UNCERTAINTY IN LIMELIGHT: A CASE COMMENT ON *SASAN POWER LTD. V. NAAC INDIA PVT. LTD.*

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Abstract

*The law regarding arbitration in India has been under the scanner recently due to the implementation of the recent amendments to the Arbitration and Conciliation Act of 1996, ("**the Act**") and more so because of the string of cases that arose due to the lacunae present in the law and the subsequent attempt by the judiciary to remove such creases through its interpretation. In light of this increasingly pro-arbitration stance taken by the judiciary as well as the legislature, the case of Sasan Power Ltd. v. NAAC India Pvt. Ltd. deserves a great deal of emphasis, as it raises convoluted issues that have plagued the Indian arbitration policy for a long time.*

This paper seeks to examine the questions posed by this case, the first being whether two Indian parties to an arbitration agreement can derogate from Indian law and if the same is contrary to the public policy of India; and

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the second relating to the circumstances that mandate the application of Part I, Part II or both these Parts of the Act, in lieu of various Supreme Court cases that outlined many scenarios regarding the application of the same. Further, the paper analyses the Court's application of the doctrine of severability in furtherance of its decision to include the review of the arbitration agreement only under the purview of Section 45 and not the substantive contract, while also examining the effect of this judgment on the competence of the tribunal to rule on its own jurisdiction.

Through a normative analysis, this paper tries to fulfill its objective of showcasing the impact that this judgment has in arriving at a conclusive answer which untangles existing uncertainties.

I. INTRODUCTION

The Indian arbitration framework and policy has witnessed a lot of hurdles in its path of proving arbitration to be a feasible method of dispute resolution. There have been various improvements in this scheme to tackle the same, such as the recent amendment to the Act,[1] and recent judicial pronouncements which have a pro-arbitration inclination. This has been done in an effort to make the Indian arbitration scheme less prone to judicial intervention and to make

[1]The Arbitration and Conciliation (Amendment) Act, 2015.

India a better seat for arbitration in accordance with international standards.

At the outset, it would be appropriate to outline the demarcation between the two sections of the Act divided on the basis of the juridical seat of the award. While Part I provides the mechanism for interim measures, relief to be provided by court and procedure for filing objections against awards in case of arbitrations conducted in India, Part II contains the same provisions for foreign awards, that is, awards rendered outside of India, in addition to provisions that provide the procedure for enforcement of foreign awards in India.

Part I of the Act has received considerable judicial interpretation in light of the circumstances that arose in various cases in the past decade or so.

One of the most recent cases in this arena is *Sasan Power Ltd. v. North American Coal Corporation India Pvt. Ltd.*[2] (‘***Sasan Power***’), which has a massive impact on the applicability of the Act to international commercial arbitrations.

A. Facts

The facts of the case are as follows. On January 01, 2009, an agreement (“**Agreement-I**”) was entered into between Sasan Power Limited (“**Appellant**”). and North American Coal Corporation, an American Company, incorporated in Delaware (“**NACC USA”)**, as per which NACC USA would provide consultancy services and other services for a mine to be operated by the Appellant in India. Subsequently, another agreement (“**Agreement-II**”) was entered into on April 04, 2011 between the Appellant, NACC USA and North American Coal Corporation India Private Limited (“**Respondent**”) by

[2]Sasan Power Ltd. v. North American Coal Corporation India Pvt. Ltd, 2016 SCC OnLine SC 855.

which NACC USA assigned all its rights and obligations to the Respondent, with the consent of the Appellant. However, the Agreement-II specifically provided for a clause that NACC USA's transfer and assignment of all its rights and obligations under the Agreement to the Respondent, would not release NACC USA, as assignor, from its obligations under the Agreement.

Section 12 of the agreement contained an arbitration clause for resolution of disputes, with the governing law of the agreement being the law of United Kingdom and the place of arbitration being London. The arbitration was to be administered by the ICC International Court of Arbitration ("**ICC**") and in accordance with the ICC Rules. The agreement also expressly excluded the application of Part I of the Act, saving Section 9 of the same.

