# Bhatia, BALCO and Beyond: One Step Forward, Two Steps Back?

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*The article charts the development of international commercial arbitration in India in light of the recent judgment of the Supreme Court in the BALCO case. It starts by outlining the relevant parts of the Indian Arbitration and Conciliation Act 1996 and relevant principles. It proceeds to explore the seminal decision in Bhatia and its after-effects. Next, the article critically examines the decision in BALCO, and reaches a conclusion as to whether or not this decision makes India more 'international arbitration friendly'.*



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## I. Introduction

Part I of the Indian Arbitration and Conciliation Act, 1996 (hereinafter "the Act") applies *"where the place of arbitration is in India."*[1] The meaning of this provision was in dispute in the case of *Bhatia*.[2] In its interventionist decision, the Supreme Court of India held that Part I of the Act could be applied to arbitration disputes with foreign seats *"unless the parties by agreement express or implied exclude all or any of its provisions."*[3]

On 10 January 2012, a five judge Constitutional Bench of the Supreme Court had the opportunity to reconsider[4] its earlier controversial ruling in *Bhatia*. On 6 September 2012, the Constitutional Bench issued a judgment in which it restricted the scope of interference by Indian courts in arbitrations conducted outside the territorial boundaries of India by excluding applicability of Part I of the Act to such arbitrations.

## The Indian Arbitration and Conciliation Act 1996

The Act has four distinct parts. For the purpose of this article, only Parts I and II are relevant.

Part I applies where the place of arbitration is in India; any award passed under this part is considered to be a domestic award. §2(2) of Part I of the Act sets out *"this Part shall apply where the place of arbitration is in India"*.[5]

Part II is concerned with the recognition and enforcement in India of foreign awards that fall within the scope of the 1958 New York Convention and the 1927 Geneva Convention.

## Core Principles

It is necessary to start by setting out some core principles of international commercial arbitration. These principles and their scope have been at the centre of the cases that this article explores.

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1 §2(2), The Indian Arbitration and Conciliation Act, 1996.

2 Bhatia International v Bulk Trading [2002] 4 SCC 105 [Supreme Court of India].

3 Bhatia International v Bulk Trading [2002] 4 SCC 105 [Supreme Court of India].

4 Civil Appeal 7019/2005 [Hereinafter, "*BALCO*"].

5 §2(2) Indian Arbitration and Conciliation Act 1996.

**a)** ***Lex arbitri***: The law governing the existence, powers and duties of the arbitral tribunal, and the proceedings. Various terms have been used to describe the expression *lex arbitri*, including 'curial law' and 'procedural law'. However, descriptions such as these may cause more confusion than clarification, because they are not sufficiently precise. The procedure of an arbitration may be regulated by the laws chosen by the parties; but the procedural law is that of the place of arbitration.[6]

**b)** **Substantive law**: The law governing the substantive issues in dispute. This is also described as[7] the 'applicable law', 'governing law' and 'proper law of the contract'.

**c)** **Law governing the arbitration agreement**: In the last century it was often considered that the arbitration agreement would also be governed by the substantive law chosen by the parties. However, it has always been possible for the parties to choose another law to govern the arbitration agreement. In the 21st century, it has been increasingly fashionable within the international arbitration community for the arbitration agreement, which is acknowledged to be autonomous, to be subjected to a distinct set of rules for the purpose of choosing the law that should govern it.

**d)** **Law of the 'Seat'** (usually described as *lex arbitri*): The juridical seat of the arbitration designated by the parties, or by an arbitral institution or, in limited circumstances,[8] the arbitrators themselves.[9] The seat must be distinguished from the physical venue of the hearings. The physical venue rarely[10] has any practical effect on the conduct or outcome of the arbitration. However, in theory, an arbitration 'governed' by the law of its 'seat', which is usually (but not always) the law of the jurisdiction in which its hearings (and other significant events such as 'making' the award) take place.

