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DETERMINING PATENT ILLEGALITY FOR SETTING ASIDE AN ARBITRAL AWARD

INTRODUCTION

The term ‘patent illegality’ has not been defined in the Arbitration & Conciliation Act, 1996 (Arbitration Act); however, it is one of the grounds to set aside an arbitral award. The ground of ‘patent illegality’ can be invoked if an arbitral award is contrary to the provisions of law. It does not apply as a ground for setting aside an international commercial arbitration.

Indian Arbitration Jurisprudence

The Arbitration Act in India has witnessed a change through an Amendment Act of 2015 which brought significant changes to the provisions of the Act. The Supreme Court first propounded the ground of patent illegality in *Oil & Natural Gas Corporation Ltd. v. Saw Pipes Ltd.* [(2003) 5 SCC 705] and held that an award would be ‘patently illegal’ if it is contrary to the substantive provisions of law, or provisions of the Act, or terms of the contract.

An award is considered to be illegal if it is passed contravening public policy; Amendment Act of 2015 brought a major amendment to Section 34 of the Arbitration Act; wherein the term ‘public policy’ was expanded. The newly inserted sub-section (2A) in

Section 34, states, “(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 re-appreciation of evidence.”

Now it includes only two grounds i.e., the fundamental policy of Indian law and justice/morality along with inducement of fraud or corruption while passing the award. The ground which was previously a part of public policy i.e. ‘in the interest of India’ has now been deleted.

In the case of *Associate Builders v. Delhi Development Authority* [(2015) 3 SCC 49]: It was clarified that the main object of 2015 Amendment is to speed up the process of arbitration and also to reduce the intervention of the courts to ensure ease of businesses in India.

The Court stated that the arbitral tribunal holds the responsibility to determine the terms of the arbitration agreement. The ground of patent illegality could be invoked if the arbitral tribunal fails to determine reasonably the terms of the agreement and if the agreement has

the terms of the agreement and if the agreement has been construed/interpreted unfairly.

Ssangyong Engineering and Construction Company Limited v. National Highways Authority of India [(2019) 15 SCC 131]- The Supreme Court of India stated that the ground of patent illegality can be attracted in very exceptional cases where the conscience of the court is shocked by the award passed by the Ld. Arbitrator. It further clarified that the permissible grounds for interference with a domestic award u/s 34(2-A) of the Arbitration Act on the ground of patent illegality is when the arbitrator:

- o Takes a view that is not even a possible one, or
- o Interprets a clause in the contract in such a manner which no fair-minded or reasonable person would, or
- o Commits an error of jurisdiction by wandering outside the contract and dealing with matters not allotted to them.

Recently in *PSA SICAL Terminals Pvt. Ltd v. Chidambaranar Port Trust Tuticorin and others* [(2021) SCC Online SC 508], the Hon’ble Supreme Court while relying upon the *Ssangyong* (supra) Judgment, held that the Arbitrator was bound to arbitrate within the terms of the contract and in case he travels out of the terms, the same shall be without jurisdiction.

Public policy and judicial intervention

The concept of public policy has not yet been defined; it can be understood in terms of an act that is in contravention of set principles and policies existing in a society. It concerns public good and public interest matters, not the policies of a particular government.

Recently, the Division Bench of Hon’ble High Court of Delhi comprising of Justice Mr. Rajiv Shakhder and Mr. Talwant Singh addressed a matter regarding the arbitral award in the case of *Oriental Insurance Co. Ltd. v. Diamond Product Ltd., 2021 SCC OnLine Del. 4319* (for short ‘Oriental Insurance Co. Case’), wherein the High Court dealt with the issue of patent illegality of an arbitral award. It focused on the method adopted by the Arbitral Tribunal for calculating the arbitral award and also the Tribunal and found an error in the report of the Surveyor.

The High Court appreciated the fact that the Tribunal has given enough reasons regarding opting to ignore the methodology adopted by the surveyor in calculating the



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loss claimed by the respondent on account of damage to its stock. The Court concluded that arbitral awards (domestic) can be challenged on the ground of patent illegality if it appears to be such that goes to the root of the matter. It held that mere erroneous application of the law, or appreciation of evidence, does not call for interference of the award on the ground of patent illegality. The Court cannot set aside the award by re-appreciation of the evidence, which is taken into consideration, by an Arbitral Tribunal. The High Court concluded that it cannot be said that the Arbitral Tribunal has done patent illegality while passing the award as it was done in a detailed and reasoned manner.

The Apex Court in 2020, in the case of *Patel Engineering Ltd. v. North Eastern Power Corporation Ltd. [22nd May 2020 in Special Leave Petition (C) Nos. 3584-85 of 2020]* dealt with the determination of issue of the 'patent illegality' as provided under Section 34 (2A) of the Arbitration Act. In the instant matter, the court recognized and re-affirmed the test of patent illegality.

Conclusion

The Amendment Act of 2015 has clarified the grounds on which an arbitral award can be set-aside under 'patent illegality'.

The decisions of the Courts as discussed above are to be interpreted to lead to the following conclusion-An arbitral award may be set aside on the grounds of patent illegality:

- a. The Award passed strikes to the very basic notions of Justice;
- b. The contravention of the provisions of the Arbitration Act or other provisions of law;
- c. An award that is unreasonable that it shocks the court's conscience.
- d. Recently on 01.02.2022, the Hon'ble Supreme Court in *Indian Oil Corporation Ltd. v. Shree Ganesh Petroleum Rajgurunagar, [Civil Appeal Nos. 837-838 of 2022, date of judgment 1st February 2022]* while allowing the Special Leave Petition filed by Indian Oil Corporation, which was represented by Meharia and Company, has held that the Arbitral Tribunal is bound to act in terms of the contract under which it is constituted. Further the Hon'ble Supreme Court while setting aside the Award declared it to be patently illegal since the Arbitral Tribunal has failed to act according to the terms of the contract and/or has ignored the specific agreed terms of a contract.