PUBLIC POLICY IN ARBITRATION

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ABSTRACT

The paper examines the concept of public policy which has been frequently used by the parties to international arbitration to resist enforcement of arbitral award. In India through series of court decision development of internationally accepted concept of public policy has been hampered by of national court. The author in the paper has extensively discussed about how the concept and jurisprudence around public policy has developed over years and how it was viewed by the Indian Courts. The paper examines as to how the interpretation of word ' Public Policy' has been done by Indian courts and how concept has been used as a mechanism to hinder the process of enforcement of foreign award which itself contradict the basis of Arbitration Act. The paper throws light on concept of public policy , interpretation by court and critical analysis of same.

Key Words: Public Policy, Arbitral Award, International Commercial Arbitration, Indian Arbitration Act , UNCITRAL Model Law

INTRODUCTION

In India, arbitration is governed by Indian Arbitration and Conciliation Act 1996. The main purpose of arbitration is minimal intervention by the court and parties autonomy to settle their dispute. But there are certain situation in which court has the right to intervene either to protect the individual right or for good of public at large. Section 34 of Part 1 which is applicable to domestic arbitration and Section 48 of Part II which is applicable to foreign arbitration gave power to court to set aside the award or refuse to enforce the award. There are various ground used by parties to challenge the decision of arbitral tribunal in the court of law. Public Policy is one the most frequently ground used by the parties to international arbitration to resist enforcement of arbitral award.[1] It is one of the most controversial and highly debated subject till date because of the diverse approach taken by the national courts in relation to concept of public policy. Although through arbitration laws, amendment it was tried to align the concept of public policy so that parties may benefit from a universally accepted concept of public policy, the difference in attitude of national courts has made this task virtually impossible. In India, through series of court decision development of internationally accepted concept of public policy has been hampered. National courts plays an important role in different phase of arbitral process , their role is perhaps most important once the arbitral award is rendered i.e. when it comes to enforcement of the award which must survive the statutory condition of the place where the award is to be enforced. Once an arbitral award has been rendered, national courts may refuse to enforce it one the ground mentioned in Article V of New York Convention. Article V safeguards the basic rights of parties in international arbitration by providing various grounds to challenge the enforcement of arbitral awards.[2] These conditions has been incorporated in national legislation on most of the countries signing the Convention and adopting the UNCITRAL Model Law.[3] Indian arbitration act 1996 is also the exact reproduction of UNCITRAL Model Law . Public Policy is important weapon in the hands of national court giving power to refuse the enforcement of arbitral award. This defense is incapable of being determined as its application depends upon the law of individual states and New York convention does not provide any guidance as to how public policy defense should

[1] Sameer Sattar, Enforcement of arbitral award and public policy : same concept different approach?
[2] Ibid.
[3] Supra 1

be interpreted.[4] Despite being uncertain, public policy has been interpreted narrowly by national courts.

1. CHAPTER 1 – PUBLIC POLICY AND ENFORCEMENT OF ARBITRAL AWARD

In arbitration public policy is commonly used to decide the validity of award and thus most widely used exception to award enforcement and setting aside the award or refuse to enforce the award in both national and international arbitration. In arbitration act 1996, section 34 deals with setting aside the award which is applicable to domestic award in Part 1 and section 48 deals with refusing to enforce the award which is applicable to foreign arbitration in part 2. Public Policy is described many a times as untrustworthy guide, unruly horse etc. it is the anvil on which legal system of a state operates, but it is an undefined concept and cannot be restricted to contours of definitive words.[5] Public Policy is the principal of judicial legislation and founded on the current needs of society. The rationale being, while parties have the autonomy to enter into contracts, when that autonomy is outweighed by public interest or when such autonomy does overboard the outlines of public interest, a court will refuse to enforce the contract.[6] In line with the ethos of the UNCITRAL Model Law, the Indian Arbitration Act was introduced with the hope that there will be minimal judicial intervention in the arbitral process. Despite this, the Indian courts have shown a great propensity towards interfering with international arbitration. In this connection, judicial intervention at the award enforcement stage on grounds of public policy is the most controversial. *Renusagar v. General Electric*[6] has been always considered as a initial point where one apprehend the intervention of Indian court on the ground of Public policy. The case involved the GAFT arbitration in Paris between the parties where the tribunal passed the order against Renusagar which general electric sought to enforce in Bombay. The award was challenged on the ground of public policy of India under 1961 Act. Court held that term public policy should be given narrow interpretation. SC made it clear that enforcement of foreign award would be refused on ground that it is contrary to public policy if, such enforcement would be contrary to 1. Fundamental policy of Indian law 2. The interest of India 3. Justice or morality.[8] The decision confirmed the position that only in exceptional circumstances, domestic court interfere with arbitral award on grounds on

