

**IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION**

**ARBITRATION PETITION NO.545 OF 2017
ALONGWITH
NOTICE OF MOTION NO.1547 OF 2017**

Fermenta Biotech Limited ... Petitioner
Versus

K.R. Patel ... Respondent

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Mr. Ashish Kamat a/w Mr. Akshay Kolse Patil and Mr. Arun Unnikrishnan
I/b AAT Legal And Co. for the Petitioner.
Mr. Rushabh Sheth a/w Neha Shah I/b M.S. Bodhanwalla & Co. for the
Respondent.

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CORAM : S.C.GUPTE, J.

DATE : 11 OCTOBER 2018

ORDER:

. This arbitration petition challenges an arbitral award on a jurisdictional issue considered by the learned Arbitrator whilst hearing an application under Section 16 of the Arbitration and Conciliation Act, 1996 (“Act”) as also the final adjudication in the reference after repelling the challenge to his jurisdiction under Section 16.

2 The brief facts of the case may be noted as follows :

2.1 The Respondent herein was originally the Managing Director of the Petitioner Company. He, as a major shareholder of two corporate entities

based in Panama, who in turn held about 39.65 per cent share capital in the Petitioner company, entered into two agreements with the Petitioner on 1 February 2002. One was a share purchase agreement on behalf of the Panaman entities as their constituted attorney, transferring their 39.65 per cent shareholding in the Petitioner company to one D. Vasant Kumar, who was the other promoter of the Petitioner. The other was a non-compete agreement, by which the Respondent agreed to cease to be the Petitioner's Managing Director and not to directly or indirectly carry on any business competing with its business. The agreements are hereinafter, respectively, referred to as "share purchase agreement" and "non-compete agreement". The consideration for the share purchase agreement was agreed to be paid to the two Panaman entities in the manner stated in the agreement. In pursuance of the share purchase agreement and in consideration of the Respondent quitting as its managing director and committing to the obligations under the non-compete agreement, the Petitioner agreed to pay to the Respondent a sum of Rs.50 lacs. This amount was to be paid from out of the net profits of the Petitioner. The non-compete agreement stipulated that the term of the agreement would be for five years from the date of commencement as defined thereunder. The agreement also provided that in the event the Petitioner's net profits, during the aforesaid period of five years, were not sufficient/adequate to pay up the entire amount of Rs.50 lacs in one or more installments, the Petitioner's commitment to pay the said amount would survive the said period of five years and extend till such time as the said amount was not fully paid. The agreement defined the term "net profits" to mean "profits available for distribution/appropriation by way of dividend to the shareholders of the company".

2.2 It is the case of the Respondent (who was the original claimant in the arbitration reference) that the Petitioner did not make any net profits within the meaning of that term as used in the non-compete agreement during the original tenure of the agreement, i.e. from the date of its commencement and until five years thereafter. It was the Respondent's case that after he learnt about the profits made by the Petitioner, he, by his letter dated 23 May 2014, called upon the Petitioner to pay the amount of Rs.50 lacs due and payable to him under the non-compete agreement. The Petitioner, in response to the Respondent's letter, denied its liability. As a result, disputes arose between the parties and upon an application made under Section 11 of the Act, were referred to the sole arbitration of the learned Arbitrator herein.

2.3 The Petitioner contested the Respondent's claim in the reference mainly on two grounds. Firstly, it was submitted that the claim was time barred as the Petitioner's liability to pay non-compete fees arose in the year 2007, when it reported profits for the first time during the tenure of the agreement and that the claim made in the year 2014 was beyond time. Secondly, it was submitted that the non-complete agreement was void under the provisions of Section 27 of the Indian Contract Act as it was in restraint of trade and no claim could be made thereunder.

2.4 The learned arbitrator negatived both objections of the Petitioner and passed an award in the sum of Rs.50 lacs with interest from the date of the claim till payment or realization at the rate of 14 per cent per annum. In addition, a sum of Rs.19,25,736/- was awarded as costs. This award has been challenged in the present arbitration petition. As noted above,

the challenge to the jurisdiction of the arbitrator on the ground of bar of limitation was separately argued and decided on an application under Section 16 of the Act filed by the Petitioner herein. Since the learned arbitrator rejected that challenge and proceeded to hear the reference and declare his final award, the jurisdictional aspect is also made a ground of challenge in the present arbitration petition whilst challenging the award.

