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PATENT ILLEGALITY- GROUND TO SET ASIDE DOMESTIC AWARD- Bhavay Malhotra¹**ABSTRACT**

Owing to endemic delays to pronounce the judgments by Indian courts, arbitration became one of the significant ways for parties to resolve their disputes. Today, arbitration has become default setting to resolve commercial disputes by circumventing delays of the courts. However, judicial interference in arbitration process is a deeply contested discussion among legal practitioner and concerned parties. Higher judicial interference is a direct threat to the two important principles of arbitration: party autonomy and finality of award.² Reliance over arbitration to resolve the disputes will decrease if these two principles are more vulnerable to judicial intervention. Arrangements must be made to minimise the scope of judicial intervention and judicial review over arbitration law to make it more commercially attractive.

Hence, in light of the afore-mentioned statement, this paper will critically analyse the provision of “patent illegality” under section 34 of the Arbitration and Conciliation Act, 1996 (hereinafter referred as 1996 Act) as ground to setting aside domestic arbitration award before competent court of jurisdiction. The ground of patent illegality was formally introduced to 1996 Act by way of Arbitration and Conciliation (Amendment) Act 2015 (2015 Amendment Act), which came into force on 23 October 2015.³ Initially, it was argued that addition of this ground would give rise to the judicial intervention in arbitration law in India but, as we move forward, the paper will examine the judicial interpretation by the courts to narrow down the scope of patent illegality as a ground to challenge the domestic arbitration award. This paper is divided into three major parts; first part will highlight the origin of patent illegality and what were the situations in the past which carved out the need to introduce patent illegality as ground to

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² Garima Budhiraja Arya & Tania Sebastian, Critical Appraisal of Patent Illegality as a Ground for Setting Aside an Arbitral Award in India, 24 BOND L. REV. 157 (2012)

³ <https://lawmin.gov.in/sites/default/files/ArbitrationandConciliation.pdf>

challenge the award, second part will examine the judicial interpretation of patent illegality after its formal introduction by way of 2015 amendment and the third part of the paper will discuss whether there was a need of a separate provision of patent illegality as a ground to challenge domestic award when the ground of “public policy” was already available.

I.) Origin and scope of patent illegality:

In order to understand the origin of patent illegality as ground to set aside the domestic award, it is pertinent to discuss the history of arbitration in India. Arbitration is not a new concept in India as people used to rely on village ‘panchayats’ to get their dispute resolved instead of moving before the courts. Familiarity of people to resolve the dispute outside the courts allowed them not only to adopt but also to rely on arbitration to get quick, clean and sophisticated way of dispute redressal mechanism. Arbitration law in India was first codified in 1899 which was entirely based on English Arbitration Act of 1899.⁴ It was then further codified in 1908 and thereafter, arbitration law was governed by three different statutes: the Indian Arbitration Act, 1940 (dealing with domestic arbitration); and the Arbitration (Protocol) and Convention) Act, 1937; and the Foreign Awards (Recognition and Enforcement) Act, 1961.⁵ Finally, the code of 1996 was adopted by repealing all earlier statutes and came to be known as The Arbitration and Conciliation Act, 1996. With the evolution of codification of arbitration law, country also witnessed the shift from indiscriminate judicial intervention in arbitration law to minimal judicial inter-reference. The shift was, however, due to the fact that 1996 Act was drafted during the economic liberalisation of India and in accordance with the provisions of *UNCITRAL Model Law on International Commercial Arbitration 1985 ('Model Law')* wherein the principles of minimum judicial intervention and party autonomy were duly enshrined.⁶ Enforcement of domestic and foreign arbitration award is governed by two different parts in 1996 Act. Part one deals with enforcement of domestic award whereas, part two deals with foreign award.

However, despite the shift, courts in India were reluctant to agree with such a view of minimum judicial intervention and one such example of it would **introduction of principle of ‘patent illegality’ through case laws in country**. The concept of patent illegality to set aside the

⁴ Cyril Amarchand Mangaldas, Arbitration in India- A story of growth and opportunity.

⁵ Ibid.

⁶ Supra 1

domestic award has its origin from *Oil & Natural Gas Corporation Ltd v Saw Pipes Ltd.*⁷ wherein the Apex Court of India while giving wider meaning to the phrase ‘public-policy’ under section 34 added patently illegal to already existing grounds⁸ (giving meaning to phrase-public policy) laid down in *Renusagar case*⁹. It further held that “illegality must go to the root of the matter and if the illegality is of trivial nature it cannot be held that award is against the public policy”¹⁰. The broad interpretation of phrase public-policy in *Saw Pipes* enhanced the possibility of limitless judicial intervention allowing the parties to challenge the award on trivial grounds and hence, the said judgements attracted several criticism from legal practitioners. But, despite all these criticism and we will see in the next sections of paper that how the Parliament fortified the stand of the Judiciary by adding the ground of patent illegality formally in section 34 of 1996 Act.

II.) 2015 Amendment & narrowing down the scope of Patent Illegality:

The addition of patent illegality under section 34 by way of Arbitration and Conciliation (Amendment) Act 2015 (2015 Amendment Act) came in the light of *246th Law Commission Report* wherein the need of addition of patent illegality as a separate ground to set aside the award was recommended. Thereafter, the Supreme Court of India in *Associate Builders v. DDA*¹¹ got an opportunity to deal with the newly added provision of patent illegality. The court while doing so laid down the test which was based in **principle of perversity**. The court held that if the award is perverse then it will fall under the meaning of patent illegality and in order to find whether the award is perverse or not, one has to be satisfied on three grounds: (i) a finding is based on no evidence, or (ii) an Arbitral Tribunal takes into account something irrelevant to the decision which it arrives at; or (iii) ignores vital evidence in arriving at its decision.¹² **In my opinion**, the decision of *Associate Builders* gave a narrow meaning to the phrase ‘patent illegality’ in comparison to the wide meaning given to it in *Saw Pipes* and it could also be looked to state that the court took it as an opportunity to interpretate the said phrase in line of object of 1996 Act aiming to minimise judicial intervention in the arbitration law.

