

RASHID RAZA v. SADAF AKHTAR

COURT: The Supreme Court of India

CITATION: (2019) 8 SCC 710

CIVIL APPEAL NO.: 7005 OF 2019 [Arising out of SLP (C) NO. 4016 OF 2019]

DECIDED ON: 04th September 2019

BENCH: HON'BLE JUSTICE ROHINTON FALI NARIMAN

HON'BLE JUSTICE R. SUBHASH REDDY

HON'BLE JUSTICE SURYA KANT

LAW APPLIED: Section 8 of Arbitration and Conciliation Act, 1996,

Section 11 of Arbitration and Conciliation Act, 1996,

Section 11(6A) of Arbitration and Conciliation Act, 1996

INTRODUCTION:

This case arises out of a partnership dispute between the appellant and the respondent. Here an FIR was lodged by one of the partners alleging that there was siphoning of funds and other business improprieties were committed, which constituted fraud. When this case forwarded to the High Court for the appointment of an arbitrator under section 11 of the 1996 Act, it witnessed that there are complicated allegations of fraud. Therefore, The High Court dismissed the application by the appellant for the appointment of an arbitrator.

FACTS OF THE CASE:

This case arose out a partnership dispute between partners, where an FIR was lodged by the Respondent alleging the siphoning of funds and various other business improprieties by the Appellant. On the other hand, the appellant (Sadaf Akhtar) filed an arbitration petition before the High Court of Jharkhand at Ranchi, under section 11 of the Arbitration and Conciliation

Act, 1996, seeking the appointment of an Arbitrator under the Arbitration Clause forming part of the partnership deed between the partners.

Before the Ld. High Court, Rashid Raza argued that the matter pertains to a serious case of fraud that will not fit to be decided in Arbitration. The respondent argued that the appellant had utilized the assets of the partnership firm i.e. S. R. Coating, in another firm run by the appellant's father and created proprietorship firm with the same name i.e. S. R. Coating and introduced it to one of the firm's existing business partners and opened a new bank account based on a fake agreement and transferred the money into the Appellant's bank account and his father's bank account

Without commenting anything on the merits of this dispute, and relying on the principles laid down by the Supreme Court in the judgement of A. Ayyasamy case, the Jharkhand High Court held that this dispute of partnership included serious allegations of fraud/ forgery/ fabrication of a complicated nature and this cannot fit to be decided in the Arbitration proceedings. The High Court of Jharkhand further held that this dispute may require voluminous evidence to be presented by both the parties and for finding out such voluminous evidence can only be properly adjudicated by a Court. For this reason, the Court dismissed the application of the appellant for the appointment of an Arbitrator.

The High Court of Jharkhand, by the impugned order on 6th December 2018, cited the judgement of the A. Ayyasamy case, wherein, the difference between the serious allegations of forgery and simple allegations were laid down. Both the parties of the dispute relied on the Para no. 26 of the supra order passed by the High Court. Para 26 of the order stated that "the nature of the dispute involving serious allegations of fraud of complicated nature is not to be decided in an arbitration proceeding. The dispute may require voluminous evidence on part of both the parties to come to a finding which can be only properly undertaken by a Civil Court of competent jurisdiction."

Ruling by the High Court-The High Court of Jharkhand while dismissing this application under sec 11 of the said Act gave the judgement that, the facts of this case are much more complex on the merits of the allegations lest it may prejudice the case of the parties in an appropriate proceeding before the competent court. However, in totality, the High Court of Jharkhand believed that the nature of this instant dispute involves serious allegations of forgery as well as fraud, which are not of simple nature rather of complicated nature and

those cannot be decided in an arbitration proceeding because it requires voluminous evidence from both the parties.

That's why aggrieved by the High Court's ruling, Sadaf Akhtar approached the Supreme Court by way of a special leave petition.

ISSUES RAISED:

Building upon the above holding of Ayyasamy, the Court in Rashid Raza laid down a two-step test to determine complex fraud:

1. Does this plea encroach the entire contract and above all, the agreement of arbitration, rendering it void or
2. Whether the allegations of fraud touch upon the internal affairs of the parties do not imply the public domain?

Answers to the issues -

Applying the above two tests two things were very clear. Firstly, it is clear that this is a case of fraud falls on the side of the simple allegation as there is no allegation of forgery which would vitiate the whole partnership deed. Or we can say that, in particular, the arbitration clause was concerned in the said deed. And secondly, all the allegations made here, have been relied upon by the counsel appearing on the behalf of the respondent, belong to all the affairs of the partnership and the siphoning of funds from the partnership firm. So this was not a matter which would fall under the public domain. Therefore, The Apex Court overruled the decision of the High Court of Jharkhand as both the inquiries of the test were failed, and at the same point, it is important to note that this ruling applies only to India-seated arbitrations. As far as foreign-seated arbitral tribunals are concerned, they would be governed by the World Sport case and would be competent to decide on arbitrability of any type of fraud.