Disputes arose between the parties, and the Respondent requested the same to be referred to arbitration August 8, 2014. The Appellant assailed the validity of the same as well as of the arbitration agreement before the District Court of Singrauli, Madhya Pradesh. An *ex-parte* order was passed whereby an injunction was given that prevented ICC from proceeding with the arbitration. The Respondent filed two Interlocutory Applications praying that the disputes be referred to arbitration as well as for seeking vacation of the injunction order. Both these applications were granted. Hence, the Appellant approached the High Court of Madhya Pradesh ("High Court"), which dismissed the appeal on the ground that once the parties have mutually agreed to resolve their disputes by arbitration and have chosen the seat of arbitration in a foreign country, then in view of the provisions of Section 2(2) of, Part I of the Act will not apply as this Part is applicable only when the place of arbitration is India. Once the agreement fulfils the conditions of Section 44 of the Act, then Part II will apply. Further, once the agreement is found to be not null or void or inoperative, then the bar created by Section 45 (which creates a bar on the jurisdiction of the Court from adjudicating a dispute when

there is a valid arbitration agreement) would come into play, which makes it mandatory for the Court to refer the parties to arbitration.

B. Issues

The Appellant approached the Supreme Court by way of a Special Leave Petition, wherein the primary issues which arose were, firstly, whether it was permissible under the consolidated Indian law of arbitration for two Indian Companies (each incorporated and registered in India) to agree to refer their disputes to a binding arbitration, with place of arbitration outside India, and with governing law being English law. Secondly, whether the two parties to the dispute, each of whom are companies incorporated and registered in India, could in law be said to have made an agreement referred to in Section 44 of the Act, so as to confer jurisdiction and authority on the competent Court to refer the parties to ICC arbitration in London under Section 45 of Act. Thirdly, whether the arbitration agreement contained in Section 12 of the agreement was invalid and void for being in breach of Section 28(a) of the Indian Contract Act, 1872 ("**Contract Act**"**),** not being saved by the exception clause, and also void because of the provisions of Section 23 of the Contract Act and hence, not referable to arbitration under Section 45 of the Act.[3]

II. CONFRONTING THE PITFALL

While considering the first issue, the Supreme Court battled with the nature of the contract and the parties to the arbitration agreement, as well as which Part of the Act would apply to the case at hand. For this purpose, the Court referred to previous cases that dealt with these issues.

[3] ¶13, Sasan Power.

The Supreme Court referred to *Bhatia International Bulk Trading S.A. & Another*[4] ("**Bhatia International**"), which considered the question of whether Part I of the Act would apply to an arbitration where the place of arbitration is outside India. It ruled that the provisions of Part I would apply to all arbitrations. It was specifically stated that when an arbitration was held in India, the provisions of Part I would completely apply and parties are free to deviate only to the extent permitted by the derogable provisions of Part I; and in cases of international commercial arbitrations held outside India, provisions of Part I would apply unless the parties by agreement, express or implied, excluded all or any of its provisions.[5]

The same position was taken further in *Venture Global Engg. v. Satyam Computer Services Ltd.*,[6] where it was held that a foreign award would also be considered as a domestic award and the procedure for challenge provided in Section 34 of Part I of the Act would therefore apply. This led to a situation where the foreign award could be challenged in the country in which it is made; it could also be challenged under Part I of the Act in India and could be refused to be recognized and enforced under Section 48 contained in Part II of the Act.

Both these cases were overruled in *Bharat Aluminum Co. v. Kaiser Aluminum Technical Services* ("**BALCO"**).[7] It stated that Part I of the Act would not apply to international commercial arbitrations held outside India[8] and the same was given a prospective effect from September 06, 2012. Thus, this law will not apply to the present case as it is an arbitration agreement entered into prior to September 06,

[4]Bhatia International v. Bulk Trading S.A. & Another, (2002) 4 SCC 105.
[5]¶32, Bhatia International.
[6]Venture Global Engg. v. Satyam Computer Services Ltd, (2008) 4 SCC 190.
[7]Bharat Aluminium Co. v. Kaiser Aluminium Technical Services, (2012) 9 SCC 552.
[8]¶194, BALCO.

2012 and hence, the law laid down in Bhatia International will hold true.

The same was re-iterated by the Supreme Court in *Harmony Innovation Shipping Ltd. v. Gupta Coal India Ltd. & Anr.*,[9] where it was held that pre-*BALCO* arbitration agreements must be considered based on the principles laid down in *Bhatia International*. Also, a host of circumstances were laid down in which Part I would be excluded, which included the existence of a foreign seat, and the choice of the substantive law of a foreign country.

Further, the Supreme Court of India in *Union of India v. Reliance Industries Limited & Ors*[10] held that in a pre-*BALCO* agreement, Part I will be impliedly excluded if either, the parties decided on a foreign seat; or if the parties agreed on a foreign law to govern the arbitration agreement.

