

# Dispute Resolution Hotline

July 19, 2013

## ENFORCEMENT OF FOREIGN AWARDS BECOMES EASIER: 'PATENT ILLEGALITY' REMOVED FROM THE SCOPE OF PUBLIC POLICY

The ever-growing judicial support to international commercial arbitration and the seminal shift in judicial mindset is now more than established from yet another landmark ruling of the apex court of the land in *Shri Lal Mahal Ltd. v.*

*Progetto Grano Spa*<sup>1</sup>, where the court has gone ahead to in fact overrule its own decision passed less than two years back. The Supreme Court while dealing with objections to enforceability of certain foreign awards on the grounds that such awards are opposed to the public policy of India, has significantly curtailed the scope of the expression 'public policy' as found under Section 48(2)(b) of the Arbitration and Conciliation Act, 1996 ("Act") and thereby have limited the scope of challenge to enforcement of awards passed in foreign seated arbitrations.

The judgment unmistakably establishes a difference between the scope of objections to the enforceability of a foreign award under Section 48<sup>2</sup> of the Act and a challenge to set aside an award altogether under section 34<sup>3</sup> of the Act.

### FACTS

The dispute arose out of a contract between an Indian seller ("Appellant") and a foreign buyer ("Respondent") whereby the Appellant had agreed to supply certain type of wheat to the Respondent. The Respondent had alleged that the wheat supplied was not of the quality as agreed to by the parties and as a result it had suffered significant damages.

The matter was referred to the Arbitral Tribunal of the Grain and Feed Trade Association, London ("GAFTA"), which passed an award in favour of the Respondent. Thereafter, the Appellant carried such award in appeal before the Board of Appeal of GAFTA, which also passed the award in favour of the Respondent. The awards were then challenged by the Appellant before the courts in U.K., where again the awards were upheld.

The Respondent then sought the enforcement of the awards in India in accordance with the provisions of the Act, to which the Appellant took objection by asserting that the award is against the public policy of India and accordingly enforcement of such awards in India ought to be refused.

The Appellant contended the award to be opposed to public policy of India on the ground that such award was contrary to clearly terms of the contract entered into by the parties. The questions pertained to the certification provided by the expert regarding the quality of the wheat and whether such certification was in the form which was agreed by the parties.

The Respondent on the other hand argued that the matters as raised by the Appellant were questions regarding appreciation of evidence and were questions of fact which could not be gone into at the stage of challenge to enforcement of a foreign award under section 48 of the Act.

### ISSUE

Thus, issue arose regarding the scope and interpretation of the expression 'public policy' which is provided as a ground to refuse enforcement of a foreign award under section 48(2)(b) of the Act and whether the enforcement of the awards could be refused on the grounds as alleged by the Appellant.

The issue further was whether the expression 'public policy' shall have the same meaning and purport under section 34(2)(b)(ii) and section 48(2)(b) of the Act?

### JUDGMENT

As the question revolved around the interpretation of the scope of the expression '*public policy*' the Supreme Court considered the following three landmark rulings in this regard:

1. *Oil and Natural Gas Corporation Ltd. v. Saw Pipes Ltd.*<sup>4</sup> ("ONGC");
2. *Phulchand Exports Limited v. O.O.O. Patriot*<sup>5</sup> ("Phulchand"); and
3. *Renusagar Power Co. Limited v. General Electric Company*<sup>6</sup> ("Renusagar").

The Supreme Court overruling the judgment in Phulchand held that the meaning of the expression 'public policy' under Section 48 was narrower as compared to section 34. Relying on Renusagar, the Court made a highly important observation that there is a fine distinction between applying the rule of public policy in a matter governed by domestic laws and a matter involving conflict of laws as is the case in majority of international commercial arbitrations. The court observed that the applicability of the doctrine of public policy is comparatively limited in cases

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involving conflict of laws and matters involving foreign element such as a foreign seated arbitration, the courts would not be easily inclined to invoke such doctrine.

The court further observed that ONGC dealt with a situation where the arbitral award was sought to be set aside under section 34 as opposed to an application to refuse enforcement of an award under section 48. **It was stated that the expression 'public policy of India' under 34 was required to be interpreted in the context of the jurisdiction of the court where the validity of the award is challenged before it becomes final and executable in contrast to enforcement of award after it becomes final.** Thus, it was seen that under Section 34 the expression public policy would also entail within its folds any 'patent illegality' for setting aside the award.

