

November 10, 2020

THE STORY OF ARBITRAL MEDDLING

**ANALYZING THE ARBITRATION AND CONCILIATION ACT
(AMENDMENT) ORDINANCE, 2020**

argus
partners
SOLICITORS AND ADVOCATES

MUMBAI | DELHI | BENGALURU | KOLKATA | AHMEDABAD

Introduction

What can be perceived as nothing but an interesting move, the President has promulgated the Arbitration and Conciliation Act (Amendment) Ordinance, 2020 (“**Ordinance**”) with the object of ensuring that stakeholders get an opportunity to seek an *unconditional stay of enforcement of arbitral awards where the underlying arbitration agreement or contract or making of the arbitral award are induced by fraud or corruption*.¹

The Ordinance has amended Section 36 of the Arbitration and Conciliation Act, 1996 (“**Arbitration Act**”) to introduce a new second *proviso* to sub-section (3) of Section 36 of the Arbitration Act. The said *proviso* enumerates that, where a court is *prima-facie* satisfied that the arbitration agreement or the contract, which is the basis of the arbitral award or making of the arbitral award, was induced or effected by fraud or corruption, it shall grant an unconditional stay on the enforcement of such arbitral award. The court can exercise the aforesaid power pending disposal of a challenge under Section 34 to the award.² The Ordinance has further clarified that the newly inserted second *proviso* to Section 36(3) of the Arbitration Act shall also be applicable to all court cases arising out of or in relation to arbitral proceedings, irrespective of whether the arbitral or court proceedings have commenced prior to or after the commencement of the 2015 Amendment. Hence, it is *ex-facie* evident that the said amendment to Section 36(3) shall have a retrospective application.

Additionally, the Ordinance *vide* its Section 3, substitutes Section 43J of the Arbitration Act by laying down that the qualification, experience, and norms for accreditation of arbitrators shall be such as may be prescribed by the regulations. Thus, consequently, *vide* Section 4 of the Ordinance, the Eight Schedule to the Arbitration Act has also been omitted.

For the purposes of this instant paper, we endeavor to only address the first part of the amendment.

Analysis of Section 2 of the Ordinance

It is pertinent to mention that *vide* the 2015 amendment³ to Section 34 (1)(b) of the Arbitration Act, the Central Government had already clarified that an arbitral award would be regarded to be in conflict with the public policy of India if the making of the award was induced or affected by fraud or corruption.⁴ However, Section 34 of the Arbitration Act does not permit setting aside of an arbitral award on the grounds of an underlying arbitration agreement and/ or contract being induced by fraud or corruption.

It is important to note that an applicant under Section 36(3) of the Arbitration Act, as on date, is anyway eligible to file an application seeking stay on the enforcement of the arbitral award pleading the grounds already enumerated under Section 34 of the Arbitration Act. The Ordinance additionally entitles an applicant to seek an unconditional stay on the enforcement of an arbitral award under Section 36(3), during the pendency of the Section 34 application, by pleading that the contract or arbitration agreement which is the basis of the award was induced by fraud or corruption.

To understand the scope of the amendment, it may be useful to delve into the position of law with respect to arbitral disputes wherein parties allege fraud in the formulation of the contract and/or arbitration agreement. The Supreme Court in the case of *Ameet Lalchand Shah v. Rishabh Enterprises*,⁵ had held that only where serious allegations of fraud are involved, arbitration of a dispute may be refused. The Apex Court, in the recent case of *Avitel Post Studios Limited v. HSBC*

¹ The Arbitration and Conciliation (Amendment) Ordinance, 2020. Notified on November 4, 2020.

² Section 2 of the Ordinance.

³ Arbitration and Conciliation (Amendment) Act, 2015 (“**2015 Amendment**”).

⁴ Explanation 1, Section 34(b)(i) of Arbitration Act.

⁵ (2018) 15 SCC 678.

PI Holdings (Mauritius) Limited,⁶ (“**Avitel case**”) while interpreting the term “serious allegations of fraud” held that such a situation arises only if two tests are satisfied, i.e. wherein:

- a. The arbitration agreement or the clause itself cannot be said to exist in which the party against whom the breach is alleged cannot be said to have been entered into the agreement relating to the arbitration at all;
- b. Allegations are raised against State instrumentalities of arbitrary, fraudulent or *malafide* conduct, thus, necessitating the hearing of the case by a writ court in which questions are raised which are not predominantly questions arising from the contract itself or breach thereof, but questions arising in the public law domain.

The Court held that a dispute is arbitrable unless there are serious allegations of fraud which vitiate the arbitration clause along with the agreement, or there are allegations of fraud which are not merely inter parties, but affect the public at large. What may constitute such fraud has been largely left to the courts to decide.

The court further noted that the expression, “*or to induce him to enter into the contract*” enumerated in Section 17 of the Indian Contract Act, 1972 (“**Contract Act**”) refers to a situation where a fraud is said to have been committed at the stage of entering into the contract.⁷ The Apex Court, thus held that a fraud which is practiced outside the scope of Section 17 of the Contract Act i.e. in the performance of the contract, may be governed by the tort of deceit, which would lead to damages, but not rescission of the contract itself.⁸

It was always open to a party which has been induced to enter into a contract through fraud or corruption, to file a suit for rescission of the said contract or damages or both was always available.⁹ The Ordinance now entitles parties to seek unconditional stay of arbitral award at the time of challenging such award where there has been fraud in the formulation of the contract and/or arbitration agreement.