3 Mr. Ashish Kamat, learned Counsel appearing for the Petitioner, submits that both aspects of the challenge, namely, the bar of limitation and the post-service negative covenant contained in the non-compete agreement, are matters of public policy and in as much as the award is in breach of the law of limitation as well as Section 27 of the Contract Act, which prohibits post-service negative covenants, the award is in conflict with the public policy of India and is liable to be set aside under clause (b) (ii) of Sub-section (2) of Section 34 of the Act. Learned Counsel submits that the award is also vitiated by a patent illegality appearing on the face of the award within the meaning of Sub-section (2A) of Section 34 and deserves to be set aside on that ground also. Learned Counsel relies on several judgments including, in particular, the judgments of the Supreme Court in **Associate Builders Vs. Delhi Development Authority**¹, **HRD Corporation Vs. Gail (India) Limited**², and **Shriram EPC Limited Vs. Rioglass Solar SA**³ in support of his case on contravention of public policy and patent illegality in the award. Learned Counsel also relies on several other judgments of the Supreme Court, particularly the cases of **Niranjan Shankar Golikari Vs. Century Spinning And Manufacturing**

1 (2015) 3 SCC 49

2 (2018) 12 SCC 471

3 2018 SCC OnLine SC 1471

Co. Ltd.⁴ , Gujarat Bottling Co. Ltd Vs. Coca Cola Co.⁵, B.T. Purushothama Rai Vs. K.G. Uthaya⁶, Percept D'Mark (India) (P) Ltd. Vs. Zaheer Khan⁷ and N. Balakrishnan Vs. M. Krishnamurthy⁸ in support of his case that both these statutes, namely, the Limitation Act and Section 27 of the Contract Act, are matters of public policy, to buttress his submissions on contravention of public policy.

4 Mr. Kamat's argument on contravention of public policy goes like this. Learned Counsel submits, firstly, that the bar of limitation as well as the nullity of an agreement which is in restraint of trade, as provided in Section 27 of the Contract Act, are matters of public policy. Learned Counsel next submits that such public policy being a fundamental policy of Indian law, any award which shows contravention of these laws is in conflict of public policy of India within the meaning of clause (b) (ii) of sub-section (2) of Section 34. I am afraid that is a wholly erroneous construction of the ground of challenge concerning conflict with public policy of India, as contemplated under Section 34(2)(b)(ii).

5 Conflict with public policy of India was a concept, which was introduced in the Foreign Awards (Recognition and Enforcement) Act, 1961 as a ground of objection for enforcement of a foreign award in India. Section 7(1)(b)(ii) of that Act provided that a foreign award might not be enforced under the Act, if the court dealing with the award were to be satisfied that its enforcement would be contrary to public policy. The Supreme Court, in its celebrated judgment in the case of **Renusagar Power**

4 (1967) 2 SCR 378

5 (1995) 5 SCC 545

6 (2011) 14 SCC 86

7 (2006) 4 SCC 227

8 (1998) 7 SCC 123

Co. Ltd. Vs. General Electrical Co.⁹, explained the meaning of the term 'public policy' under Section 7(1)(b)(ii) of that Act. Firstly, the court noted that 'public policy' here meant 'public policy of India' and not of the country whose law governed the contract or of the country of the place of arbitration. The court then went on to explain the content of the expression 'public policy' in this context. The court observed that the expression "public policy" in Section 7(1)(b)(ii) had been used in a narrower sense and in order to attract the bar of public policy the enforcement of the award must evoke something more than a mere violation of the law of India. After considering the principles of private international law and Indian and foreign judgments on the subject, the court held that enforcement of a foreign award would be refused on the ground that it was contrary to public policy, if such enforcement would be contrary to (i) fundamental policy of Indian law; or (ii) the interests of India; or (iii) justice or morality. On the date of **Renusagar**, Indian law separately provided for recognition and enforcement of domestic awards and foreign awards, respectively, under Arbitration Act, 1940 and Foreign Awards (Recognition and Enforcement) Act, 1961. When the arbitration law was consolidated by enacting the Arbitration and Conciliation Act 1996 covering both domestic and foreign awards under it on the lines proposed by United Nations Model Law, the Legislature incorporated the principle of public policy in Section 34. The section provides for a ground of challenge to an arbitral award if it was "in conflict with the public policy of India". The expression 'public policy' used by the legislature in Section 34, as it stood prior to its amendment by Amending Act, 2016, was considered by the Supreme Court in the case of **Associate Builders** (supra) along with