[4] Supra 1
[5] Gracious Timothy, The final chapter to the public policy saga: the Arbitration Amendment Act 2015, Indian Arbitration law review 2016 [6] Ibid.
[6] Renusagar v. General Electric 1994 AIR SC 860 [8] Ibid.

public policy. But in contrast to its decision in above case the court took altogether different stand in *Oil & Natural Gas Corp v. Saw pipes*[7] and disregarded the commonly accepted principles of public policy. The case of Saw pipes arose out of dispute regarding the payment of liquidated damages under supply contract and the same was referred to arbitration and an award was rendered in which it was held that ONGC is not entitled to damages since it failed to establish any loss as a result of late supply. ONGC challenged the award before the Indian court on ground of public policy. In that case SC held that public policy is required to be given wider meaning because public policy connoted matter which concerned public good and public interest. SC held as per law ONGC was not required to prove its loss and entitled to damages. The SC felt that award violating the law could not to be said in public interest as it affect the administration of justice and thus in addition to three heads set forth in Renusagar case, arbitral award may be set aside on grounds of public policy if it is patently illegal. It held that an award was patently illegal if the award was contrary to the substantive law, the Indian Arbitration Act and/or the terms of the contract. The effect of this was that these included any error of law committed by the arbitrators. Another case which shows that act by court defeating the very purpose of arbitration is *Bhatia International v. Bulk trading*[8] in which the SC held that provisions of Part I of arbitration act 1996 which apply only to domestic arbitration would now also apply to Part II which is applicable on foreign award unless specially excluded. This means that parties relying on Bhatia could use patent illegality ground added in saw pipes as a fourth head to resist the enforcement of foreign arbitral awards. In 2008, the court went further in *Venture Global Engineering v. Satyam Computer service*, [9]that even though there was no provision in Part 2 of act for challenge to a foreign arbitral award, a petition to set aside the same could be lie under Part 1 of Act i.e. foreign award could be now challenged under section 34 of act. The same was overruled in *Bharat Aluminium Co Ltd. v. Kaiser Aluminium Technical Service Inc.*[10] in which it was stated by court that Part 1 of 1996 act would not be applicable to an arbitration not seated in India. In *Phulchand Exports Ltd v. OOO Patriot*,[11] SC expanded the meaning of 'public policy' under section 34 and 48 of act and now the award can be set aside under section 48 if it is ' patently illegal'. The decision was overruled in *Lal Mahal Ltd v. Progetto Grano Spa*,[12] in which it was held that expression 'public policy' under

[7] Oil and Natural Gas Corp v. Saw pipes, (2003) 5 SCC 705
[8] Bhatia International v. Bulk Trading, (2002) AIR SC 1432
[9] Venture Global Engineering v. Satyam Computer Service (2008) S.C.A.L.E. 214
[10] Bharat Aluminium Co ltd v. Kaiser Aluminium Technical Service Inc (2012) 9 SCC 649
[11] Phulchand Exports Ltd v. OOO Patriot, (2011) 10 SCC 300
[12] Lal Mahal Ltd v. Progetto Grano Spa (2014) 2 SCC 433

section 48 does not cover the ground of patent illegality, such ground is limited to Section 34 of act when issue is whether the award should be set aside or not. Public Policy under section 48 is limited to heads laid down under Renusagar case. Further in *ONGC Ltd v. Western Geco International Ltd* [13]in order to made clarity in conflict related to heads laid down in Saw pipes case the court created subhead under ' Fundamental Policy of India' and elaborated it, court held that phrase include three principles 1. Judicial Approach 2. Principles of Natural Justice 3. Principle of Reasonableness.