As far as the scope of inquiry of a court in respect of the provision of the Ordinance is concerned, it is also important not to lose sight of the fact that under Section 34 of the Arbitration Act, the court is usually not required to examine the merits of the interpretation provided in the award by the arbitrator, if it comes to a conclusion that such an interpretation was reasonably possible.¹⁰ Even in cases where there are two views which are possible, the court cannot interfere with the plausible view taken by the arbitrator supported by his reasoning.¹¹

As the Ordinance makes use of the words “*prima-facie*”, it may be useful to see how courts have interpreted.

The Hon'ble Supreme Court of India in *Martin Burn v. R.N. Banerjee*¹² held that:

"27...A prima facie case does not mean a case proved to the hilt but a case which can be said to be established if the evidence which is led in support of the same were believed."

(emphasis supplied)

⁶ Civil Appeal No. 5145 of 2016. Decided on August 19, 2020.

⁷ *Id.* at para. 17.

⁸ *Id.* at para. 17.

⁹ Pollock & Mulla, *The Indian Contract and Specific Relief Acts*, 14th Edition, Volume I at page 400.

¹⁰ *South East Asia Marine Engineering and Construction Limited v. Oil India Limited*, (2020) 3 SCC (Civ) 1.

¹¹ *Id.*

¹² AIR 1958 SC 79.

Further, the Hon'ble Bombay High Court in the case of *H.R. Gokhale v. Bharucha, Noshir C.*,¹³ while reiterating the aforesaid judgment held:

“15...It is, therefore, clear that, in arriving at its conclusion as to whether a prima facie case in regard to a particular point has been made out, a Court of law is not bound to weigh the evidence or to judge the credibility of the witnesses, but has only got to see whether that case could be said to be established if the evidence led by the party concerned on the point were believed, taking it at its “face value...”

The inclusion of the word '*prima facie*' introduces doubts as to the scope of inquiry that the court may conduct while granting an unconditional stay. Is it the case then that a mere averment alleging fraud or corruption in respect of the arbitration agreement or the arbitral award will enable the court to grant an unconditional stay in respect of the award?

Further, a reading of Section 36(3) of the Arbitration Act would clearly reveal that the court has already been bestowed with the power to stay the enforcement of an arbitral award, on conditions that it may deem fit and for such reasons, that it shall record in writing. This can be interpreted to include within its purview the power to stay an arbitral award without conditions where it considers fit, even prior to promulgation of the Ordinance. It is not clear as to why there may be a requirement of the amendment specially carving out a further proviso with additional grounds for grant of an unconditional stay. Does this mean that now the court will have the power to grant an unconditional stay only where there is an allegation/ claim of fraud and corruption with respect to formulation of the arbitration agreement and/ or contract or making of the arbitral award and not otherwise? The Ordinance fails to provide any clarity on the said aspect. Hence, it would be interesting to see how courts interpret it.

Lastly, insofar as the retrospective application of the second *proviso* to Section 36(3) of the Arbitration Act is concerned,¹⁴ the same would indicate that an applicant under Section 34 of the Arbitration Act where the court proceedings have commenced even before October 23, 2015 and are pending, would also be eligible to seek an unconditional stay under the second *proviso* Section 36(3) of the Arbitration Act alleging fraud and/ or corruption in formulation of the underlying arbitration agreement or contract or making of the arbitral award. In cases where a stay of award, conditional upon deposit of amounts, have already been granted Section 36(3) of the Arbitration Act, this may lead to an avalanche of applications seeking an unconditional stay on the enforcement of the award and consequent refund of deposit of the sums deposited.

Conclusion

The Statement and Objects of the 2015 Amendment to the Arbitration Act mentioned that India has been ranked at 178 out of 189 nations in the world in contract enforcement and that it was high time that urgent steps were taken in order to facilitate quick enforcement of contracts, easy recovery of monetary claims and award of just compensation for damages suffered and reduce the pendency of cases in courts in order to hasten the process of dispute resolution through arbitration, so as to encourage investment and economic activity.¹⁵

Through unconditional stay of awards, the Ordinance thus, defeats the aforesaid objective of the 2015 Amendments by taking the arbitration landscape of the country back to the situation which

¹³ AIR 1969 Bom 177.

¹⁴ Explanation to Section 2 of the Ordinance.

¹⁵ *Recital 4*, Statement of Objects and Reasons, 2015 Amendment.

existed prior to the 2015 Amendment by introducing another avenue to arbitration award debtors to evade payment of amounts rightfully due, while petitions under Section 34 of the Arbitration Act languish.

This paper has been written by Pooja Chakrabarti (Partner) and Kunal Dey (Associate).

DISCLAIMER

This document is merely intended as an update and is merely for informational purposes. This document should not be construed as a legal opinion. No person should rely on the contents of this document without first obtaining advice from a qualified professional person. This document is contributed on the understanding that the Firm, its employees and consultants are not responsible for the results of any actions taken on the basis of information in this document, or for any error in or omission from this document. Further, the Firm, its employees and consultants, expressly disclaim all and any liability and responsibility to any person who reads this document in respect of anything, and of the consequences of anything, done or omitted to be done by such person in reliance, whether wholly or partially, upon the whole or any part of the content of this document. Without limiting the generality of the above, no author, consultant or the Firm shall have any responsibility for any act or omission of any other author, consultant or the Firm. This document does not and is not intended to constitute solicitation, invitation, advertisement or inducement of any sort whatsoever from us or any of our members to solicit any work, in any manner, whether directly or indirectly.

**You can send us your comments at:
argusknowledgecentre@argus-p.com**

Mumbai | Delhi | Bengaluru | Kolkata | Ahmedabad

www.argus-p.com