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Arbitrability Of Fraud In India – Anomaly That Is Ayyasamy

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The decision of the Indian Supreme Court in *A. Ayyasamy v. A. Paramasivam* ('Ayyasamy') [(2016) 10 SCC 386] has been previously discussed on this blog here, and here. This post seeks to analyse the distinction between arbitrability of fraud concerning India-seated arbitrations and foreign-seated arbitrations created as a result of this judgment.

The court in *World Sport Group Ltd. v. MSM Satellite* ('World Sport') [(2014) 11 SCC 639] had concluded that disputes involving fraud are arbitrable (without making a differentiation between mere allegations of fraud and serious allegations of fraud as made in Ayyasamy), so far as foreign-seated arbitrations are concerned. However Ayyasamy declares that serious allegations of fraud are inarbitrable in India-seated arbitrations, thus creating an artificial difference concerning arbitrability of fraud between foreign-seated and India-seated arbitrations. While all disputes involving fraud are arbitrable for foreign-seated arbitrations, serious allegations of fraud are inarbitrable for domestic arbitrations. There appears to be no legal basis for this differentiation.

Indian case law, as well as jurisprudence in other countries have indeed differentiated between domestic and international public policy, the latter often construed more narrowly than the former for considerations of international trade and commerce. However courts haven't used public policy as the reason for having different standards for arbitrability of fraud for domestic and international arbitrations, which but would have also required making differentiation between international commercial arbitrations seated in India, and pure domestic arbitrations seated in India.

The reasoning of courts rather, is rooted in the competence of the arbitral tribunal; though there exists no evidence to the effect that tribunals appointed in foreign-seated arbitrations are more competent than those appointed for arbitrations seated in India, nor do these form two separate groups – the same arbitrator can be appointed for both foreign and India seated arbitrations. The argument that it is more legitimate to interfere in domestic awards than in foreign awards might be plausible, but has not been fleshed out by the court either.

- §8 and 45 provide for the powers of the Indian courts to refer disputes to arbitration, when there exists an arbitration agreement concerning the dispute prescribing for India-seated and foreign-seated arbitrations respectively. The difference in the language of §§8 and 45 of the Indian Arbitration and Conciliation Act, 1996, where the latter allows for more interference than the former, can be argued as a source of this differentiation similar to the rationale in the case of *Swiss Timing Ltd. v. Organising Committee* [(2014) 6 SCC 677, ¶28]. However there is a difference between the issues of court interference in the determination of arbitrability and

> determination of whether a particular dispute is arbitrable. The former is a procedural enquiry, while the latter is substantive. The difference in the language of the aforementioned sections can at best be a source of the procedural enquiry, i.e. for the argument that courts can decide arbitrability of the dispute before making a reference under §45, as against under §8; but not for the substantive enquiry. Though the difference in the substantive enquiry resulting from the difference in the languages of §§ 8 and 45 has been undertaken in previous cases as well. [*See*, Shin-Etsu Chemicals Co. v. Aksh Optifibre Ltd., (2005) 7 SCC 234; Kalpana Kothari v. Sudha Yadav, (2002) 1 SCC 203; Chloro Controls India (P) Ltd. v. Severn Trent Water Purification Inc., (2013) 1 SCC 641; India Household & Healthcare Ltd. v. LG Household & Healthcare Ltd., (2010) 1 SCC 72; Sundaram Brake Linings v. Kotak Mahindra Ltd., (2010) 4 Comp. L.J. 345 (Mad).]

If anything, the difference in language demanded explanation from the bench in World Sport, when it expanded the ambit of arbitrability under §45 in comparison with §8. This is because even assuming that the difference in language can be a source of the substantive enquiry as well, language of §45 is more permissible than that of §8 (allowing for greater interference in foreign-seated arbitrations), leading to a reverse conclusion from the present position of law.

Chandrachud J. in his concurring opinion in Ayyasamy indeed misses the opportunity to notice this flaw. In the course of his opinion, he draws attention to the difference in the language of §8 of the Act, and the corresponding provision in the UNCITRAL Model Law, the latter also allowing the courts to decline reference to arbitration when the AA is "null and void, inoperative and incapable of being performed". This leads the court to conclude that §8, as against the provision in UNCITRAL Model Law, is mandatory in nature (though the conclusion reached by the court in Ayyasamy does not seem to be in accordance with this peremptory language). §45 mirrors the language of UNCITRAL Model Law, yet ironically, the court concludes that the ambit of arbitrability while making a reference under §8 is narrower than §45 (while the court does not state so explicitly, though the legal position after the pronouncement of Ayyasamy is exactly this).

At another level, it is suspect if Indian law should at all govern the question of arbitrability in all foreign arbitrations, unless Indian courts also have exclusive natural jurisdiction over the dispute. If such jurisdiction does not exist, the issue should be decided in accordance with the law of the seat or the law of the place of enforcement. Hence, application of Indian law to the question of arbitrability in foreign-seated arbitrations is in itself problematic. Indian courts, as against elsewhere in the world, have applied the substantive law of contract to the question of arbitrability (*Reliance Industries Ltd. v. Union of India*, 2014 SCC Online SC 411, ¶76: Note that this judgment was passed after World Sport). Yet, in the context of arbitrability of fraud, without making the analysis of the applicable law, courts have used Indian law for making the determination. For instance in World Sport, the substantive law of contract was that of England and Wales, where fraud, irrespective of its seriousness, is arbitrable (*Fili Shipping v. Premium Nafta Products*, [2007] UKHL 40), yet this did not find traction in the judgment of the court.

Lastly, the position as it stands right now goes against the precedent in *National Insurance Co. Ltd. v Boghara Polyfab Pvt. Ltd.* [(2009) 1 SCC 267], which had explicitly denied the court the power to rule upon the question of arbitrability at the stage of reference, ruling this to be the mandate of the arbitral tribunal under §16 of the Act. [*See also*, Meguin GmBH v. Nandan Petrochem Ltd. (2007) 5 RAJ 239 (SC) (appointed arbitrator in accordance with §11, despite involvement of issues of fraud in the dispute); SBP & Co. v. Patel Engineering Ltd., (2005) 8 SCC 618; Arasmeta Captive Power Co. (P) Ltd. v. Lafarge India (P) Ltd., (2013) 15 SCC 414].

Incidentally, §7 as well was sought to be amended by the 246th Report, making it clear that the subject matter of the arbitration had to be capable of settlement by arbitration for it to be a valid AA, however this suggestion was not introduced in the final amendment act.

As suggested previously, the language of neither §45, nor §§8 and 11, warrant the court to answer the question of arbitrability. Indeed both Swiss Timing and World Sport are decisions based on this reasoning, rather than arbitrability of fraud. Ayyasamy on the other hand, licenses the court to determine the question of arbitrability and analyse the merits of the dispute to the extent required in determining whether allegations of serious fraud are involved. The tribunal might in fact feel obligated by such determination by the court, even when it might think otherwise.

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