What is patent illegality? A short comment in light of *Aksh Optifibre* and *Mohan Steels*

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Bharat Sanchar Nigam Limited v. Aksh Optifibre Limited

Court: High Court of Delhi | **Case Number:** OMP (Comm.) 131 of 2017 **| Citation:**(2021) 277 DLT 348 (DB) | **Bench:** Jyoti Singh J| **Date**: 04 March 2020

Mohan Steels Limited v. Steel Authority of India (SAIL)

Court: High Court of Delhi | **Case Number:** OMP 488 of 2015 **| Citation:** Not available | **Bench:**Jyoti Singh J | **Date**: 04 March 2020

A. Introductory

On 04 March 2020, Jyoti Singh J of the High Court of Delhi delivered two judgments in cases that were filed under Section 34 ACA to set aside the arbitral awards. These are *Bharat Sanchar Nigam Ltd.* v. *M/s Aksh Optifibre Limited*, OMP Comm. 131/2017 and *Mohan Steels Limited* v. *Steel Authority of India*, OMP 488 of 2015. She upheld the award in *Bharat* and set it aside in *Mohan*.

In BSNL, Singh J upheld the tribunal's findings on fixation of rate and rejected BSNL's arguments that it was arbitrarily fixed without any supporting material. She noted that it was based on common business sense and the proposals submitted by Aksh. She said that BSNL neither gave any proposal nor controvert Aksh's proposals. She found the finding "well-reasoned" and "not only a possible but a plausible view."

Setting aside the award in *Mohan*, Singh J held that the award was patently illegal because: –

(a) Though the interpretation of the contract is purely in the domain of the arbitral tribunal, the arbitrator is a creature of the contract. Therefore, the arbitrator cannot decide contrary to or outside the ambit of the terms of the contract between the parties. Section 28 (3) ACA mandates so, and it has been so held in *Associate Builders Delhi Development Authority* (2015) 3 SCC 49 (citing paragraphs 42.3 and 44).

(b) The tribunal interpreted the escalation clause based purely on the circulars placed on record by SAIL with their written arguments. It was neither pleaded nor annexed to the reply. Consequently, Mohan Steels did not have the opportunity to rebut its applicability. Significantly, the circulars are internal guidelines of SAIL and did not form part of the tender conditions or the contract.

This is a short case comment on the decisions, the content of "patent illegality", and how the test was applied in the cases.[1]

B. The test of patent illegality—how determined generally, and how applied in the two cases

A Section 34-judge always has a delicate task at her hands. *Ssangyong* declared the law on several aspects of Section 34 ACA and attempted to streamline the legal position[2]. But, howsoever coherent, because of the

[1] I acknowledge the research assistance of Madhawi Agrawal, a fifth-year student at Amity Law School, Delhi for her research assistance.

[2] A reader interested in the law declared by *Ssangyong* may also refer profitably to two recent decisions of the Bombay High Court in *Union of India* v. *Recon*, decided on 13 February 2020 and *Mann Housing Development and others* v. *Paarijat Co-Operative Housing Society Limited*, MANU/MH/0408/2020. GS Patel J considers "at some length the position in law under amended Section 34."

nature of the decision-making process, there is always room for discretion and a different interpretation. The ground of "patent illegality" underlines the point.[3]

Tracing the precedent and the developments, *Ssangyong* declared the content of patent illegality ground as follows: –

(a) There must be patent illegality appearing on the face of the award;

(b) Illegality which goes to the root of the matter;

(c) It does not mean the mere erroneous application of the law or contravention of substantive law or statute of India);

(d) Reappreciation of evidence, which is what an appellate court is permitted to do, is not allowed;

(e) A contravention of the ACA would be patent illegality;

(f) Construction of the terms of a contract is primarily for an arbitrator to decide unless the arbitrator construes the contract in a manner that no fair-minded or reasonable person would. In other words, where the arbitrator's view is not even a possible view to take;

(g) If the arbitrator wanders outside the contract and deals with matters not allotted to him;

(h) A perverse decision, as understood in paragraphs 31 and 32 of *Associate Builders* (2015) 3 SCC 49. A finding of the award is perverse if:

1) It is based on no evidence at all;

2) It considers something irrelevant to the decision;

3) Ignores vital evidence;

4) So outrageously defies logic as to suffer from the vice of irrationality;

(j) But a finding is not perverse if:

1) There is some evidence on record that is acceptable and could be relied upon, howsoever compendious it may be.

2) Additionally, a finding is based on documents taken behind the parties' back because it would be a decision based on no evidence (led by the parties).