9 1994 Supp (1) SCC 644

the expression 'patent illegality' used in Section 34 of the Act. The Supreme Court in **Associate Builders** considered all three aspects of public policy discussed in **Renusagar**. It also considered the construction of 'public policy of India' contained in Section 34(2)(b)(ii) of the Act of 1996 (as it then stood prior to the Amendment of 2016) in **ONGC Ltd Vs. Saw Pipes Ltd**¹⁰. The net result of the law, as noted by the Supreme Court in **ONGC Ltd**, was expressed in the following words: The award could be set aside, if it was contrary to : (a) fundamental policy of Indian law; or (b) the interest of India; or (c) justice or morality, or (d) in addition, if it was patently illegal. Coming to the first head, namely, 'fundamental policy of India', the court noted, after referring to **Renusagar**, that disregarding orders of superior courts in India would be regarded as being contrary to the fundamental policy of Indian Law; to this it could be added that the binding effect of the judgment of a superior court being disregarded would be equally violative of the fundamental policy of Indian law. Fundamental policy of Indian law, as the court noted, is informed by three basic juristic principles of Indian law. The first amongst these is the requirement of a "judicial approach", which demands that a decision must be fair, reasonable and objective. On the obverse side, anything arbitrary or whimsical would obviously not be fair, reasonable or objective. The second was the principle of *audi alteram partem*, which undoubtedly has always been treated as a fundamental juristic principle, also contained in Sections 18 and 34(2)(a)(ii) of the Arbitration and Conciliation Act, 1996. The third juristic principle was infirmity of a perverse or irrational decision such that no reasonable person would have arrived at. The court also noted the settled law on the measure of perversity or irrationality in this

10 (2003) 5 SCC 705

behalf in the following words : where (i) a finding is based on no evidence, or (ii) the arbitral tribunal takes into account something irrelevant to the decision arrived at, or (iii) ignores vital evidence in arriving at its decision, such decision would necessarily be perverse. After taking into account the tests discussed in its earlier judgments, the Supreme Court in **Associate Builders** made it clear that when a court applied the public policy test to an arbitration award, it did not act as a court of appeal and consequently errors of fact could not be corrected. A possible view by the arbitrator on facts has necessarily to pass muster as the arbitrator is the ultimate master of the quantity and quality of evidence whilst delivering his arbitral award. The court thereafter noted the other two aspects of public policy, namely, interest of India, and justice or morality. Coming to patent illegality, the court, after taking into account judicial dicta in its earlier judgments, noted that the principle of “patent illegality” contained three sub-heads : (a) contravention of the substantive law of India, which goes to the root of the matter and which is not of a trivial nature; (b) contravention of the Arbitration Act itself; and (c) contravention of the terms of the contract. This last contravention, the court noted, must be understood with a caveat. The construction of the terms of a contract was primarily for the arbitrator to decide and unless the arbitrator construed the contract in such a way that it could be said to be something that no fair-minded or reasonable person could do, such construction was not open to challenge. Applying these tests, the Supreme Court set aside an order of a Division Bench of Delhi High Court, by which the latter had interfered with an arbitral award, with a view to do 'rough and ready justice'.

6 The grounds of (i) conflict with the public policy of India and (ii)

patent illegality appearing on the face of the award have been further restricted or watered down by the Indian legislature whilst enacting the Arbitration and Conciliation (Amendment) Act, 2015 (Act 3 of 2016), which came into effect from 23 October 2015. An explanation has been added as Explanation 1 to clause (b) of sub-Section (2) of Section 34 of the Act, clarifying for avoidance of any doubt that an award is in conflict with the public policy of India only if (a) in making of the award, the tribunal was induced or affected by fraud or corruption or violated Sections 75 or 81 of the Act or (b) it is in contravention with the fundamental policy of Indian law or (c) it is in conflict with the most basic notions of morality or justice. So also, a separate sub-section has been introduced to deal with the ground of patent illegality, namely, sub-section (2A). Sub-section (2A) provides that an arbitral award in an arbitration other than international commercial arbitration may also be set aside by the Court, if the Court finds that the award is vitiated by a patent illegality appearing on the face of the award. There is a proviso to that sub-section, which requires that an award cannot be set aside merely on the ground of erroneous application of law or by re-appreciation of evidence.