In the present case, the question of whether Part I or Part II or both apply arose. Since the law laid down in Bhatia International applied, it was a question of whether the arbitration agreement was in conformity with the test laid down in *Bhatia International*.

To determine this question, three factors were considered, namely, the parties to the arbitration agreement, the venue of arbitration and whether in a foreign seated arbitration, where one of the parties is a non-Indian entity, the parties have agreed to exclude the application of Part I of the Act or not.[11]

Here, the Court ruled that the arbitration agreement was not between two Indian parties, but rather, that it was a tripartite agreement. The Court delved into Agreement-II between the parties and held that the

[9]Harmony Innovation Shipping Ltd. v. Gupta Coal India Ltd. & Anr., 2015 (3) SCALE 295.
[10]Union of India v. Reliance Industries Limited & Ors, (2015) 10 SCC 213.
[11]¶39, Bhatia International.

Respondent would be liable in the same manner as NAAC USA since Agreement-II amended Agreement-I. The Court reasoned this by concluding that there was neither an assignment nor a novation of the contract.

At this stage, it is worth mentioning that an assignment is a contract whereby a party to the original contract assigns all benefits arising out of it to a third party, but not the obligations under the contract. Whereas, a novation is where the original contract is replaced, and the debt extinguished in place of a new contract. Since Agreement-II, in the instant case transferred obligations as well, and did that by way of an amendment, the court did not consider it an assignment or novation.

Thus, the Appellants' assumption that the second contract was between only two Indian parties was disregarded, since the second agreement was a tripartite contract with two Indian parties and one American company, thereby incorporating a 'foreign element', i.e., rights and obligations of the NAAC USA.[12] Thus, the stipulation regarding the governing law cannot be said to be an agreement between only two Indian companies.

Since the agreement had a non-Indian entity as a party (NAAC USA is an American company and a party to Agreement-II), it became an "international commercial arbitration" within the meaning of Section 2(f) of the Act which provides that if one of the parties to the agreement is a foreign entity, then such an agreement would be regarded as an international commercial arbitration.

Further, since the venue of the arbitration was London and Section 12 of the agreement stated that excluding Section 9, Part I of the Act would not apply, the test of exclusion as laid down in *Bhatia International* is satisfied. Therefore, only Part II of the Act applies.

[12] ¶24, Sasan Power.

With respect to the second issue regarding whether the suit is maintainable or barred by Section 45 of the Act, it is pertinent to note that Section 45 of the Act permits an enquiry into the question of whether the agreement is 'null and void, inoperative and incapable of being performed'. In the event that it meets the aforementioned criteria, the judicial authority to whom the dispute (for which the parties have made an agreement for 'international commercial arbitration')[13] has been referred to, is precluded from referring the parties to arbitration. It is here that the doctrine of separability and the principle of competence-competence must be analyzed.

The doctrine of separability is a general principle of international law, accepted unilaterally by institutions and also accepted in most common law jurisdictions. For example, in England, the Arbitration Act was amended in wake of the ruling in *Harbour v. Kansa*,[14] to include the application of this norm.[15] In India, the adoption of Article 16(1)[16] ad verbatim from the UNCITRAL Model Law on International Commercial Arbitration has made it mandatory for arbitral tribunals to rule on their own jurisdiction.

This doctrine states that the arbitration agreement is an independent or "self-contained" agreement, autonomous from the substantive contract. Thus, it is through the application of this doctrine that the competence-competence principle, i.e. the competence of a tribunal to rule on its own jurisdiction, is upheld, as opposed to a court ruling upon it. Although this principle is applicable to arbitral tribunals, the tribunal does not have absolute discretion to rule on the validity of the arbitration agreement since it is subject to other forms of statutory

[13]Arbitration and Conciliation Act, 1996, § 44.
[14]Harbour Assurance Co. Ltd. v. Kansa General International Insurance Co. Ltd. et al., (1993) QB 701.
[15]Arbitration and Conciliation Act, 1996, c.2, § 7 (Eng.).
[16]United Nations Commission on International Trade Law, UNCITRAL Model Law on International Commercial Arbitration 1985: with amendments as adopted in 2006, art. 16(1), U.N. Doc. A/40/17 (2008).