CHAPTER II: JURISPRUDENCE AROUND PUBLIC POLICY

Arbitration is seen as mechanism by various international firm resolve their dispute as it is based upon party autonomy thus it plays a major role in international scenario. International commercial arbitration has globalizing impact on the law as it bring new transnational legal framework and common characteristics of civilization.[14] The area of debate in international commercial arbitration is scope of public law- each country has its own law, its own public policy . it is possible that arbitral award may violate public policy of other country and inconsonance with the country where the underlying contract is to be performed. Public law is not only concern in arbitral proceedings but also factor to be considered at point of judicial intervention.[15] If the particular arbitral proceeding or award are against the public law than the court has power to refuse the enforcement of same as provided in New York convention and UNCITRAL Model law.[16] Mandatory public law refer to those rules of law that cannot be derogated from by private parties in the exercise of their party autonomy. Donald Donavan has explained that mandatory rules are those that "arise outside the contract, apply regardless of what the parties agree to, and are typically designed to protect public interests that the state will not allow the parties to waive.[17] The exception of Public policy is used by court as potential means to interfere in international arbitration but as the same many court continue to exercise deference towards arbitral awards. It is reflected not only in narrow view of public policy but also in doctrinal development such as Kompetenz – Kompetenze , principal of severability, arbitral tribunal jurisdiction to deal with interim relief. Public policy is a dynamic

[13] ONGC Ltd v Western Geco International Ltd (2014) 9 S.C.C. 263
[14] Christopher S Gibson, Arbitration, Civilization and Public Policy: Seeking Counterpoise between Arbitral Autonomy and the Public Policy Defense in View of Foreign Mandatory Public Law, SCC Online
[15] Texas law review, Indian Arbitration and Public Policy, Vol 89
[16] Kaustav Saha, Public Policy and attitude of Indian court towards enforcement of foreign arbitral award, SCC Online
[17] Supra 16

concept that evolved to meet the changing needs of society. Public policy is an appropriate tool of external constraint on freedom of members of international business community to determine their commercial relationship and to structure their dispute resolution. According to some scholars, if public policy defence is exercised improperly by state it may undermine the fundamental arbitral principles such as party autonomy, finality and integrity of international arbitration system. ILA report recommends that the enforcement court exclude consideration of public policy that may be relevant at place of underlying performance of the contract. Disputes are of various character such as state – state dispute, mixed public – private , private – private and at each level dispute settlement system adopted to provide an international legal framework for adjudicating the parties.[18] In international commercial arbitration, the expansion of arbitral claims to include public policy matter invites public policy consideration into fray. Public policy gives expression to certain fundamental principles of a state and its legal system and public policy within arbitration reflect these principles as the arbitration has had an expansive impact on society. Hence, the public policy in arbitration not only pertinent to interaction between procedure but also interest of large society. Thus public policy in arbitration not only reflects the fundamental concept of dispute resolution but also as an ' interface of exchange' with larger civilization.[19] This exchange interface took place through public policy defence to recognition and enforcement of international arbitration award. There is no definite meaning of civilization in arbitration. Building civilization of arbitration implies seeking high achievement while maintaining cross – cultural encounters as constituent element. The civilization of international arbitration have a unifying global vision and coherent legal system, yet maintain exchange with other external or national legal systems. The public policy defence also serves as an interface for the exchange between arbitral civilization and other external communities, where State interest and sovereignty (reflecting the values of a particular country) are given weight. International arbitration represent significant legal dimension to globalization. Tom Palmer, writing for the Cato Institute, has defined globalization along economic lines as "the diminution or elimination of state-enforced restrictions on exchanges across borders and the increasingly integrated and complex global system of production and exchange that has emerged as a result.". international commercial arbitration is transnational dispute settlement framework that facilitates certain globalizing tendencies by private commercial actors. It enables them to exercise high degree of autonomy

[18] Supra
[19] Ibid.

and waive off the national regulation. Thus public policy defence is useful to put limitation on globalizing actors to the extent that they don't overstep the fundamental policy limits. In England, court enforced an award that was not contrary to public policy of governing law, or at the law of the arbitration even though underlying contract was unlawful in the country of performance. In US, even if the public policy is in conflict with an arbitral award or the court has close relationship to party, US court are reluctant to enforce enforcement of the arbitral award.

