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# Foreign awards under the judicial scanner

## INTRODUCTION

The Arbitration and Conciliation Act, 1996 (**"the Act"**) implemented UNCITRAL Model law on international commercial arbitration and added to the pro-arbitration legal regime in India. The basic intent was to have an expeditious and cost-effective dispute resolution mechanism with minimum supervisory role of courts. The restrictive mechanism of the courts and their non-interventionist approach got radically altered with the paradigm shift in the interpretation of the term "public policy" in various cases. The courts in India are now making a deliberate attempt to expand their extra territorial jurisdiction and intervene in the international arbitral awards.

With the Supreme Court (**"SC"**) deciding in *Venture Global Engineering v. Satyam Computer Services Ltd. & Another*[1] that foreign awards can be challenged in India under section 34 of the Act, the consequences of judicial interference in international commercial arbitration requires fresh examination. In the milieu of an open economy with various foreign companies actively investing in India, the present newsletter examines the commitment of Indian judicial system for an evolved alternate dispute resolution mechanism.

### 1.0 The Factual Matrix

A US-based company called Venture Global Engineering (**"VGE"**) had entered into a joint venture agreement with Satyam Computer Services Limited (**"SCSL"**) to constitute a company named as Satyam Venture Engineering Services Limited (**"SVESL"**) in which both VGE and SCSL had 50% equity shareholding. According to the shareholders agreement executed between the two partners, the governing law was that of Michigan, US and disputes were to be resolved amicably and, failing resolution, such disputes had to be referred to arbitration before the London Court of International Arbitration (**"LCIA"**).

In February 2005, SCSL alleged that VGE had committed an event of default under the shareholders agreement owing to several venture companies becoming insolvent and they had exercised its option to purchase the VGE shares in SVESL at its book value. Disputes arose between the parties and a reference was made to arbitration before LCIA. VGE entered appearance to defend this proceeding by filing a cross petition and opposing the transfer of shares. However, an award was passed directing VGE to transfer the shares to SCSL. Subsequently, a petition was filed by SCSL before the United States District Court, Eastern District Court of Michigan, to recognize and enforce the award.

VGE filed a suit in the civil court of Secunderabad in Andhra Pradesh, seeking to set aside the award under section 34 of the Act and a permanent injunction on the transfer of shares under the award. The court passed an ad-interim ex parte order of injunction restraining SCSL from effecting the transfer of shares either under the terms of the award or otherwise. The order was challenged in the High Court of Andhra Pradesh. On February 27, 2007, the High Court dismissed the appeal holding that the award cannot be challenged even if it is

[1] AIR 2008 SC 1061.



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against the public policy and in contravention of statutory provisions, as pleaded by VGE. The appellant VGE thereafter preferred an appeal by way of special leave petition before the SC. Respondent SCSL contented that in view of section 44 of shareholders agreement between the parties, no suit would lie in India to set aside a foreign award. The question before the SC was that whether Part I of the Act is applicable to international commercial arbitrations and if the arbitration clause in the shareholders agreement between the parties, would have overriding effect, thereby excluding the Respondent from approaching the US court for enforcement of the award.

## 2.0 The Observation and ruling of the SC

Prior to this judgment the judicial position is that Part I of the Act applies only to domestic awards and Part II applies to foreign awards. While examining the question of jurisdiction, the SC held that a proper and conjoint reading of all the provisions of the Act indicates that Part I of the Act applies to international commercial arbitration which takes place out of India, unless the parties by agreement, express or implied, had chosen to exclude it or any of its provisions. Section 34 of the Act falls within Part I of the Act. This means that the Indian courts have the power to intervene in foreign awards issued in international arbitrations held outside India. Accordingly, the court did not consider the application of section 34 to "foreign awards" as inconsistent with section 48[2] of the Act or any other provision of Part II that relates to foreign awards.

Further, the SC held that the non-obstante clause in section 11.5 (c) embodied in the shareholders agreement overrides the entire agreement. Section 11.5(c) reads as- "*notwithstanding that the proper law or the governing law is the law of the State of Michigan, their shareholders shall at all times act in accordance with the Companies Act and other applicable Acts/Rules being in force in India at any time.*"

Therefore, according to the SC regardless of the fact:

- that the award was issued outside India; and
- the parties had not expressly excluded the application of Part I of the Act in its contract; and
- in view of the non-obstante provision of the shareholders agreement, Indian law is applicable. This means that the parties have a right to go to court in India seeking an injunction against the enforcement of a foreign award.

While deciding this case the SC relied heavily on the case law of *Bhatia International v. Bulk Trading S.A. & Anr*[3], whereby the provisions of Part I of the Act was made available to parties even with respect to the enforcement of a foreign arbitration award in India. The reason behind the judgment in Bhatia's case was that the relief contained in the award was contrary to Indian public policy.