But how does one say that illegality is a patent and when not so? How does the judge decide if the illegality strikes at the root? Similarly, is there, or can there be a uniform test to apply the perversity principle? A reader might recall that while reviewing the award in *MMTC Limited* v. *Anglo American Metallurgical Coal Pty. Ltd.*, the single-judge of the High Court of Delhi completely agreed with the tribunal's interpretation of the contract and roundly upheld it. But considering the same facts and reasoning, the division bench considered the tribunal's interpretation downright perverse.

Neither the concept of patent illegality as a ground to set aside (or refusing to recognise it) is new nor the principles that give this ground its content. But the situations in which the ground will be tested will be far too vast to admit of a clear and absolute rule. So, the cases will have to be decided as they come. This is what a 7-judge bench of the Supreme Court said in *Hari Vishnu* v. *Ahmad Ishaque*, AIR 1955 SC 233, which was

[3]Section 34 (2A) ACAnow provides that "an arbitral award arising out of arbitrations other than international commercial arbitrations, may also be set aside by the Court, if the Court finds that the award is vitiated by patent illegality appearing on the face of the award." The proviso explains that an award shall not be set aside merely on the ground of an erroneous application of the law or by reappreciation of the evidence.

an application for a writ of certiorari on the ground that there was an error apparent on the face of the record[4].

It was observed that an error apparent on the face of the record could not be described precisely or exhaustively. On the contrary, there is an element of indefiniteness inherent in its very nature, and it must be left to be determined judicially on the facts of each case.

This is what a 4-judge bench of the Supreme Court said in *KM Shanmugam* v. *SRVS (P) Ltd.*, (1964) 1 SCR 809 in the context of an analysis of the error apparent on the face of the record.

It was argued in that case that no error could be said to be apparent on the face of the record if it was not self-evident and if it required an examination or argument to establish it. This is the test which Das Gupta J had also formulated in *Satyanarayan* v. *Mallikarjun*, AIR 1960 SC 137 ("An error which has to be established by a long-drawn process of reasoning on points where there may conceivably be two opinions can hardly be said to be an error apparent on the face of the record").

However, speaking for the court, Subba Rao J said in *KM Shanmugam* that the "test might afford a satisfactory basis for decision in the majority of cases. But there must be cases in which even this test might break down, because judicial opinions also differ, and an error that might be considered by one Judge as self-evident might not be so considered by another". He also said that the test of the complex nature of the arguments as a test of an apparent error of law may also break for what is complex to one judicial mind may be clear and obvious to another.[5]

Clearly, Subba Rao J was right when he said further that the concept of error apparent on the face of the record cannot be posted on *a priori* reasoning and must, as has always been done, be decided on a case to case basis.

What the court must, however, bear in mind is that the ground of patent illegality, though invoked profusely, must be applied very rarely. Its content is filled with superlatives ("patent", "outrageous", "irrational", "vital"). The Supreme Court has been at pains to emphasise that their application requires an out of the ordinary situation.

BSNL's case was clearly not so. Once the authority of the arbitrator to fix the rate was agreed, and once it was seen that there was some basis for the arbitrator's decision, his decision had to be upheld.

Ssangyong's holding and reasoning directly covered *Mohan Steels*, and Jyoti Singh J rightly set the award aside. *Ssangyong* had strikingly similar material facts. A circular issued unilaterally by one party was relied on in the majority-award of the tribunal without allowing the other party a chance to comment on its applicability or interpretation.

The court held that it is clear that the majority award needs to be set aside under Section 34 (2) (a) (iii) because the appellant "was unable to present its case".

The court held it violated the most basic notions of justice (that is, public policy of India under Section 34 (2) (b) (ii), Explanation (iii). But the court was quick to repeat that "this ground is available only in very exceptional circumstances, such as the fact situation in the present case. Under no circumstance can any Court interfere with an arbitral award on the ground that justice has not been done in the opinion of the court. That would be an entry into the merits of the dispute …".

It does not appear that these two grounds were argued in *Mohan Steels*. Anyway, *Mohan Steels* holding should be read to say that a contractual term cannot be picked from outside and then interpreted with other terms.

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[4]MC Mahajan, CJ, B.K. Mukherjea, Sudhi Ranjan Das, Vivian Bose, NH Bhagwati, B Jagannadhadas and **TL Venkatarama Aiyyar**, JJ.

[5]Subba Rao J in fact heavily borrowed his language as well as the argument from the 7-judge bench decision in *Hari Vishnu*.