Kluwer Arbitration Blog

Can two Indian parties choose a foreign seat for arbitration?

Kartikey M. · Thursday, January 21st, 2016

The Indian Arbitration and Conciliation Act, 1996 ("**Act**") makes it clear that an arbitration between an Indian and a foreign party can be governed by foreign law and can have a foreign seat. This is defined as 'international commercial arbitration' under the Act. However, whether two Indian parties can agree to a foreign seat for arbitration is not expressly addressed by the Act. Recent judicial pronouncements of the Indian courts have made the position murkier.

On 12 June 2015, the Bombay High Court in *Addhar Mercantile Private Limited v. Shree Jagdamba Agrico Exports Pvt Ltd.* (Arbitration Application 197/2014, "**Addhar**"), and the Madhya Pradesh High Court in *Sasan Power Limited v. North American Coal Corporation India Pvt. Ltd.* (First Appeal No. 310/2015, "**Sasan**") arrived at contradictory findings on this question.

This post highlights how *Addhar* arrived at an incorrect conclusion by holding that two Indian parties cannot choose a foreign seat. The post concludes by highlighting that in the absence of a conclusive judgment on this point by the Supreme Court of India ("**SCI**"), the strength of precedents in India including *Sasan,* point towards allowing two Indian parties to choose a foreign seat.

A. Judgment of the Bombay High Court in Addhar

The Indian parties had entered into an agreement wherein the arbitration clause read: "*Arbitration in India or Singapore and English law to be (sic) apply*." A dispute arose ultimately reaching the Bombay High Court. The Bombay High Court held that two Indian parties cannot be allowed to derogate from Indian law as that would be against public policy and thus the arbitration has to be conducted in India. Although, the court did not explicitly find that two Indian parties couldn't opt for a foreign-seated arbitration, the judgment can be wrongly interpreted to imply just that.

B. Why Addhar got it wrong?

1. ***Improper Reliance on TDM Infrastructure***

While arriving at its conclusion, the court in *Addhar* relied on the observations of the SCI in *TDM Infrastructure Pvt Ltd v. UE Development India Ltd* (2008) 14 SCC 271, "***TDM Infrastructure")*** which held – *"the intention of the legislature would be clear that Indian nationals should not be permitted to derogate from Indian law. This is part of the public policy of the country.* (para 8)*"* However, it is noted that such blind reliance on the observations in *TDM Infrastructure* is misplaced.

India follows the doctrine of precedents i.e. a judgment of the court has to be read in the context of questions, which arose for determination before it. The questions which arose and were conclusively determined by the SCI are part of the *ratio decidendi* of the court and binding on all other courts in India. The observations in *TDM Infrastructure* were made with respect to an application under section 11 of the Act concerning the appointment of an arbitrator. The case never concerned the question of whether two Indian parties can contract out of Indian law or in other words can adopt a foreign law to govern their contract. Thus, the observations in *TDM Infrastructure* were merely *obiter dicta* and hence non-binding on the Bombay High Court in *Addhar*.

2. ***Section 28 of the Act***

Usually in an arbitration agreement, three types of laws are applicable at a given point of time. These are the 1) the law governing the substantive contract, 2) the law governing the arbitration agreement, and 3) the curial law governing the arbitration proceedings. This position holds true in the Indian context as well (*Sumitomo Heavy Industries Ltd.* v. *ONGC Ltd. & Ors.*, (1998) 1 SCC 305).

TDM Infrastructure relied on section 28 of the Act in concluding that Indian parties are not entitled to derogate from Indian substantive law and *Addhar* relied on the same provision. In both *Addhar* and *TDM Infrastructure*, the court deemed the '*substantive law of contract*' must be Indian law, which cannot be derogated from by the Indian parties in an Indian-seated arbitration. If Indian parties choose a foreign governing law for their contracts that will be a violation of public policy and hence such contracts are void under section 23 of the Indian Contract Act, 1872 ("**Contract Act**").

However, these judgments do not make any explicit observations with respect to choosing a foreign seat of arbitration (thereby making applicable a foreign curial law) or a foreign law governing the arbitration agreement. Arguably, the Indian parties are not restricted by the *TDM Infrastructure* and *Addhar* judgments from choosing a foreign seat of arbitration. Such an interpretation appears to be consistent with the interpretation accorded to the scope of section 28(1)(a) of the Act by the SCI in *Bharat Aluminium Co v. Kaiser Aluminium Technical Services Inc* ((2012) 9 SCC 552 at para 118, "**Balco**").

Balco clearly explained that the applicability of section 28 of the Act is restricted to the substantive law of the contract (and has nothing to do with choosing a foreign seat (curial law) or a foreign law governing the arbitration agreement). This shows that two Indian parties are free to choose a foreign seat and / or a foreign governing law for the arbitration agreement. The only limitation that applies is that the substantive law of contract has to be Indian as per section 28 of the Act.

