was not dependent on nature of challenge to award. High Court had committed jurisdictional error in holding that specified provisions were relevant only for determination of curial law applicable to proceedings.

- Held: High Court was not correct in holding that even though arbitration agreement would be governed by laws of England, Part I of Arbitration Act would still be applicable as laws governing substantive contract were Indian laws. Therefore, appeal allowed.

Swiss Timing Limited v Organising Committee, 2010 Olympic Games, Delhi Arbitration Petition No. 34 OF 2013 in the Supreme Court of India

- Issue: Whether in cases of fraud claims Indian Law can be imposed on foreign seated Arbitrations?

- Finding: The Court overturned the previous authority on this point and held that even in the context of India-seated arbitrations, fraud allegations are capable of being dealt with by arbitral tribunals.

- Held:

  Section 16 of the Arbitration Act requires a Court to direct parties to arbitration where there is an applicable arbitration agreement between the parties;

  Allegations as to the voidness or voidability of the substantive agreement would not (save in exceptional cases) prevent the dispute being referred to arbitration – the Court "ought to decline reference to arbitration only where the Court can reach the conclusion that the contract is void on a meaningful reading of the contract document itself without the requirement of any further proof"; and

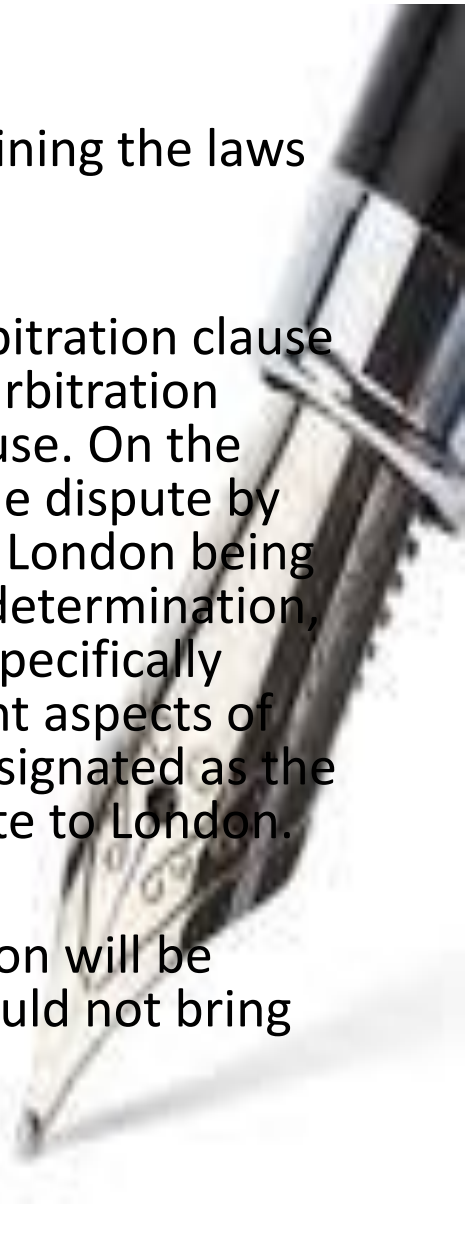
  The fact of ongoing parallel criminal proceedings is not a reason to delay the commencement of the arbitration.

Enercon India Ltd v Enercon GmbH (2014)5SCC1

- Issue: Whether the venue is a decisive factor in determining the laws applicable to the parties to the arbitration proceedings?

- Findings: Applied the principles of severability of the arbitration clause from the underlying contract and referred a dispute to arbitration despite some flaws in the drafting of the arbitration clause. On the facts, the Court retained supervisory jurisdiction over the dispute by holding that the seat of arbitration was in India, despite London being chosen as the 'venue' of the arbitration. In making this determination, the Court was heavily swayed by the fact that the laws specifically chosen by the parties in the contract to apply to different aspects of the dispute were Indian laws, and that besides being designated as the 'venue', there was no other factor connecting the dispute to London.

- Held: In such circumstances, the hearing of the arbitration will be conducted at the venue fixed by the parties, but this would not bring about a change in the seat of the arbitration.



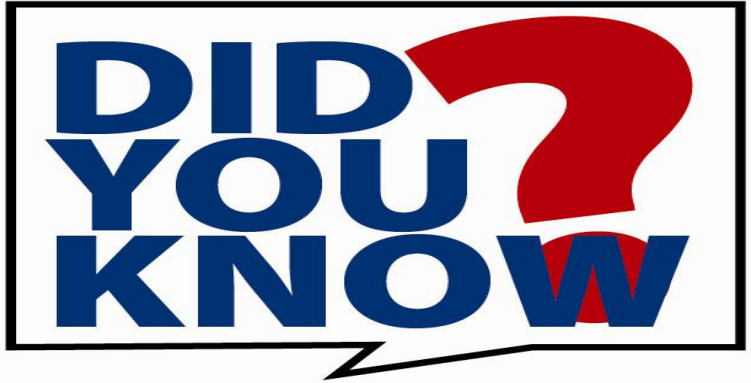
Union of India v Panacea Biotec O.M.P. 1295/2013 and I.A. No. 21089/2013 (Delhi High Court)

- Issue: Whether the mandate of arbitral tribunal can be terminated due to excessive delay in giving the award ?

- Findings: The tribunal was accused of taking an unreasonably long time to progress proceedings and had incurred very significant costs. In addition to allowing the application, the Court penalized the tribunal by holding that no further fees would be payable to it. The court has since referred the arbitration to be conducted under the auspices of the Delhi International Arbitration Centre.

- Held: The Delhi High Court allowed parties to use their statutory rights under the Arbitration Act to terminate the mandate of an arbitral tribunal.

Trivia



- 18 Feb,2015: Law Ministry has proposed to develop a panel of bodies to provide institutional arbitration and advise central departments and public enterprises on ways to include arbitration clause in their contracts.

- The Supreme Court in an order dated March 24, 2015 has directed Entrack International Trading (EITPL) and luxury writing instrument maker Montblanc Simplo GMBH to appoint an arbitration panel of three individuals to settle their dispute.

THANK YOU