CHAPTER III: PUBLIC POLICY IN ARBITRATION WITH RESPECT TO PUBLIC GOODS

Economist Paul Samuelson defined public goods as those goods that are perfectly non rival in consumption and are nonexcludable.[20] Non rival in consumption means that one individual's consumption of a good does not affect another's opportunity to consume the good and nonexcludable mean that individual cannot deny each other the opportunity to consume a good. National defence, public statistics are the examples of core public goods.[21] Non excludability argues poses main challenge for producing public goods because when goods are available to all and is costly to produce some people will be tempted to free ride on the efforts of others. Other people, recognizing the existence of free riders, will decline to contribute because they lack the assurance that enough others will pitch in to make their effort worthwhile.[22] Thus public good poses problem to welfare economics to the extent that they induce market failure. Adam Smith argued that government should be tasked with three main roles which are directly related to public good. The first two are to defend against external aggression and to maintain impartial legal and judicial system. The third one is establishment of public institution which benefit society at large.[23]

Several other good resemble public good and are called ' quasi – public' good. Most quasi-public goods are to some extent rivalrous or excludable like road can become clogged with traffic, and water can be rationed. All of these good can be brought broadly under 'public

[20] Public goods , available at https://scholar.harvard.edu/files/stantcheva/files/lecture8.pdf , last seen 22 October 2019
[21] Ibid.
[22] Jonathan Anomaly , Public goods and government action, Politics philosophy and Economics 2015, Vol. 14(2)
109–128
[23] Ibid.

good'.[24] Nearly every government made its policies and restrict its action keeping in mind the public good. Public Policy is the principal of judicial legislation and founded on the current needs of society. It is one the most frequently ground used by the parties to international arbitration to resist enforcement of arbitral award. when the award is outweighed by public interest or when such award shoots over the limitations of public interest, the court refuses to enforce the award. ILA in its report recommended that international public policy of any State includes: (i) fundamental principles, pertaining to justice or morality, that the State wishes to protect even when it is not directly

concerned , (ii) rules designed to serve the essential political, social, or economic interests of the

State, these being known as "lois de police" or "public policy rules , (iii) the duty of the State to respect its obligations towards other States or international organizations (e.g., through international treaties.[25] Public good in economics and public policy in arbitration are linked to each other in a way that both are concerned with the benefit of society at large. In economics, the principal of public policy are "non-rivalrous" and "non-excludable." Non-rivalry means that one person's "use" of a public good does not diminish another's ability to enjoy it. Non-excludability means that it's impossible — or at least deeply impractical — to exclude anyone from the benefits of the good. This implies that in both the situation the main priority of government that everyone should be benefit and that equality should be maintain between the people. Similarly if we take into account the public policy in arbitration, then there also government refuse to enforce the award on the ground that it is against the basic principles of law. No contract is greater than the law of land. So in general the court has no power to interfere in arbitral proceedings but when the award is against the basic principle then the court refuse to enforce it. The basic idea behind this is interest of society at large as can be related with the principles of public good.

CONCLUSION

In India ,arbitration is governed by Indian Arbitration and Conciliation Act 1996. The main purpose of arbitration is minimal intervention by the court and parties autonomy to settle their dispute. There are various ground used by parties to challenge the decision of arbitral tribunal

[24] A politics of Public good, available at https://www.nationalaffairs.com/publications/detail/a-politics-of-publicgoods, last seen 24 October 2019
[25] Supra 16

in the court of law. Public Policy is one the most frequently ground used by the parties to international arbitration to resist enforcement of arbitral award. the Indian courts have shown a great propensity towards interfering with international arbitration . whenever the award passed is against the general public at large then the court refused to enforce the same.