It is pertinent to mention here that the grounds for challenging an award rendered in India in a domestic or international arbitration are provided under section 34 and are materially the same as the New York Convention grounds for challenging an enforcement application. An award can be set aside under section 34 of the Act if:

- The party challenging the award furnishes proof that he was under some incapacity;
- That the arbitration agreement was not valid under the governing law;
- That the party was not given a proper notice of the appointment of an arbitrator or of the arbitral proceedings or was otherwise unable to present his case;
- That the award deals with a dispute not contemplated by or not falling within the terms of submission to arbitration or it contains decisions beyond the scope of the submission;
- The composition of the arbitral tribunal or the arbitral procedure was not in

[2] Section 48 deals with conditions of enforcement of a foreign award.

[3] (2002) 4 SCC 105.



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accordance with the agreement of the parties;

- In the opinion of the court, the subject-matter of the dispute is found not capable of settlement by arbitration under the law; and
- In the opinion of the court, the award is in conflict with the public policy of India.

Apart from the above, there are other additional grounds also which have evolved from the various precedents. For instance, where the arbitrator had acted in bias or where the award is an unreasoned award.

The concept of public policy evolved as an additional ground for challenging an award with *Renu Sagar*[4] wherein the SC presented a narrower interpretation of the doctrine. The central idea behind this policy has been that in no circumstance the aggrieved party is left with no recourse to justice and law should serve the purpose of justice. Subsequently, it was widely defined in *Oil & Natural Gas Corporation Limited v. Saw Pipes Limited.*[5] The SC explained that public policy shall include the fundamental policy of India or the interests of India or justice or morality or in addition, if an award is patently illegal. The application of the expanded interpretation of public policy to foreign awards is clearly *per incuriam*. In Patel Engineering case,[6] the SC sanctioned further court intervention in the arbitration process by stating that while adjudicating contentious preliminary issues like the existence of a valid arbitration agreement, the decisions of Chief Justice will be considered final and binding on the arbitral tribunal.

## 3.0 Implications

In the present case, the SC for the first time ruled that broadly interpreted public policy considerations that were previously available as grounds for challenging the domestic arbitration awards are now also appropriate grounds for challenging foreign arbitration awards. The decision has important implications for any foreign company that might be a subject of potential enforcement proceedings or may find itself involved in an arbitration proceeding in India or involving an Indian company.

Arbitration is the vastly preferred method of dispute resolution in most commercial contracts involving India. However, as a result of this decision, new risks exist with respect to the impact of Part I of the Act on contracting parties' rights and expectations in agreements involving India that contain arbitration clauses. When parties enter into transactions, they calculate the potential legal costs of enforcing their rights. Further, the additional risk factor associated with the dispute resolution mechanism or the enforcement procedure is measured and added to the cost of the transaction. A poor or a prolonged enforcement mechanism acts as a deterrent for any foreign investor.

Many foreign companies having relevant business interests in India have relied heavily upon Indian law based on the Act itself and already opted for arbitration procedures.

The case is far reaching for it creates a new ground for challenge to a *foreign award* which is not envisaged under the Act. Now a person seeking enforcement of a *foreign award* has to satisfy a dual test - i.e. make an application under section 34 of the Act seeking to set aside the award together with filing an application for enforcement under section 48 of the Act. So, now not only must the award pass the New York Convention grounds incorporated in section 48, it must also pass the expanded "public policy" ground created under section 34 of the Act.

The SC's decision did recognize, however, the right of contracting parties to address the application, in whole or in part, of Part I of the Act in their contracts. Therefore, while drafting the arbitration agreement the foreign companies having business relations with and in India may by agreement, express or implied, exclude all or any of the provisions of Part I of the Act in their arbitration clause, otherwise foreign awards can be challenged under sections 9 and 34 of the Act in India. Thus, while drafting the arbitration provision, it is advisable for a foreign contracting party to consider and incorporate the appropriate language (1) establishing the seat of the arbitration outside of India, and (2) expressly

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[4] Renusagar Power Co. v. General Electrical Corporation (1994) Suppl (1) SCC 644.
[5] (2003) 5 SCC 705.
[6] AIR 2008 SC1061.



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including a provision excluding Part I of the Act, if they do want Indian law to govern their agreements.

## CONCLUSION

Be that as it may, till this decision is clarified or modified, the enforcement mechanism of foreign awards has become uncertain with a cacophony of unrest created in the foreign stakeholders in India. However, in totality, India does not come across as a jurisdiction which carries anti-arbitration or, more significantly, which carries any anti-foreigner bias. Irrespective of a few instances as above, Indian courts have followed the non-interventionist scheme. To meet the current situation, the foreign parties must be very cautious and stay on top of the judicial interpretation so that appropriate safeguards are built in the commercial contracts. ***(Neeraj Dubey)***



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## Contact Lawyer

Priti Suri
p.suri@psalegal.com
Mobile +(91) 98100-92842

Neeraj Dubey
n.dubey@psalegal.com
Mobile +(91) 98186-04907

## Contact Details

PSA
Legal Counsellors
E-601, Gauri Sadan
5, Hailey Road
New Delhi – 110 001
India

Tel: + (91 11) 43500-500
Fax:+ (91 11) 43500-502



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