7 The net result of these amendments is that the ground of conflict with public policy of India has been further narrowed down to restrict it to (i) inducement or affectation by fraud or corruption or violation of section 75 or section 81 in making of the award; (ii) contravention of the fundamental policy of India law; and (iii) conflict with the most basic notions of morality or justice. This change has been explained by the Supreme Court in the case of **HRD Corporation** (supra). The Court has noted in that judgment that “public policy” would now include only two of

the three things set out in the case of **Renusagar**, viz. “fundamental policy of Indian Law” and “justice or morality”; the ground relating to “interest of India” no longer obtains. “Fundamental policy of Indian law” is now to be understood as was laid down in **Renusagar**, whilst the concept of “justice or morality” has been tightened and is now to be understood as meaning only the basic notions of justice and morality, i.e. such as would shock the conscience of the court as explained in **Associate Builders** (supra). The court also noted in this behalf the amendment to Section 28(3) under Act 3 of 2016, by which the provision was brought in line with the judgment of the Supreme Court in **Associate Builders**, making it clear that the construction of the terms of the contract was primarily for the arbitrator to decide, and no such construction was open to challenge unless it was found that it was not a possible one.

8 In sum, thus, short of the ground of fraud or corruption or contravention of Sections 75 or 81 of the Arbitration and Conciliation Act 1996, to make out a ground of conflict with public policy of India, the Petitioner has to now make out a case that it is in contravention with the fundamental policy of Indian law, that is to say, it shows infringement of either of the three basic juristic principles referred to above or is against the very basic notions of justice and morality, i.e. such as would shock the conscience of the court, as explained in **Associate Builders** case.

9 So also, for making out a case of patent illegality, it must be shown that the award contravenes (a) the substantive law of India on an aspect which goes to the root of the matter and which is not of a trivial nature or (b) the Arbitration and Conciliation Act, 1996 itself or (c) the contract

between the parties, as explained in **Associate Builders** case. It must further be shown that such illegality appears on the face of the award. The illegality, in other words, must be so self-evident and plain as not to admit of any dichotomy of opinions; it should not be necessary to, firstly, refer to any document or matter which is not made part of the award to assess such illegality and, secondly, it should be obvious and not require any elaborate or intricate explanation. Lastly, it is important to remember that it is not good enough to say that the Arbitrator has wrongly applied the law or has not properly appreciated the evidence. If the arbitrator notes or acts on a correct principle or provision of law, but makes a mistake in applying it to the facts of the case, such error is not amenable to a challenge under Section 34. That is now clarified by the explanation to sub-section (2A) of Section 34 of the Act.

10 As much as a conclusion of fact, even a conclusion of law, where two views are possible, is not open to challenge on the ground of either contravention of fundamental policy or the very basic notions of justice and morality, as understood above, or on the ground of a patent illegality appearing on the face of the award, as explained above, so long as the arbitrator takes one possible view of it. This applies across the board for all conclusions of law. There is no distinction to be made in this behalf between different laws on the basis of their legislative importance – whether they seek to lay down any public policy or simply govern the relationship between individual parties. There is nothing particular about laws of limitation or laws forbidding restraint of trade, for example, which should require the court to treat either their interpretation or application by the arbitrator differently. An award which applies a limitation or

restraint of trade statute incorrectly, for example, cannot be termed as an award in breach of public policy because these laws contain matters of public policy any more than other statutes which may not be laying down strictly matters of public policy.