review by civil courts post-award. The Supreme Court has held that the arbitral tribunal's authority under Section 16 of the Act goes to the very root of its jurisdiction.[17] However, the Supreme Court has also held that the tribunal does not have the freedom to ignore any ruling of judicial authorities under Section 11(7) of the Act. The latter has been criticized as undermining the concept of *Kompetenz-Kompetenz* and being contrary to the legislative policy as laid down in Section 16 of the Act.[18]

In this case, the Supreme Court upheld the doctrine of separability of the arbitration agreement. Thus, the scope of enquiry was limited to legality of the arbitration agreement and not the substantive contract. This has resulted in the Court upholding the autonomy of the arbitration tribunal, as the tribunal now has the freedom to determine the validity of the contract in accordance with the conflict of law principles of United Kingdom.

It is necessary to understand the scope of review under Section 45 of the Act. The statute provides for considering whether the arbitration agreement is 'null and void, inoperative or incapable of being performed' before the dispute is referred to arbitration. Whether this shall include an extensive review on the grounds or only prima facie review has been considered by the Supreme Court previously in *Shin-Etsu v. AkshOptifibre*,[19] in which the Court comprehensively examined the scope of review in other Model Law Countries and observed that not only is the Section[20] copied ad verbatim from the

[17]Konkan Railway Corporation Ltd. v. Rani Construction Pvt. Ltd., (2002) 2 SCC 388.
[18]Indu Malhotra, The Law And Practice Of Arbitration And Conciliation 773 (3rd ed., 2014).
[19]Shin-Etsu v. AkshOptifibre, (2005) 7 SCC 234.
[20]Arbitration and Conciliation Act, 1996, § 45.

UNCITRAL Model Law,[21] other model law jurisdictions including Switzerland and France provide only for a prima facie review of the arbitration agreement. Hence, the Court held that the fact that arbitration proceedings are stayed till the decision of the court is rendered in such appeals, coupled with the presence of various other factors (including determination of foreign law applicable, cost to the parties, etc.), make a final review of the contract at the pre-reference stage inconvenient. Therefore, it was held that courts should only conduct a prima facie review of the validity of the arbitration agreement, with expeditious disposition of the appeal (within 3 months). The Court held that there is provision for an extensive review provided post-award in Section 48 of the Act.

In the instant case, the court cited *Hindustan Petroleum Corpn. Ltd. v. Pinkcity Midway Petroleums*,[22] which held that any question with respect to the applicability of the arbitration clause to the facts of the case will have to be raised before the Arbitral Tribunal concerned. The Court also applied the analogy of a civil court, which states that if a civil court is precluded from deciding the jurisdiction of the arbitration agreement, then the civil court cannot decide the validity of the substantive agreement under Section 45 of the Act as well.

With respect to the third issue that deals with whether the agreement was invalid due to being contrary to public policy, the Appellant alleged that the arbitration agreement is contrary to Section 23 of the Contract Act as it was contrary to public policy. The term public policy has been described as an 'unruly horse'[23] due to the vast criteria under which an agreement can be assailed by applying this

[21]United Nations Commission on International Trade Law, UNCITRAL Model Law on International Commercial Arbitration 1985: with amendments as adopted in 2006, U.N. Doc. A/40/17 (2008).
[22]Hindustan Petroleum Corpn. Ltd. v. Pinkcity Midway Petroleums, (2003) 6 SCC 503.
[23]Gherulal Parekh v. Mahadeodas, AIR 1959 SC 781.

restriction. Hence, it should be used in rare cases by the courts to outlaw that which would affect public interest.[24]

As aforementioned, the court refused to consider whether the substantive contract violates public policy for the mere reason that it is the validity of the arbitration agreement which is under review in Section 45 of the Act and not the validity of the substantive contract.

III. EFFECT OF THE SASAN DECISION

While the Supreme Court held that the legality and validity of the substantive contract is not to be questioned in a case under Section 45 of the Act in a pro-arbitration spirit, there is yet another question that remains unanswered in this judgment. The most important issue put forward by the Appellant in this case was whether two Indian parties can agree to refer their commercial disputes to a binding arbitration, with place of arbitration outside India, and with governing law being a foreign law. The Supreme Court did not deal with this issue at all and merely applied the test as laid down in Bhatia International as it concluded that the tripartite agreement included a foreign party. It simply upheld the ruling of the High Court regarding the same arbitration agreement.