**e)** **Party autonomy**: This is the guiding principle in determining the procedure to be followed in an international arbitration. It is generally accepted, and

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6 Nigel Blackaby, Constantine Partasides, Alan Redfern & Martin Hunter, Redfern and Hunter on International Arbitration 3.50 (5th edn, 2009).

7 *Ibid* at [3.07].

8 Art. 18, *UNCITRAL Arbitration Rules* (as revised in 2010).

9 §3, The (English) Arbitration Act 1996.

10 For example, if the purpose of the visit is to take evidence from witnesses, the arbitral tribunal should respect any provisions of the local law that govern the taking of evidence like not permitting arbitrators to take evidence from witnesses on oath.

the Model Law states that *"Subject to the provisions of this Law, the parties are free to agree on the procedure to be followed by the arbitral tribunal in conducting the proceedings."*[11]

## I. Bhatia International

In the earlier years of the 21st century, a three judge bench of the Indian Supreme Court[12] considered whether it could accede to a request for interim measures to an Indian court in ICC arbitration with its seat in Paris. One of the respondents had sought interim relief from the court under Part I of the Act. The appellant objected that the court had no jurisdiction because Part I did not apply to arbitrations in which the seat of arbitration is outside India. The issue eventually reached the Supreme Court.

The bench held that *"the provisions of Part I of the Act would also apply to international commercial arbitrations seated outside India, unless the parties had expressly or impliedly agreed to exclude its application."* The rationale was as follows:

- The Act is based on the Model Law. The provision[13] analogous to §2(2) of the Act contains the word *'only'*. It was held that the omission of 'only' from §2(2) of the Act was evidence of intent of the Indian legislature to permit Part I of the Act to apply to arbitrations that take place outside India.

- §2(2) of the Act provides that Part I will apply where the place of arbitration is in India. §2(4) of the Act provides that Part I *'shall apply to every arbitration'*. §2(5) states that it *"shall apply to all arbitrations and to all proceedings relating thereto."* Therefore, it was held that the finding that Part I applies to all arbitration resolves any apparent inconsistency between these provisions.

- The court held that parties to an arbitration to which Part II applies would find themselves without any 'interim relief'[14] remedy in India if Part I was not made applicable to arbitrations held outside India.

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11 Art. 19(1), The Model Law.

12 Bhatia International v. Bulk Trading [2002] 4 SCC 105 [Supreme Court of India].

13 Art. 1 (2) UNCITRAL Model Law 1985.

14 §9: *"A party may, before, or during arbitral proceedings or at any time after the making of the arbitral award but before it is enforced...apply to a court for an interim measure of protection..."*.

## II. Chaos Post-Bhatia

As a consequence of the *Bhatia* decision, in *Venture Global,*[15] the courts intervened in a foreign seated arbitration. The case dealt with an LCIA arbitration award, with its seat in England. The Supreme Court held that Part I of the Act applied to such an award, and hence the courts in India would have jurisdiction to set aside the award. Next, in *Indtel,*[16] the courts adopted the power to appoint arbitrators in arbitrations seated outside India pursuant to §11 of the Act.

In an attempt to restore party autonomy, the courts sought to restrict the application of Part I of the Act to arbitrations seated outside India. The courts demonstrated a willingness to infer implied exclusions of Part I where parties had chosen a foreign seat and a foreign law to govern the arbitration. In *Videocon Industries,*[17] the courts held that, since the parties had agreed to an arbitration clause governed by English law, even though the main contract was governed by Indian law, they had impliedly excluded Part I of the Act. In *Yograj,*[18] the Court ruled that the nomination of a non-Indian seat of arbitration could also be sufficient to amount to an exclusion of the Indian courts' supervisory jurisdiction over the arbitration.

The international arbitration community took notice of the chaotic situation in India, because it appeared to blur India's stance on the principle of party autonomy. The only way around it seemed to be for parties to renegotiate existing arbitration agreements, expressly excluding the application of Part I of the Act.