After studying the case the judges of the Supreme Court viewed that this dispute raised between both the parties is arbitral and so they proceeded to appoint an arbitrator under section 11 of the said Act to resolve the disputes between the parties.

RULE APPLIED:

The Apex Court analyzed the law laid down on arbitrability of forgery within the case of A. Ayyasamy v. A. Paramasivam¹. In that case, the Apex Court held that a simple allegation of fraud cannot be a ground to nullify to the effect of any Arbitration agreement. So, when the complex and heavy allegations of fraud are involved, the Supreme Court held that any court can dismiss an application referring to a dispute referring to Arbitration under sec 8 of the said Act. And therefore the fixed some criteria which can connote the serious allegations of fraud of forger; those are-

- All the allegations which may make a virtual case of a criminal offense
- All the intense allegations of forgery of documents in support of the plea of fraud
- The allegations of fraud is so complicated, which becomes essential that such complex issues can only be decided by the Civil Courts on the appreciation of voluminous evidence which requires to be produced
- Where the fraud is alleged against the arbitration provision including the agreement to arbitrate, meaning thereby in those cases where fraud goes to the validity of the contract itself of the entire contract which contains the arbitration clause².

In that case, the Apex Court had further held that in the scenario where there were simply allegations of forgery, which only touching upon the internal affairs and did not have any implication in the public domain at large, the arbitration clause thus needs to be avoided, so both the parties can be relegated to the arbitration. And applying all the principles from the said case to this case the Supreme Court held that there must be a distinction between “serious allegations” of forgery supporting the plea of fraud and “simple allegations” to check arbitrability.

ANALYSIS OF JUDGEMENT:

Based on the examination of the principles laid down in Ayyasamy case and also the twin tests done in this case, anyone could argue that the Apex Court has potentially narrowed down the ambit to assert the serious allegations of forgery when courts are approached with an application for appointment of an arbitrator under Section 11 of the said Act.

¹ (2006) 10 SCC 386

² A. Ayyasamy v. A. Paramasivam, (2006) 10 SCC 386 at Paragraph 25

However, it's to be noted that Ayyasamy case involved an application under Section 8 of the said Act where Section 8 provides a wider ambit to the Court to judge the allegations of fraud for the aim of referring the matter or denying the imputation of arbitration. But in opposite to the sec 8, in any application under Section 11 of the said Act, all the courts have a narrow purview to look at merely the existence of an Arbitration Agreement while appointing an arbitrator. Hence, it's arguable whether the working tests suggested by Ayyasamy to work out the arbitrability of the allegation in-depth propel courts to move beyond merely examining the existence of an Arbitration Agreement and conduct an inquiry upon the seriousness or simplicity of the allegations of forgery or fraud.

Anyone could suggest that the Apex Court has assessed the existence of the arbitration agreement and laid out the primary working test i.e. whether the existence of the arbitration agreement itself has not been perverse by the allegation of fraud. However, the second working test relies on the effect of fraud either between the parties or within the public at large. A blanket application of the test to the commercial disputes would always entail a control inter se between the parties. However, since fraud by its very nature is both a civil action and a criminal offence, this enquiry would be a matter of fact in each case.

In any event, the Supreme Court's ruling does set a positive precedent ensuring cautioned and minimum interference by courts within the matters involving arbitration and allegations of fraud. It also settles faith within the arbitral tribunal to work out these allegations to fulfillment.

CONCLUSION:

The decision within the case of Rashid Raza is a welcome one. This case removes the haziness over how courts should approach disputes involving allegations of fraud because it lays down a less complicated test to check whether a dispute loses arbitrability on accounts serious allegations of fraud or complex fraud. The court in this case also held that judicial interference into the determination of complex fraud must be made after strict scrutiny and should not be made an instrument for unholy parties trying to twist out of the arbitration agreement by using false allegations. This decision not only strengthens the holding of Ayyasamy but also would result in the lesser judicial intervention into arbitral proceedings. While the judicial approach to arbitrability is appreciable, the creation of a non-exhaustive

list of non-arbitrable matters might be beneficial for the judiciary and an arbitration-friendly regime.

Rashid Raza upheld Paragraph 25 of the Ayyasamy judgment which expressly states as an extra qualification that the intense and serious allegations of fraud must also cause a virtual criminal offense. The necessity to qualify for a virtual criminal offense marks a difference in cases that involves complicated commercial misdoings. The Apex Court of India adopted a pragmatic and efficient view in this case of Rashid Raza to ensure that the main objective and purpose of the act should not get defeated. The tests which are laid down in the Para 25 of the A. Ayyasamy's case were upheld which also clarifies the law upon the subject that Court should overlook Arbitration Agreement only if there were complex and serious allegations of fraud which complex allegations can only be adjudicated by the civil court and those allegations are of such nature that it will cover the whole contract including the provisions of the Arbitration clause as well.



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