

Award patently illegal because it contravened Section 28 (3) ACA: Supreme Court of India

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State of Chhattisgarh and another v. Sal Udyog Private Ltd.

Court: Supreme Court of India | **Case Number:** Civil Appeal No. 4353 of 2010 | **Citation:** 2021 SCC OnLine SC 1027 | **Bench:** NV Ramana, CJ ; Surya Kant and **Hima Kohli**, JJ | **Date:** 8 November 2021

The Supreme Court has applied the patent illegality ground to set aside a portion of the award on the reason that the illegality in question went to the “root” of the matter. Because it was taken in the appeal and is available to the court on its own, the court also rejected an objection that the ground was not raised in the set-aside application, hence waived.

A. Background

The matter concerned a contract where the State had to supply Sal seeds to the respondent. Under Clause 6 (b), the price payable by the respondent to the State included:

- a. royalty at a specified rate, and
- b. All expenses incurred by the Government each year till the delivery of the Sal seeds to the purchases, which would include the cost of collection and/or the purchase price paid to the growers, as well as handling supervision charges, commission to agent, cost of storage, transportation.

Faced with a loss of revenue, the State government enacted a legislation to annul all agreements relating to forest produce. Thus, the agreement with the respondent was also terminated.

Some of the facts are not stated clearly. It appears that because the respondent had already made some advance payments, it invoked arbitration claiming a refund of INR 1.72 crores approximately. It also seems that the claim included a prayer for a refund of the supervision charges paid by the respondent over the years. The State refuted this claim on the basis that: (i) Clause 6 (b) of the contract clearly stated that supervision charges were to be borne by the respondent; (ii) further, even as per a circular of the State dated 27 July 1987, the application of which was not disputed, a *de minimus* 10 per cent supervision charges (*paryavekshan vyaya*) were to be paid by the buyers of Sal seed (for expenses like the salary, telephone expenses etc., of the department personnel supervising the supply).

Rejecting the State’s objection, the tribunal disallowed the deduction of supervision charges of 1.49 crore. The claim of the respondent was allowed. A sum of INR 7.43 crores approx. which included interest of 18 percent per annum till the date of award was awarded in favour of the respondent, along with future interest at that rate.

The portion of the award extracted in the Supreme Court’s judgment is wholly confusing and it is not clear if the court had before it a copy of the correctly typed/translated award. The court also has made no comment on that aspect. However, it appears that the tribunal’s reason for disallowing supervision charges when calculating the price (thus, granting refund of the supervision charges) was that the tasks performed as ‘supervision’ were already covered under other expenses. For this reasoning, the tribunal also relied on a notification of the state government (different than the circular above noted, and guidelines of a trade association). It said that supervision charges could not yet again be levied as an indirect expense.

The set-aside court reduced the interest to 9 per cent per annum. The appellate court rejected the State's appeal.

B. The Supreme Court's decision

The Supreme Court had granted the leave to appeal limited to the question of supervision charges.

Hima Kohli J authored the judgment for the 3-judge bench. She noted that the existence of Clause 6(b) was not disputed. Nor was the applicability of the State's circular imposing 10 per cent supervision charges questioned.

Thus, the State's objection had been turned down by the arbitrator by giving a "complete go by to the terms and conditions of the Agreement governing the parties" and also ignoring the circular. This, as per the court, was a patent illegality manifest on the face of the award.

One other factor that weighed, in conclusion, was that the respondent had never objected to paying the charges until the termination.

In the court's view, "failure on the part of the learned Sole Arbitrator to decide in accordance with the terms of the contract governing the parties, would certainly attract the "patent illegality ground", as the said oversight amounts to gross contravention of [Section 28\(3\)](#) of the 1996 Act, that enjoins the Arbitral Tribunal to take into account the terms of the contract while making an Award."

Hima Kohli J also said that patent illegality "is not only apparent on the face of the Award, it goes to the very root of the matter and deserves interference."

Further, the respondent had argued before the court that the objection regarding 'supervision charges' had not been taken in the [Section 34](#) petition and, thus, was waived. The court rejected this argument by saying: (i) the ground was taken in the [Section 37](#) appeal; (ii) Moreover, given the expression "the court finds that" in [Section 34\(2A\) ACA](#), the patent illegality ground was available to the court on its own.

Categories: [Application for Setting Aside Arbitral Award](#) | [Patent Illegality](#) | [Pleading Requirement Under Section 34 ACA](#) | [Public Policy](#) | [Section 34 ACA](#) | [Section 37 ACA](#) | [Standard for Setting Aside Arbitral Award](#) | [Waiver](#)