Accordingly, the court held that:

*"enforcement of foreign award would be refused under Section 48(2)(b) only if such enforcement would be contrary to*

1. *fundamental policy of Indian law; or*
2. *the interests of India; or*
3. *justice or morality.*

*The wider meaning given to the expression "public policy of India" occurring in Section 34(2)(b)(ii) in Saw Pipes (ONGC) is not applicable where objection is raised to the enforcement of the foreign award under Section 48(2)(b)."*

Thus, relying on the above law, the Supreme Court observed that the same ground had also been raised by the Appellant before the courts in U.K. to have the award set aside. However, the High Court of Justice at London did not consider the ground to be sufficient enough for the award to be set aside. Thus, the court viewed that the same argument could hardly be good enough to refuse enforcement. The court further provided that section 48 does not offer an opportunity to have a second look at the foreign award at the enforcement stage. The court affirmed that section 48 does not permit review of the award on merits and also that procedural defects in course of foreign arbitration do not necessarily imply that foreign award would be unenforceable. Accordingly, the appeal was dismissed by the court and that award was held to be enforceable.

## ANALYSIS

The judgment in ONGC led to expansion of the meaning of the expression 'public policy' as provided under section 34 of the Act, which opened the floodgates to petitions challenging the arbitral award on the ground of 'patent illegality'. The decision was criticized as it allowed the parties to have a second bite at the matter, to the extent that the ground of patent illegality was viewed broad/y.

The above decision coupled with the pre- BALCO<sup>7</sup> scenario i.e. applying the law as enunciated under the Bhatia International case<sup>8</sup>, permitted awards passed in arbitrations seated outside India to be challenged under section 34 in certain cases. This led to a very broad ground being available to parties to set aside awards passed in international commercial arbitrations. Though, the BALCO decision has now clarified that awards passed in foreign seated arbitrations<sup>9</sup> cannot be challenged under section 34, the difficulty arose on account of the judgment of Phulchand.

Phulchand<sup>10</sup> expanded the meaning of the expression 'public policy' as provided under section 48 of the Act and provided that the scope and purport of the expression under section 34 and 48 would be the same. The decision of Phulchand thus also received heavy criticism. Surprisingly, Hon'ble Justice R.M. Lodha, who previously wrote the judgment in Phulchand on behalf of the bench has now himself, overruled the decision of the court of Phulchand and it has now been laid down that the meaning of the expression 'public policy' is narrower under section 48 as compared to section 34.

Therefore, now enforcement of foreign awards would not be refused so easily. Thus, a practical takeaway from the above would be to give preference to a foreign seated arbitration as a mechanism for dispute resolution as this would afford a speedy remedy without significant court interference.

- Ashish Kabra, Payel Chatterjee and Vyapak Desai

You can direct your queries or comments to the authors

<sup>1</sup> Civil Appeal No. 5085 of 2013 arising from SLP(c) No. 13721 of 2012

<sup>2</sup> **48. Conditions for enforcement of foreign awards.**

(2) Enforcement of an arbitral award may also be refused if the court finds that-

(a) the subject-matter of the difference is not capable of settlement by arbitration under the law of India; or

(b) the enforcement of the award would be contrary to the public policy of India.

Explanation: Without prejudice to the generality of clause (b), it is hereby declared, for the avoidance of any doubt, that an award is in conflict with the public policy of India if the making of the award was induced or affected by fraud or corruption

<sup>3</sup> **34. Application for setting aside arbitral award.**

(1) Recourse to a Court against an arbitral award may be made only by an application for setting aside such award in accordance with sub-section (2) and sub-section (3).

(2) An arbitral award may be set aside by the Court only if

(a)

(b) the Court finds that

(i) the subject-matter of the dispute is not capable of settlement by arbitration under the law for the time being in force, or

(ii) the arbitral award is in conflict with the public policy of India.

Explanation: Without prejudice to the generality of sub-clause (ii), it is hereby declared, for the avoidance of any doubt, that an award is in conflict with the public policy of India if the making of the award was induced or affected by fraud or corruption or was in violation of section 75 or section 81.

<sup>4</sup> (2003) 5 SCC 705

<sup>5</sup> (2011) 10 SCC 300

<sup>6</sup> 1994 Supp (1) SCC 644

<sup>7</sup> *Bharat Aluminium Company and Ors. v. Kaiser Aluminium Technical Service, Inc. and Ors.*, (2012) 9 SCC 552

<sup>8</sup> *Bhatia International v. Bulk Trading S.A. and Anr.*, (2002) 4 SCC 105

<sup>9</sup> Where the arbitration agreement has been entered into after September 6, 2012

<sup>10</sup> Please refer to our hotline titled *"Enforcement of Awards- Erasing the distinction between Domestic and Foreign Award"*

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