## III. Bharat Aluminium Co ('BALCO')

In *BALCO,*[19] a two-judge Supreme Court expressed reservations about the decision in *Bhatia* and referred the matter to a three-judge Supreme Court that included the Chief Justice of India. The three-judge Supreme Court agreed that *Bhatia* and *Venture Global* should be reconsidered by a five-judge bench. The Court also invited *amici curiae* briefs from leading arbitral institutions operating in India, including LCIA India and the SIAC.

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15 Venture Global Engineering v. Satyam Computers Services [2008] 4 SCC 190 [Supreme Court of India].

16 Indtel Technical Service Pvt Ltd v. WS Atkins Plc [2008] 10 SCC 308 [Supreme Court of India].

17 Videocon Industries Ltd v. Union of India [2011] 6 SCC [Supreme Court of India].

18 Yograj Infrastructure Ltd v. SSang Yong Engineering and Construction Co Ltd [2011] 9 SCC 735 [Supreme Court of India].

19 *BALCO.*

### (a) §2(2) of the Act, applicability of Part I and exclusion of 'only'

The court held that §2(2) of the Act is a provision clarifying the application of the law, not an enabling provision (as held in *Bhatia*). Further, it held that §2(2) was a legislative declaration of the doctrine of territoriality. Therefore, Part I of the Act applies only to arbitrations which had their seats in India.

It held that the absence of the word 'only' did not mean that the Indian legislature intended to make Part I applicable to arbitrations with their seats outside India. The reason for the omission was explained by the 330th Meeting of the drafters of the Model Law on 19 June 1985 - Article 1(2) of the Model Law contained the words '*except articles 8,9,35 and 36*', and therefore had to insert the word 'only' to clarify that these provisions would apply also to domestic arbitrations.[20]

Enforcement of awards rendered in international commercial arbitration held outside India would only be subject to the jurisdiction of the Indian courts when such an award was sought to be enforced in India in accordance with the provisions contained in Part II of the Act.

Further, the court held that §2(2) does not conflict with §2(4) or 2(5) of the Act. §2(5) only means that the Act applies to all arbitrations where it would be otherwise applicable.[21]

### (b) No jurisdiction to grant interim measures

The court held that, "*if held outside India, interim relief cannot be granted by Indian courts under §9 or any other provision of the Act as applicability of Part I of the Act is limited to arbitrations which take place in India.*"[22]

The court rejected the argument that §9 is a standalone provision. Further, the court also rejected the argument that parties would be left without a remedy in such a scenario. The court stated that parties were free to seek appropriate remedies in their chosen jurisdiction. Though the court recognised that this might lead to hardship, it noted that statutory interpretation should not be guided by such factors.

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20 *BALCO* at [63] and [68].

21 *BALCO* at [85].

22 *BALCO* at [199].

On a strict interpretation, this result is consistent. However, the courts should have acted positively and carved out §9 or given the parties an option to opt into it. While interpreting §2(2), the courts referred to foreign legislation for aid. Similarly, in this case, the courts could have referred to several jurisdictions, including England, to conclude that there was legislative intent to allow parties to apply to the courts for interim relief even where an arbitration has its seat outside India.

Alternatively, the court could have undertaken a purposive interpretation. The result of the court's finding is that parties with assets in India can dispose of it while the arbitration is in progress and effectively frustrate its purpose. The lack of interim relief means that, when dealing with parties with assets in India, the parties are practically forced to choose India as their seat and to tolerate the interventionist attitude of the Indian judiciary.

### (c) Seat of Arbitration and the Doctrine of Territoriality

The court held that the country where the seat of arbitration is located and the country whose law is chosen by the parties, do not give concurrent jurisdiction over the proceedings. It held that only the courts of the country where the seat of arbitration is located have jurisdiction to address any matter relating to such arbitration. It is only in the absence of a choice of seat of arbitration that the country whose law is chosen by the parties has jurisdiction to entertain the matter.[23] The Principle of Territoriality is the governing principle of the Act and accordingly, the seat of arbitration determines the jurisdiction of the courts.[24]

### (d) Challenging Foreign Awards in India

It was argued that §48(1)(e) of Part II of the Act, analogous to Art V.1(e) of the New York Convention, indicated that foreign awards could be set aside by courts under the substantive law of which it was rendered. This argument was based on the expression 'under the law of which' contained in the section.