⁷ (2003) 5 SCC 705

⁸ Existing grounds in *Renusagar Case*: (a) fundamental policy of Indian law; or (b) the interest of India; or (c) justice and morality.

⁹ *Renusagar Power Co Ltd v General Electric Co.* (1994) Supp 1 SCC 644

¹⁰ *Supra* 6

¹¹ (2015) 3 SCC 49

¹² *Ibid*, Para 31

Further, the Supreme Court in *Ssangyong Engg. & Construction Co. Ltd. v. NHAI*¹³ went a way forward to give more narrow interpretation to patent illegality as they laid down several limitation while deciding the award under said ground. The court held that the ground of patent illegality cannot be used as a backdoor to set aside the award when the impugned award is not in contravention to any public policy. Also the court stated that the test laid down in *Associate Builders* shall be construed in a strict sense while invoking the ground of patent illegality and said that “illegality” under patent illegality shall go into the root of the matter and must not amount to mere erroneous application of the law. Hence, the test and principles laid down under *Ssangyong Engg & Associate Builders* is the law of land while invoking ground of patent illegality. Recently, the Supreme Court of India while setting aside the arbitration award in *Patel Engineering Ltd. v. North Eastern Electric Power Corporation Ltd.*¹⁴ reiterated the test of reasonable man as laid down in *Associate Builders* and held that “no reasonable person could have arrived at a similar conclusion while interpreting the contract, as the sole arbitrator did; and that the arbitrator took into account various irrelevant factors in his decision, and ignored vital clauses of the tender documents. thus, the award suffered from the vices of irrationality and perversity, and suffered patent illegality.”¹⁵

III.) Was a separate ground necessary?

The recommendation of 246th Law Commission Report to formally introduce patent illegality as separate ground to set aside the arbitration award was made to do away with unintended consequences of the decision in *Saw Pipes* judgement “which, although in the context of a purely domestic award, had the unfortunate effect of being extended equally to both awards arising out of international commercial arbitrations as well as foreign awards.”¹⁶ As per the drafting of 1996 Act, the grounds for setting aside award under section 34 and conditions for refusal of enforcement of foreign award under section 48 are in pari-materia which causes extreme difficulty for legal practitioners to understand the scope of phrase ‘public policy’. The said difficulty could be noticed in *Phulchand Exports Limited v OOO Patriot*¹⁷ wherein the court extended the interpretation of public-policy in *Saw Pipes* case to set aside the foreign

¹³ (2019) 15 SCC 131

¹⁴ Special Leave Petition (C) 3584-85 of 2020

¹⁵ Ibid

¹⁶ 246th Law Commission Report

¹⁷ (2011) 10 SCC 300

award as well. As a result, enforcement of foreign award could be resisted if they were patently illegal. However, the court corrected its view adopted by it in *Phulchand Export* in the subsequent judgement, *Shri Lal Mahal Ltd v Progetto Grano Spa*¹⁸, wherein it was categorically stated that the scope of judicial interference in enforcing foreign award is minimal and hence, enforcement of a foreign award will be refused under Section 48(2)(b) only if it fulfils the categories set out in *Renusagar*.¹⁹ Therefore, in line with *Lal Mahal* and the recommendation in *246th Law Commission Report*, the Parliament enacted provision of patent illegality under section 34 to set aside domestic award in India.

The addition of patent illegality as ground to set aside domestic award clearly depicts the intention of court that “the legitimacy of judicial intervention in the case of a purely domestic award is far more than in cases where a court is examining the correctness of a foreign award.”²⁰ In other words, when it comes to domestic arbitration, our country is more keen to open the gates to judicial review the awards rendered by them. Whereas, at the same time, the proviso²¹ was also added to the provision to maintain balance and allow the courts to interpretate the said provision in harmonious manner to prevent any injustice caused to the party.

Conclusion

This paper examined the evolution of ‘patent illegality’ as a ground to set aside the domestic award and how it became the tool for judiciary to intervene in the arbitration law of the country. From adopting a wider view in *Saw Pipes* case to a narrow view in *Associate Builders*, the courts tried to interpretate patent illegality to maintain balance between growing need of independent arbitration law and to prevent injustice caused due to irrational awards passed by the tribunal. At the same time, the court and the parliament had made it categorically clear that the principle of patent illegality can only be invoked in domestic awards and not in foreign awards. The reason behind the same is the fact that courts have legitimate reasons to intervene in the proceeding governed by Indian laws through principle of patent illegality but, if the proceedings are governed by complex laws or public international laws then in that case the

¹⁸ (2014) 2 SCC 433

¹⁹ Supra 7

²⁰ Supra 15

²¹ Provided that an award shall not be set aside merely on the ground of an erroneous application of the law or by reappreciation of evidence.

higher satisfaction is required to intervene in the said proceedings.²²

To conclude, it is pertinent to mention that, in my opinion, I do not find strong reasons to justify the formal inclusion of patent illegality under section 34 of the 1996 Act. The scope of public policy discussed in *Saw Pipes* could have been dealt in great detail to lay down the principle of patent illegality through case laws.



²² Supra 17