C. Sasan – Setting the right precedent

In *Sasan*, the Madhya Pradesh High Court reached an opposite conclusion from that of *Addhar*, by holding that the Indian parties are free to choose a foreign seat (in this case being London). While arriving at its decision, the Madhya Pradesh High Court concluded that the above observations of *TDM Infrastructure* were non-binding as they were only for the purpose of determining the jurisdiction under section 11 of the Act (as discussed above). Further, the judgment in *Sasan* considered the case of *Atlas Exports Industries* v. *Kotak & Company*, ((1997) 7 SCC 61, "**Atlas***")*, which was a larger bench decision than *TDM Infrastructure* and thus a more binding precedent

than the latter (judgments of larger benches of SCI are binding on smaller benches). In *Atlas*, the SCI considered the applicability of sections 23 and 28 of the Contract Act and held that merely because the arbitration is situated in a foreign country would not by itself be enough to nullify the arbitration agreement that the parties entered into on their own volition.

D. What did Sasan miss?

Although**,** *Sasan* has rightly held that two Indian parties are allowed to choose a foreign seat, it is worth mentioning that the same position was indirectly adopted in another SCI case that was decided before *Addhar* and *Sasan*. This is the case of *Reliance Industries Limited v Union of India* ((2014) 7 SCC 603, "***Reliance Industries***") wherein the SCI dismissed a challenge to the arbitral award arising from a foreign-seated arbitration between two Indian parties.

Though, the SCI did not explicitly decide upon the ability of two Indian parties to have a foreign-seated arbitration, it implicitly recognized the autonomy of the Indian parties to agree on a foreign seat. Additionally, it has been discussed on this blog previously by the author (here), that due to the combined effect of *Balco* and *Reliance*, choosing a foreign seat makes Part I inapplicable. This in turn makes section 28 of the Act inapplicable making the observations of *TDM Infrastructure* nugatory.

Conclusion

Although the issue of whether two Indian parties are permitted to choose a foreign seat in their arbitration agreements may not have been resolved definitively by the SCI, presently a case can be made out for allowing such a foreign-seated arbitration on the basis of reading *Sasan*, *Atlas*, *Balco* and *Reliance* decisions. This is in line with other jurisdictions like England and Singapore which allow parties to choose a foreign seat. In England, for example, section 3(a) of the Arbitration Act, 1996 explicitly recognizes the autonomy of parties to decide their seat. Similarly, Singapore does not place any restriction on the parties ability to choose a seat by adopting Article 20(2) of the Model Law (*PT Garuda Indonesia v Birgen Air* [2002] 1 SLR(R) 401 at [36]).

However, the decisions in *TDM* and *Addhar* mean that there is still an element of uncertainty due to which Indian parties may be hesitant to choose a foreign seat if they intend on enforcing the arbitral award in India, as some courts may follow these decisions in the absence of a clear judgment by SCI. The Indian parties who envisage enforcing their awards outside India may still feel confident in choosing foreign-seated arbitration, as any challenge on public policy grounds is less likely to be sustainable.

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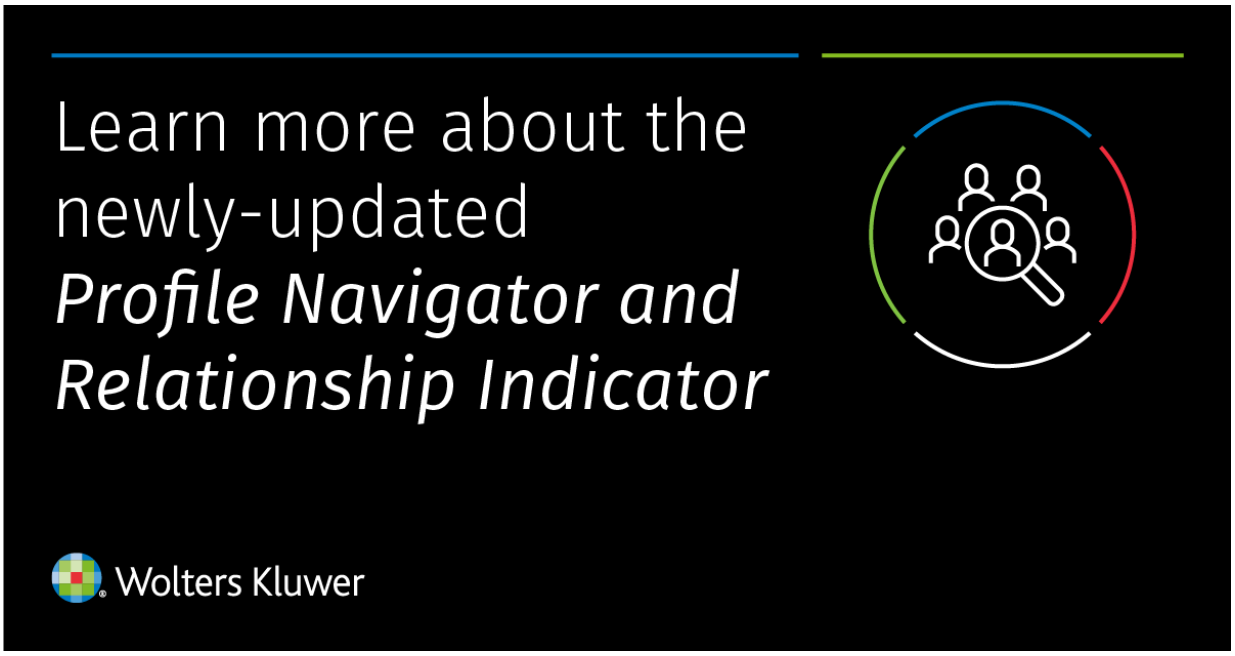

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