Rejecting this argument, the court held that the courts of the place of arbitration and the law under which the award is made do not have concurrent jurisdiction. Further, the court held that the 'under the law of which' the award is made is an alternative only when the court of the place of arbitration does not have power to set aside an award under its local legislation.

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23 *BALCO* at [137] and [148].

24 *BALCO* at [167].

Moreover, the court clarified that even where the parties are not Indian but the seat of arbitration in India, the award would be classified as a domestic award. This is consistent with the position in most countries.

### (e) Prospective Application

In an attempt to do 'complete justice',[25] the court held that the judgment will apply prospectively to arbitration agreements made after 6 September , 2012.

Though this may appear practical, the court could have narrowed the application of the judgment. Instead of making it prospectively applicable, the courts could have made it applicable to all arbitration agreements that are either: (a) existing but not subject to a dispute before any Indian court or (b) existing and subject to dispute before an Indian court but no final judgment has been delivered.

This finding dilutes the positive impact of the judgment, in that, it means parties will need to re-negotiate their arbitration agreements to bring them within the ambit of the judgment. Unless this is done, the *Bhatia* principles can potentially apply to those arbitration agreements.

## IV. Comment

The *BALCO* judgment is likely to be well received since Part I of the Act contains several provisions that (under previous interpretation) allowed judicial interference by Indian courts in arbitration proceedings, thereby prolonging the entire process. Especially, §9 (passing interim orders) and 34 (setting aside an award) of the Act were notorious for being readily invoked by parties attempting to stall arbitration proceedings by invoking the jurisdiction of the Indian courts.

After *Bhatia*, parties were more hesitant in dealing with India owing to the invasive nature of the judiciary. Many parties insisted on terms in agreements to compensate for this legal risk. This made numerous transactions commercially unviable. This judgment is expected to equip foreign investors with renewed confidence. However, the lack of interim relief means that it is still possible for Indian parties to frustrate such arbitrations. Further, the prospective application of the judgment means re-negotiating agreements to exclude the potential application of *Bhatia*. Thus, though overall this judgment is a step in the right direction, it does not offer a complete solution.

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25 Art. 142(1), Constitution of India, 1950.

A lot of the published comment on *BALCO* is focused on the problem of prospective application of the principles it establishes. However, as stated above, parties have it in their hands to deal with this by re-negotiating their arbitration agreements. The more serious problem is the absence of interim relief in arbitrations with their seats outside.

On a separate note, the question remains as to how the Indian courts will now treat an arbitration where the parties have chosen the Indian law as the *lex arbitri*, but located the proceedings in another country. In the *Peruvian Insurance case*,[26] the English Court of Appeal considered a contract that provided for an arbitration to be located in Peru but subject to English procedural law. The Court of Appeal construed the contract as providing for arbitration in London under English law. If the Indian courts were to follow the international arbitration community, then the conclusion would be that the parties chose India as the 'seat' while holding the physical hearings in another country.

## V. Conclusion

The main consequence of this judgment will be to insulate arbitrations seated outside India from unwelcome interference by the Indian courts. The decision takes a step forward in clarifying the mutual exclusivity of Parts I and II of the Act, concluding that Part I of the Act is not applicable to international arbitrations held outside India. However, the judgment leaves such parties without the possibility of obtaining interim relief in India.

India has taken a significant step in the right direction in the international arbitration context. However, the absence of any provision to obtain interim relief under Part II of the Act means that there is still some way to go before India creates an international arbitration regime that is in full accordance with international norms.

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26 Naviera Amazonia Peruana SA v. Compania Internacional de Seguros de Peru, [1988] 1 Lloyd's Rep 116.