11 Let us now see if the Petitioner in the present case makes out either of these two grounds. The Petitioner's case on limitation is based on its contention that the Respondent's invocation of the arbitration agreement is after three years of accrual of the right to sue. Learned Counsel for the Petitioner argues that the right to sue accrued in this case at the end of the financial year 2006-07, when the Petitioner had sufficient net profits available for distribution/appropriation towards dividend so as to pay up the entire amount of Rs.50 lacs in one or more installments and that in as much as such invocation was after three years of the end of that financial year, the reference was beyond time. There is no dispute between the parties as to the applicable article of the Limitation Act. Both agree that it should be Article 113. The controversy really is about the date of accrual of the cause of action. The learned arbitrator, having regard to Clauses 4 and 5 of the non-compete agreement, held that the Petitioner had a continuing obligation to pay to the Respondent, since there was no net profit within the original tenure of the non-compete agreement, namely, five years from its commencement, within the meaning of the term 'net profit' as used in the agreement, namely, "profits available for distribution/appropriation by way of dividends to the shareholders of the company". The arbitrator, secondly and in the alternative, held that the relevant clauses of the agreement necessarily implied a duty on the part of the Petitioner to inform the Respondent as and when the former earned

such net profits and the right to sue accrued to the latter only when such information was given to him. The arbitrator accordingly held that the right to sue accrued to the claimant only on 16 July 2014, when he was informed about the net profits and the arbitration reference commenced within three years of such date was within time. For all these reasons, the learned arbitrator held the reference to be within time under the provisions of Article 113 of the schedule to the Limitation Act. The entire exercise involves two aspects, the first being construction of the agreement between the parties and the second being application of the law of limitation to the agreement so construed. Based on the documents before him and the submissions advanced, the learned arbitrator construed the agreement to mean an agreement providing for (a) a continuing duty to pay in the event 'net profits', within the specific meaning of that term, were not made in the original tenure of five years and in the alternative, (b) an implied duty on the part of the Petitioner to inform the Respondent about the factum of making of such profits so as to make accrual of cause of action relatable to such information being conveyed to him. The arbitrator's construction of the agreement in this behalf is not open to challenge simply on the ground either that such construction was wrong or opposed to law or that it was contrary to evidence. It must be further shown to be opposed to fundamental policy of Indian law or basic notions of justice or morality as understood in **Renusagar** and explained in **Associate Builders** or vitiated by a patent illegality in the sense in which the term is understood in Sub-section (2A) of Section 34, as explained above. The appreciation of evidence or application of law by the arbitrator cannot be termed as patent illegality, as explained above, since the so-called contravention of the statute of limitation is, firstly, not a matter of disregarding any particular

provision of law. The arbitrator has correctly used Article 113 of the Limitation Act for deciding the controversy. The question which really fell for his consideration was when did the cause of action accrue – did it accrue on the date as suggested by the Petitioner or on the date as suggested by the Respondent or was it continuous. The arbitrator took one view of the matter. It is a possible view. Merely because it is possible to hold another view, the arbitrator's view cannot be faulted under Section 34. There is no error apparent on the face of the award. Secondly, and at any rate, it is a matter of application of law. Even if one were to assume that the application was wrong, it is not open to challenge under the explanation to sub-section (2A) of Section 34.

12 The above discussion also holds good for the ground of restraint of trade under Section 27 of the Contract Act. The learned arbitrator has not disregarded the law against restraint of trade contained in Section 27 of the Act, but after construing the agreement between the parties and the nature of their transaction, applied the law to the particular fact situation before him. There is neither contravention of fundamental policy of Indian law nor patent illegality here in the sense explained above. The learned arbitrator essentially has proceeded on the footing that the non-solicitation clauses contained under sub-clauses (b), (c) and (d) of Clause 1 of the non-compete agreement as also the restriction against disclosure of confidential information relating to the business of the company received from the company to any third party under clause 6 of the non-compete agreement, were perfectly valid stipulations which were not in restraint of trade as per Section 27 of the Contract Act. The learned arbitrator held that though other clauses of the agreement might be in breach of the

mandate of Section 27, these clauses, which were perfectly valid, would by themselves sustain the consideration payable to the Respondent under the non-compete agreement and on that basis, awarded the claim. This is certainly a possible view, and not an impossible view or a view which no reasonable or judicially minded person could have arrived at or a view as would shock the conscience of the court.

13 In the premises, there is no merit in the challenge to the impugned award. The arbitration petition is accordingly dismissed.

14 In view of the dismissal of the arbitration petition, the Notice of Motion does not survive and the same is also dismissed.

(S.C. GUPTE, J.)