The effect of derogation from Indian law by two Indian parties is still uncertain. The issue lacks a conclusive judgment on the same. While it is argued that the choice of the parties as to which law must apply is paramount in arbitration, others argue that contracting out of Indian law would violate public policy.

Ironically, while the High Court ruling stated that two Indian parties can opt out of domestic law in the context of arbitration (with a

[24]Ratanchand Hirachand v. Askar Nawaz Jung, AIR 1976 AP 112.

foreign seat and with a foreign substantive law) and that the resultant award would be a 'foreign award' as envisaged under Part II of the Act, the Supreme Court ruling did not touch upon this issue at all, and instead chose to recognize the existence of a foreign element in Agreement-II and concluded that the arbitration can be under foreign law.

There have been other observations made in different cases. In *TDM Infrastructure Pvt. Ltd. v. UE Development India Ltd.*[25] ("**TDM Infrastructure"**) before the Supreme Court, which was relied upon by the *Bombay High Court in Adhar Mercantile Pvt. Ltd. v Shree Jagdamb,*[26] ("**Adhar**") later, the Courts relied on Section 28 of the Arbitration and Conciliation Act of 1996 and stated that two Indian parties cannot opt for a foreign law to govern their contract as it would violate Section 23 of the Contract Act and result in being contrary to public policy. Section 23 of the Contract Act states that agreements that have considerations that are unlawful shall be void. The category of violating 'public policy' falls within the category of unlawful considerations.

The question of whether two Indian parties can opt for a foreign seat or a foreign law governing the arbitration agreement has not been explicitly dealt with and remains unanswered; although, based on the judgments in *TDM Infrastructure* and *Adhar*, it is possible to reason that two Indian parties can do so as neither of the two judgments make any reference to a situation which entails a foreign seat of arbitration or a foreign law governing the arbitration. Thus, Indian parties are free to choose a foreign seat of arbitration or a foreign law governing the arbitration agreement. Such an interpretation is consistent with *BALCO's* interpretation of Section 28 of the Act

[25]TDM Infrastructure Pvt. Ltd. v. UE Development India Ltd, (2008) 14 SCC 271.
[26]Adhar Mercantile Pvt. Ltd. v Shree Jagdamb, Arbitration Application No 197 of 2014, along with Arbitration Petition No. 910 of 2013, (Bombay HC, 12/06/2015).

wherein it had only read substantive law under Section 28 (not a foreign seat of arbitration or a foreign law governing the arbitration) with an intention to ensure that two or more Indian parties do not circumvent to substantive Indian law by resorting to arbitration.

The High Court in its analysis held that two Indian parties can choose a foreign seat and held the findings concluded in *TDM Infrastructure* and *Adhar* to be obiter dicta as they dealt with issues with respect to jurisdiction under Section 11 of the Act concerning the appointment of an arbitrator. These cases never dealt with the question of whether two Indian parties can contract out of Indian law or whether a contract can be governed by a foreign law. The High Court also considered *Atlas Exports Industries v. Kotak & Company*,[27]which supported party autonomy and held that an award passed by a foreign seated tribunal was not unenforceable or contrary to public policy with respect to Section 28 of the Act and Section 23 of the Contract Act. Thus, the High Court judgment allowed parties to choose a foreign seat and indirectly adopted a position taken by the Supreme Court in *Reliance Industries Ltd. v. Union of India*,[28] in which a challenge to an award arising from a foreign seated arbitration between two Indian parties was dismissed.

Although the Supreme Court has remained completely silent on this issue, the answer can be inferred by the implied recognition of autonomy of parties to choose a foreign seat, as was upheld by the High Court judgment. Further, it must be noted that due to the law set forth in *BALCO*, Section 28 of the Act deserves no consideration in foreign seated arbitrations since the jurisdiction of Indian Courts under Part I of the Act is impliedly excluded and further under the

[27]Atlas Exports Industries v. Kotak & Company, (1997) 7 SCC 61.
[28]Reliance Industries Ltd. v. Union of India, (2014) 7 SCC 603.

Bhatia International regime, if the arbitration agreement provides for a foreign-seated arbitration.[29]

Thus, *Sasan Power* has thrown light on the convoluted issue of whether two Indian parties can choose a foreign seat or a foreign law to govern their arbitration agreement and has had a significant impact in paving the path of solving this dilemma, but failed on the account of not giving any explicit and authoritative answer. Hence, uncertainty still looms around this issue and one can only await another precedent to guide parties towards a more hassle free arbitration experience.

[29]Supra note 10.